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An Assessment of 2023 Recession and Potential Economic Performance of Turkey

2023 Resesyonu ve Türkiye'nin Potansiyel Ekonomik Performansı Üzerine Bir Değerlendirme

Özlen Hiç [a, *] & Ozan Kireççi [b]

[a] Prof.Dr., İstanbul Üniversitesi, İBF, İktisat Bölümü, 34452, İstanbul/Türkiye
ORCID: 0000-0002-2308-3393
[b] Bağımsız Araştırmacı, İstanbul Üniversitesi, İBF, İktisat Bölümü, 34452, İstanbul/Türkiye
ORCID: 0009-0005-1251-5671

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ÖZ

Bu araştırma ekonomi konjönktürü genelince tartışılan "2023 Resesyonu" olgusunu gerekçeli sebepler ile açıklamaktadır. Covid-19 Pandemisi ve 2008 Büyük Resesyonu olaylarını yaşayan dünya ekonomisinin gerçekleştirmiş olduğu "Parasal ve Mali Genişleme" refleksi veriler ile gün yüzüne çıkarılmaktadır. Bu gündemlere ek olarak yakın zamanda meydana gelen "Rusya-Ukrayna" savaşının tartışılagelen "Resesyon" olgusu üzerinde yarattığı etkiler veriler ile ele alınmıştır. "Genişleyen Kamu Harcamaları ve Para Arzı", "Enerji ve Hammadde Fiyatlarındaki Artış" gündemleri üzerinden oluşturulan makalenin son kısmını gelişmekte olan bir ekonomi olarak "Türkiye" oluşturmaktadır. Türkiye'nin özgün bir gelişmekte olan ekonomi olması ve Ukrayna-Rusya savaşında kritik bir rol üstlenmesi sebebiyle "Türkiye'nin Olası Pozisyonu" üzerine bir takım senaryolar oluşturulacaktır. Bu senaryolar sadece ekonomik verilerden yapılan çıkarımları (tahminleri) kapsayacaktır.

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ABSTRACT

This research explains the phenomenon of "2023 Recession",with justified reasons. The "Monetary and Fiscal Expansion" reflex of the world economy, which experienced the Covid-19 Pandemic and the 2008 Great Recession, is brought to light with data. In addition, the impact of the recent "Ukranian War" on the discussed "Recession" phenomenon with data. "Expanding Public Expenditures and Money Supply", " Increasing Energy and Commodity Prices " are the topics of the article, and the last part of the article is devoted to "Turkey" as an emerging economy. Since Turkey plays a critical role in the Ukraine-Russia war, a number of scenarios will be created on "Turkey's Possible Position". These scenarios will only include inferences (forecasts) made from economic data.

1. Introduction

In this study, explanations will be made in general terms about the reasons why 2023 will be a year of "Recession" in the economic conjuncture. After the "2008 Great Recession" crisis, the phenomenon of "Expansionary Monetary Policy" followed by central banks, especially the FED, in order to overcome the recession, started to give various "Inflationary" signals in the world economic conjuncture since 2018. Between 2008 and 2015, there was a huge expansion in the money supply because of the "Expansionary Monetary Policy" and the consensus

* *Sorumlu yazar/Corresponding author*.
e-posta: *ozlen.birol@istanbul.edu.tr*

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accepted a financial system that revolved with "Liquidity Abundance". The "Expansionary Monetary Policy", which was used to relieve the financial system, which was left with liquidity shortages due to the "2008 Great Recession" crisis, and to get the wheels turning again, was gradually replaced by the "Tightening Monetary Policy" starting from December 2015 with the FED's interest rate hikes. In this interim period, although the ease of financing at low interest rates whetted investors' appetite for risk, the system was not able to incorporate enough new economic actors to carry its weight, so the abundance of liquidity followed a breakthrough in the direction of creating inflation. We will analyze the phenomenon of "Global Recession", which came to the agenda again after the recession that was felt and experienced between 2008 and 2010, under three headings.

