Reasons of 2008 global economic crisis, measures taken and recommendations for Turkey

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HIGHLIGHTS:
1. This study attempts to identify nature and causes of global economic crisis.
2. The macroeconomic perspective of the crisis in the context of globalization has been scrutinized.
3. The effect of global economic crisis and its reflections on Turkish economy has also been studied.
4. Examines the measures taken against global economic crisis.

ABSTRACT

Starting in the USA housing sector in June 2007 and acquiring global dimension in September 2008, many macroeconomic factors played influential roles in the formation of the recent global economic crisis. Spreading from the USA to other developed economies at first and to developing economies afterward, the crisis gradually acquired a real dimension. Though as a consequence of the measures taken, there have been some signs of recovery in the global economy since the second half of 2009; it is thought that there are still some significant risks in the process of permanent recovery process. This study an examination of the policies applied and the result achieved has been done in the context of the globe in general and Turkey in specific. The scrutiny led to some policy recommendations for facing similar crisis in the future.

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1.0 Introduction

Entering into recession in the beginning of 2000, the USA economy maintained its economic growth till the end of 2006 with successive interest discounts of Federal Reserve System (FED) in order to stop stagnation. Although the economic growth carried on in Eurozone in 2006, the commodity and energy prices increased, unemployment and current deficit mounted up, expectations of growth turned into negative in the USA. Along with the increase in interest rates, the most serious problems were observed in the housing sector in which there were lots of difficulties in paying the subprime mortgage loans back, decrease in the demand and slowing down in the growth. The process starting with the uncontrolled growth in financial assets spread to Euro Zone in the global financial system and to other developing countries. Since policy makers and monetary authorities could not foresee in the first instance that the rapid increase in loans and asset prices would lead the world to a global crisis, later the effects of large-scaled bailouts remained weak. With the fluctuation started in financial markets, devaluation in developing countries’ stocks, decrease in foreign capital inflows, increase in exchange rate and disruption in the balance sheets.
of financial institutions were observed. This financial disruption caused the economic recession and shrinkage in employment, and it turned into a real economic crisis including private sector with the course of proceeding. Even the comparison of the new crisis with 1929 crisis, the greatest crisis in the world economy history that began in financial markets and spread to other sectors is significant in terms of indicating to what extent the effects of the crisis spread (Takım, 2011).

In the first part of the study, the reasons of the crisis will be analyzed, its effects on Turkey in the second part, the economic policies applied in developed countries and Turkey in third part and evaluations on the measures to be taken or carried on to be applied are given in the fourth part.

2.0 Start of crisis and its globalization

Although, as the cause of the crisis, the problems are seen to be based on “subliminal housing loans” of the USA banking sector, when the reasons of the problems studied, the reasons of the applications related to the subject intended to the solution of the problem could be understood better (Arslan, 2010). In the low-interest period, the subprime mortgage loans provided without investigation of the credit backgrounds of people caused a rapid increase in the demand for loans and interest rates; besides, this situation also caused an increase in the number of seized houses because people with low incomes had troubles in repaying their loans and a dramatic decrease in house rates (Demir et. al. 2008). This unfavorable situation spread over the system with complicated derivatives. Although the increase in home prices was one of the reasons of global financial crisis, the decrease in home prices appeared in the consequences of the crisis.

Financed by banks and financial institutions that they give notes for, rating agencies could not identify the financial problems of companies. These agencies rating on the basis of the corporation rather than the product rated the institutions issuing these products instead of securities and that led the real risk level of securities to remain hidden. Appearing less risky than it was, securities increased investor’s appetite, it added financial instruments based on mortgage loans (Zorlu and Başyigit, 2010). The bankruptcy of General Motors only after a few days of their rating announced as AAA lays bare that the reliability of credit rating agencies is a subject needed to be questioned thoroughly (Tutar; Tutar and Eren, 2011). The crisis arising with the failure of some financial companies in the USA decreases in the stock market and the USA’s various bond issues deepened in September 2007. Loss of trust in the financial sector and the pessimism of investors about the future of the sector caused a sharp decrease in share prices (Ocal, 2011). Increase in the avoidance of investors about investing decelerated the production in the real sector. As a result of international free trade and financial mobility, crisis had made its negative effects felt in the leading EU countries (Germany, England, France) since 2008. As it is stated in Table 1 below, decreases in export and production, diminutions in raw material prices, decrease in consumer confidence index and cuts in consumer expenditures were observed in other developed economies except China (Tülerli and Türkay, 2009).