In the first section, we will introduce the topic of "Expanding Public Expenditures and Money Supply" and explain the adventure that started in 2008 as mentioned above. We will take a closer look at the effects of the "Tightening Monetary Policy", which had to be suspended with the Covid-19 period, and the feedback received against it. We will take a closer look at how the process, which progressed in the field of Central Banks and Monetary Policy before Covid-19, moved to Public Expenditures and Fiscal Policy with the "Pandemic", and how governments increased public expenditures during the pandemic with the understanding of "Social State". We will interpret the process within the framework of the world economy. In this process, we will use data such as Budget Deficit; Government Debt, Money Supply and Policy Rate to provide a basis for what we say.

In the second topic, "Increasing Energy and Commodity Prices", we will touch upon the ongoing "Russia-Ukraine" war and observe how energy and raw material prices deepen the "recession" phenomenon, how governments' attitudes towards this war and the economic conjuncture, their energy policies and how they maintain the "Usual Normal" with market indifference. We will make predictions on the effects of the possible war situation on energy and raw material prices and how these situations will affect the economic conjuncture. In this section, we will support our views by using data on energy and commodity prices and their effects on inflation.

At the last section, " Turkey's Potential Position in Light of the Facts ", we will analyze Turkey's active role in this process and make a general assessment of the situation. A general conclusion will be made by examining Turkey's possible attitude and reflexes with Good-Base-Bad scenarios.

2. Topics and Analyses

2.1. Why Policymakers Argue the “2023 Recession” ?

At the beginning of the Great Recession in 2008, the world economy changed and reached a fresh era. The international economy underwent a change in trend in 2008 because of the collapse in the American real estate markets, and replaced the Neo-Classical economics approach with a Post-Keynesian approach. In an attempt to halt "Aggregate Demand," which was shaken the most following the crisis, governments resorted to the implementation of fiscal stimulus. The reason behind this was that fiscal stimulus was seen as a double return, improving both short-term demand and long-term potential output (Padoan, 2009).

As a consequences of the 2008 Financial Crisis, central banks implemented "Expansionary Monetary Policy" in an attempt to mitigate the circumstances and boost demand. Based on what Orthodox Economics teaches us, the point of this was to encourage investment and spending in hopes of stimulating aggregate demand. As a result, the significant impact of the crisis, "Inadequate Aggregate Demand," were stimulated by governments and central banks. So, both the monetary and fiscal policies moved towards the identical objective. According to Figure 1, this led to an enormous expansion of the money supply and an unprecedented twin "Expansionary" economic policy. Under such circumstances, the Great Recession of 2008 forced economists to reconsider many of the policies they thought they had hammered (Alesina, 2012).

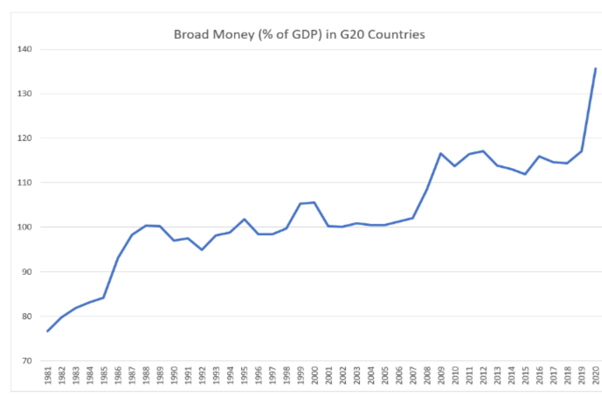


Figure 1; Broad Money in G20 Countries between 1981-2020.