The growth rates in the world economy slumped, and industrial production lowered considerably. The decrease in industrial production indexes both in developing and developed countries continued up to the first months of 2009 (Atay, 2010). As it is stated in Table 1, economic growth of developed countries (the USA, Germany, France, and England) decelerated along with global financial crisis and decreased afterward. As it could be understood from Table 1 that shows the macroeconomic indicators of some significant countries, crisis affected negatively the leading countries of EU (Germany, England, France) along with the USA. Inflation rates of these countries declined, and the unemployment rate increased because of the shrinkage shown in the below table.

<table>
<thead>
<tr>
<th>Countries</th>
<th>GDP with ruling prices (Billion $)</th>
<th>Growth rates (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
<td>2007</td>
</tr>
<tr>
<td>The USA</td>
<td>13.336</td>
<td>13.995</td>
</tr>
<tr>
<td>China</td>
<td>2.712</td>
<td>3.494</td>
</tr>
<tr>
<td>Germany</td>
<td>2.902</td>
<td>3.323</td>
</tr>
<tr>
<td>France</td>
<td>2.255</td>
<td>2.582</td>
</tr>
<tr>
<td>England</td>
<td>2.444</td>
<td>2.810</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Inflation rates (%)</th>
<th>Unemployment rates (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Countries</td>
<td>2006</td>
</tr>
<tr>
<td>the USA</td>
<td>3.2</td>
</tr>
<tr>
<td>China</td>
<td>1.5</td>
</tr>
<tr>
<td>Germany</td>
<td>1.6</td>
</tr>
<tr>
<td>France</td>
<td>1.7</td>
</tr>
<tr>
<td>England</td>
<td>2.3</td>
</tr>
</tbody>
</table>


3.0 Reflections of global economic crisis on Turkish economy
Turkey did not experience similar problems observed in developed countries during this period. When the financial data of the finance sector is reviewed today, it can be seen that our country have a stronger structure compared to other countries (Metinsoy, 2010) Because Turkish economy underwent a structural transformation and it learned to live with the crisis during the banking system crisis in Turkey in 2001, it was observed that Turkish economy had escaped from the current global crisis with almost "little or no harm" (Darci et al. 2010). Because of the global crisis, falling energy prices associated with falling consumption and investment demand caused a considerable decrease of the current deficit as of the last quarter of 2008. Besides, the financial structure of the current deficit is undergoing a change with the effect of the crisis in Table 2 (Akbulut, 2010).

As a result of a decrease in foreign and domestic demands and shrinkage in foreign trade volume, the current deficit went back from 41.9 billion dollars in 2008 to 13.9 billion dollars in 2009. As can be seen in Table 3, outstanding external debt increased in general in 2006-2010 period, although it decreased in 2009 with the effect of the crisis. As Short Term Foreign Debts were 53.1 billion dollars in 2008, it scaled down to 49.7 billion dollars in 2009, and it rose up to 78.1 billion dollars by increasing severely in 2010. Similar facts could be seen in the other indicators as well. It could be observed that the run of outstanding external debt was not affected too much.

As stated in Table 4, the ratio of considerable external debt to GDP was 37.8% in 2008; however, it rose up to 43.5% in 2009 and turned into its normal progress.

Table 5 below shows the effect of the crisis on GDP and industrial production, according to the table, GDP decreased 4.8% in real terms and lowered to 616,703 dollars. The increase from 950,534 to 952,559 in TL in the same year arose from the rise in exchange rate of the dollar. One of the significant real indicators of the crisis, industrial production index contracted 9.9%, activity ratio of the industry realized 65.2% with 11.5 point decrease in 2009.
As it can be seen in Table 6, although there was an increase in the number of employees in the period of 2005-2010, the unemployment rate showed an increase of 14% by reaching the highest level in 2009. It can be said that the main reason of this was that the increase in the number of the labor force was faster than the increase in the number of new job opportunities.

In Table 7, after the productivity per employee and per working hour in the industrial sector bottomed out in 2008 and 2009, it reached 8.2% and 8.3% by leaping forward in 2010 subsequently.

This data shows that 2009 was the year in which Turkey was mostly affected from the crisis, and it entered the recovery period in 2010.

### 4.0 Measures taken against global economic crisis

#### 4.0.1 In the world

In the struggle with the crisis, many countries, notably the USA, applied expansionary fiscal and financial policies and put serious financial aid packages into effect. The ratio of the increasing financial aid to GDP in 2009 is given in the table below.