Although attempts at preventing it in the period, the Covid-19 Pandemic continued this expansion which started in 2008, then by mid-2021, the FED balance sheet had expanded to up to $7.7 trillion (Mulligan, 2021). In the first quarter of 2020, the Covid-19 Pandemic triggered a worldwide economic downturn and a physical shutdown of manufacturing. The Covid-19 pandemic came with a massive deficit in terms of total national income because of the disruption of global supply chains and the constraint of international mobility (Yeyati, Filippini, 2021), and governments have been pressured to assume the position of "Social State" in response to this scenario.Governments made significant expenditures on health and fighting the pandemic as a consequence of this situation, which led to a rise in Public Expenditure. As a result, unmanageable inflation was a result of an enormous money supply and government expenditure (fiscal stimulus). In consequence to these events, central banks hiked its policy rates. The cost of investment increased higher as a consequence of central banks' "Contractionary Monetary Policy," which even created the threat for a recession. Cuts and decrease in "Public Expenditures" followed these.

The world was talking a recession that was merely triggered by economic factors when they faced a long-awaited explosion. An unfortunate war started out among the governments of Kiev and Moscow, Moscow had critical resource reserves like natural gas and oil and Kiev had been a "Agricultural Giant" with its abundant agricultural areas. Because of the political effects that the war, which started around the end of February 2022, brought on top of the economic effects of previous economic policies, it has damaged investor and consumer confidence. Households' economic attitude in this situation changed because expectations deteriorated. Considering that the outcomes of the unexpected Covid-19 pandemic outbreak and the Russia-Ukraine War were not considered is when 2018 OECD projection was made (Mariotti, 2022), it would not be too unreasonable to predict that the "Real GDP Growth" rate will shrink further than the projected rate (Mariotti, 2022).

Another facet of the already concerning "Recession" risk was sparked by the war. A second cost has been experienced by producers as they attempt to absorb the cost of inflation brought on by the broken supply chain and rising energy and raw material prices. In addition to their currency losing value, they are also paying more for the production factors they need for a number of different causes. The prevailing situation with the world's economy, which is already fragile, forces us to go through an extremely tough and deal with the "Recession" phenomena once more after a long break. Due to these factors, we will 's intent on two issues: "*Expanding Public Expenditures and Money Supply*" and "*Increasing Energy and Raw Material Prices*"

2.2. "Expanding Public Expenditures and Money Supply"

The Great Recession of 2008 continues to be the most significant economic downturn until the Great Depression of 1929. The global economy had a breakthrough in external finance but failed to integrate this into real economic growth (Verick, Islam, 2010), and ultimately led to a consumption boom and then a "tragedy" became. Although the "dot.com" bubble in 2001 and Alan Greenspan's "Expansionary Monetary Policy" during his tenure as Fed Chairman seem to be the beginning of the story, the truth went much deeper because economic institutions did not accurately assess risk appetite and the circumstances (Verick,Islam,2010). Investors and financial institutions both contributed extensively to the crisis's evolution also while fully they are experienced it. Economic indicators were altered in the wake of the recession, and the economy experienced unprecedented instability. Locally, the crisis first damaged "Aggregate Demand," which was severely rocked to become a major factor in the economy's systemic disruption. What steps were therefore going to be taken by the government and Central Bank? Since many of the policies they believed to be proper had to be reconsidered (Alesina, 2012), how were those in economic circles going to employ the tools of policy at their disposal? Should fiscal policy or tools for monetary policy be used to handle the crisis?

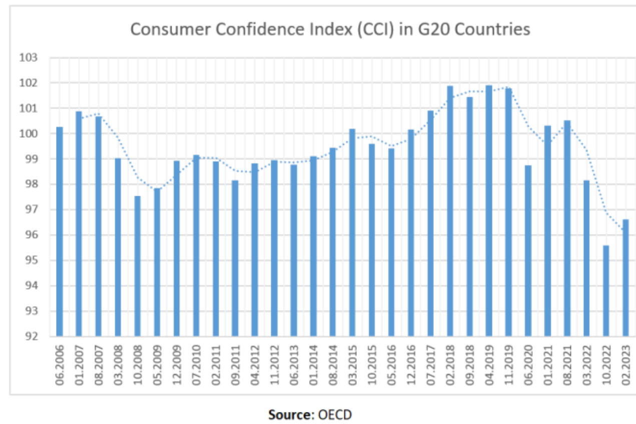


Figure 2: Consumer Confidence Index (CCI) in G20 Countries between 2006-2023.