<table>
<thead>
<tr>
<th>Year</th>
<th>Per employee</th>
<th>Per working hour</th>
<th>Per employee</th>
<th>Per working hour</th>
</tr>
</thead>
<tbody>
<tr>
<td>2005</td>
<td>100.0</td>
<td>100.0</td>
<td>4.4</td>
<td>5.0</td>
</tr>
<tr>
<td>2006</td>
<td>104.4</td>
<td>105.0</td>
<td>3.1</td>
<td>2.4</td>
</tr>
<tr>
<td>2007</td>
<td>107.6</td>
<td>107.5</td>
<td>-0.3</td>
<td>0.3</td>
</tr>
<tr>
<td>2008</td>
<td>107.3</td>
<td>107.8</td>
<td>-0.4</td>
<td>1.1</td>
</tr>
<tr>
<td>2009</td>
<td>106.9</td>
<td>109.0</td>
<td>8.2</td>
<td>8.3</td>
</tr>
<tr>
<td>2010</td>
<td>115.7</td>
<td>118.0</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>


(1) It involves aids for the financial sector.
(2) Based on the financial year, these are the estimations based on the budget of 2009/2010.
(3) Involving aids for the financial sector, it also involves the subsidiaries provided for public financial institutions and
Applied expansionary fiscal policies show that it could be a political tool removing the risk of devaluation by increasing the supply of money. Accordingly, Central Banks in developed countries increased the supply of money consistently by using different instruments apart from traditional monetary policy instruments and provided consistency in credit markets (İncekara, 2010). Within the framework of expansionary fiscal policies, tax rates were lowered down; however, priority was given to providing a balanced budget by applying tight spending policies.

In order not to exclude the private investments, support packages were prepared for expenditures to be made for companies, consumers and infrastructure investments (Akdoğan Gedik, 2010). In G-20 Leaders Summit, member countries made a commitment about the implementation of expansionary fiscal policy in the amount of 5 trillion dollars till the end of 2010. Within the scope of financial aid packages, tax reductions for companies and supports especially for export sectors and SMEs put into effect. In order to keep the consumption demand alive, the applications such as consumer tax reductions supports through social security programs and resource transfer to the poor who have high consumption tendencies were put into practice. Similarly, the share of the infrastructure investments in the budget was increased to boost the domestic demand; the infrastructure investments, which were planned to be implemented in the future, were drawn to an earlier date. Despite the risk that it could cause to the growth of financial packages’ budget deficits and impairment of financial discipline, these precautions were seen as compulsory to overcome the crisis. Along with rebuilding the trust to markets and rectification of demand conditions, it was expected the financial discipline to be reformed (Birdal, 2009). Upon the criticisms about the countries’ taking measures against the crisis uncoordinatedly, an agreement was made to sustain the developed precautions to re-accomplish global growth on the dates of 14th and 15th November 2008 in the G-20 Summit in Washington. In this context, on 1st and 2nd April 2009, in the summit performed in London, a consensus was reached to meet the global liquidity need by means of the implementation of expansionary fiscal policies, enhancement of financial resources of the international institutions like IMF and the World Bank and expansionary monetary policies of central banks (Akbulut, 2010).

4.02 In Turkey

With intent to lessen the effects of the financial crisis, a range of measures similar to those of developed countries were taken in Turkey. These are: liquidity supports, tax supports, employment supports, credit and guarantee agreements provided for producers and exporters.

-CBT (Central Bank of Turkey) put into practice a range of applications stated in the table below in order to reassure the foreign exchange and effective markets.

<table>
<thead>
<tr>
<th>Validity Date of the decision</th>
<th>Explanation</th>
</tr>
</thead>
<tbody>
<tr>
<td>09.10.2008</td>
<td>CBT restarted their brokerage operations in foreign exchange stock market of itself with intent to increase foreign currency liquidity.</td>
</tr>
<tr>
<td>16.10.2008</td>
<td>In order to keep the liquidity pulled out of the market permanently with foreign exchange purchase tenders, the exchange tenders of CBT were suspended.</td>
</tr>
<tr>
<td>14.10.2008 / 24.10.2008</td>
<td>The transaction limits of banks in foreign exchange and effective markets scaled up from totally 5.4 billion dollars at first and later to 10.8 billion dollars.</td>
</tr>
<tr>
<td>24.10.2008</td>
<td>With foreign exchange sale tenders, CBT would provide up to 50 million dollar foreign currency liquidity to the markets in a day.</td>
</tr>
<tr>
<td>21.11.2008</td>
<td>Within the borrowing limit, term of foreign exchange stocks that banks could get from CBT raised from 1 week to 1 month; 10% borrowing rate of interest in this market is lowered to 7% for dollar, 9% for the euro.</td>
</tr>
<tr>
<td>05.12.2008</td>
<td>Required reserve ratio for foreign currency reduced from 11% to 9%; thus about 2.5 billion dollars liquidity is provided for the banking system. Interest rate payment for required reserve ratio for foreign exchange is stopped to encourage counter-dollarization. The interest rate paid for TL required reserve rationalized up from 75% to 80% of CBT overnight borrowing rate.</td>
</tr>
<tr>
<td>05.12.2008</td>
<td>Export discounting credit limit scaled up from 500 million dollars to 1 billion dollars, and this raised the credits’ ease of use.</td>
</tr>
<tr>
<td>Ocak 2009</td>
<td>The half of the interest rates of the credits to be used by Tradesmen and Artisans Indemnity Cooperatives began to be funded by the government, 15.6% interest rate (including commission etc.) was lowered down to 12%.</td>
</tr>
<tr>
<td>22.01.2009</td>
<td>As of January 28, 2009, the registers in CBT were to be erased after the total debt was paid in the event that checks and protested bills and the debts regarding credits and credit cards were paid or readjusted within six months.</td>
</tr>
</tbody>
</table>
| 20.02.2009                    | The term of exchange stores that the banks could get from CBT was extended from one month to three months, lending rate in CBT straddles was lowered for dollar from 7% to 5.5% and for the euro from 9%
These measures were all for the prevention of liquidity shortage to be experienced in the market.

- With the aim of revitalizing domestic demand by providing tax and bonus supports to customers and companies and promoting the production by lowering production cost, the tax debts were split into installments in October 2008 (Secretariat of Treasury, 2009), the tax rates applied to earnings from stock trading was reset in November 2008, reductions, amnesties and penalty reductions of consumer and company taxes were applied in various dates from 2008 to 2010.
- Production and export oriented loan and guarantee supports were provided (TİSK, 2009). Zero or low interest loans were given to SMEs, the leading power of the national economy; resources allocated for these loans were increased, access to the loans was made easier. The context and limits of loans provided for export were extended, their dating forwarded, treasury guarantee enhanced. The paid-up capital of Eximbank was increased by 50%. The period of agricultural and investment loans was extended. The use of foreign currency loans was rearranged. The opportunity to restructure the unpaid credit card debts was enabled.
- In order to prevent an increase in the unemployment rate, in accordance with the crisis and the population participating to the labor force, support programs were prepared (Sönmez, 2010 and Akdoğan Gedik, 2010). Unemployment and short-time working allowances were enhanced. Source transferred to work programs constituted for public workfare program (TYCP) was increased. The education activity of Turkish Employment Agency (İŞKUR) was expanded, and the attendance to these activities was supported. With the corporation of İSKUR and Small and Medium Enterprises Development Organization (KOSGEB), intensive entrepreneurship and education counseling services were provided. Bonus support for additional employment was given to workplaces; employer’s premium over minimum wage was decided to be paid by the state for six months. Employment incentives for young and woman were applied. The review of vocational education and an increase in activities after these educations were extended. Studies on active labor force were carried out.

5.0 Measures to be taken against global economic crisis

1. The increase of investments, production and productivity, should be encouraged. Investments especially in industry sector should be encouraged with short and long term measures parallel with the export and employment policies. The main purpose should be the development basing on export and the increase of the economy’s competitiveness. Using the labor most productively will make the production productive as well (Karakayali et al. 2010).

2. Population growth rate is rapidly falling down. Without a doubt, the decrease in population growth rate and its effect on employment will be seen in very long term. However, realizing an optimum population growth for the economic and social development of the country has great importance for different directions. For this purpose, it is necessary to extend family planning and birth control methods and raise awareness of rural people with public arrangements accordingly.

3. Educational and technological developments should be given importance. The most significant factor in the change of scientific and technological structure is the existence of competition in the field and changing and various demands for products. The most significant factor of competition is technology rather than the prices of the products.

4. Problems related to unrecorded economy should be resolved. Unrecorded part is increasing after 1980 in Turkey scales up the rate of the employment of low-income and deprived workers, and it hinders the creation of new employment areas. Therefore, it is compulsory to avoid this unhealthy employment style preventing the development of modern industrial working and enable to increase employment opportunities in recorded part. (Karakayali et al. 2010).

5. Injustice in tax rates is to be cleared up. According to common opinion, which is if the share of indirect taxes in total tax revenues in the country is higher than direct taxes, justice of taxation cannot be mentioned in that country, justice of taxation in Turkey is decreasing every passing year. As long as the share of indirect taxes in total tax revenues is increased on paper, black economy will grow up, tax assessments and collection will be deteriorated (Karakayali et al. 2010).

6. Regarding the estimates of the decrease in economic growth, World Central Bank should be directive about adopting a common currency, interest and exchange policies in a global world and make an effort about price stability. Also, the transparency structure in credit facilities of banks and financial institutions should be sighted, there should be a guide for underdeveloped countries that are mostly affected by the crisis, these subjects should be supported by countries; advices and rules taken should be obeyed. (Vidinoğlu and Kaya, 2010).

7. It is better to make income transfer for poor and middle income earners about spending in order to increase public expenditures since it is impossible to expect a boom in production without demand growth.
Global economic crisis will be overcome like other former ones and economic recovery will start again. However, whether the crisis has reached the bottom is not clear now. With intent to overcome this crisis and not to face severe crisis in the following terms, It should be considered that more careful risk management should be carried out in extensions, rating agencies should do more objective scoring; specific standards related to capital requirements should be set, risk management regarding liquidity, interests, and exchange rates should be followed meticulously; governments should keep company with central banks, measures taken should be applied synchronously and World Central Bank should be found as the chief regulatory body in order to control all of these precautions. (Vidinoğlu and Kaya, 2010).

1. It is required that measures taken in Turkey against the global crisis to provide recovery after crisis, they should also realize structural transformation. The losses of production during the latest crisis are observed to cause a decrease of employment. It is necessary to make the production speed-up by booming the domestic demand to increase employment. Credit supports for SMEs and encouragement of the banks for credit should be among the first and foremost policies to be implemented. Besides, programs aimed at gearing up human capital should be supported. (Konur and Çakıcı, 2010).

2. World monetary system should be rearranged. In this system, a money basket should be created by enabling some strong currencies beside dollar in international payments. (Yıldırım, 2010).

3. A new regulation should be made in the financial market especial derivatives.

4. Central Bank should help banks for their payments of foreign borrowings. Recent high real interest rates should be decreased. (Yıldırım, 2010).

5. Banks should continue to give support to workplaces especially SMEs during the period of crisis.

6. Controlled exchange rate should be applied.

7. Economic growth must be carried out with a model based on production (Yıldırım, 2010).

8. In order to decrease current accounts deficit and unemployment, a significant part of the production of intermediate goods and capital goods should be made within the country. Also, a restriction for the most part of imports should be imposed. (Yıldırım, 2010).

9. Turkish economy should be made self-sufficient in the production of energy and agriculture with new projects based on the source of the country.

10. Turkey should produce advanced technology. For the production of technology, 2-3% source should be allocated from GDP instead of 0.70% because the number of developed countries without making any production is quite rare among the worlds countries. (Yıldırım, 2010).

11. The demand for our export products from EU countries decreased. The way of export should be changed to our neighbor countries especially Russia and Central Asian Turkish Republics apart from EU. (Yıldırım, 2010).

6.0 Conclusion

As of the third quarter of 2008, a global crisis took its effect in the way that the rapid decrease of export, increase in the unemployment rate and a decrease in consumer confidence index and fall of consumption expenses in the world economy. Germany, England and USA come first in the mostly affected countries from the global financial crisis. China and Turkey were affected comparatively less from the crisis. Turkey, it strengthens its banking system after taking lessons from 2000-2001 crisis, and it almost did not experience such serious problems like developed countries did. Monetary and fiscal policies play a crucial role within austerity packages for crisis. USA being in the first place many countries experiencing a crisis deeply preferred to struggle with the crisis by implementing expansionary fiscal policies. In the mostly affected countries from the crisis, financial supports that were provided by their countries to various sectors should be carried on until the total recovery. There are some measures that should be internationally taken due to the global crisis. About Turkish economy demand increasing measures should be implemented; banks should not cut credits to companies but give them controllably. In addition, strategic production, energy and agricultural production should be increased, and advanced technology must be supplied. Central Bank should lower the loan interest rates. The tourism potential of Turkey, cradle of civilization and surrounded on three sides by the sea should be resurrected. Besides, a strategic production, energy generation and agriculture production should be increased; high-technology must be provided, and the export of high-value-added products should be given weight to.

References


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