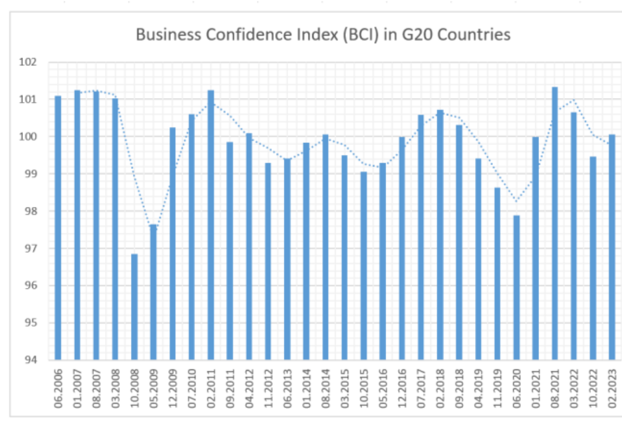
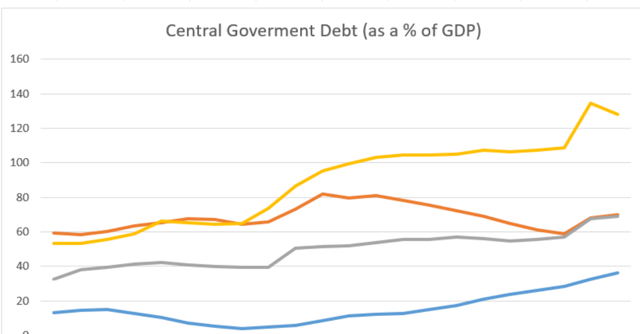


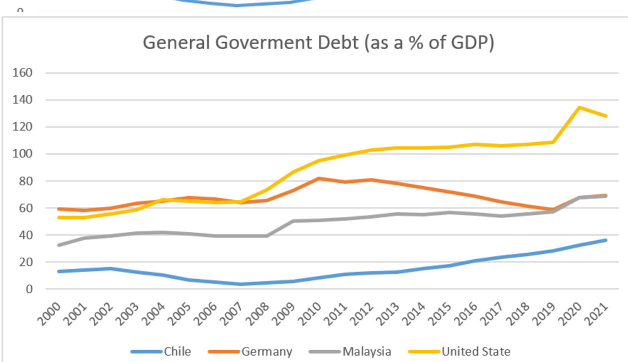
Figure 3: Business Confidence Index (BCI) in G20 Countries between 2006-2023.

Our big question has an answer: neither of the two tools, taken alone, would have had any effect, even if they had gone beyond the limits of intervention. The burden was significantly heavier than it should have been because the crisis arrived unexpectedly and was also much "deeper" than imagined. Because of this, an extraordinary "expansionary" policy was put into place, necessitating coordination between monetary and fiscal policy. The magnitude of the fiscal stimulus packages was so great that, according to See Zhang's study in 2008, they equaled 3.9% of the world's GDP in 2010. (Verick, Islam, 2010). What format should fiscal stimulus accordingly take? Taxes and spending were the available options to policymakers. Of course, lowering tax rates would boost consumption, but the anticipated result wouldn't occur until household expectations increased, uncertainties eased gradually, and private sector welfare normalized (Padoan, 2009). Along with this stretched process, there was also the additional reality of financial market debt obligations brought on by the crisis, which could only be addressed by raising household savings (Padoan, 2009). The Keynesian Model was utilized in light of these factors, and if a financial regulation was to be implemented, it should be based on "Expenditures," as it is commonly accepted that "Expenditures" are frequently less expensive than "Taxation." (Alesina,2012).

Figure 4: Central Goverment Debt in Two Developed and Two Developing Countries between 2000-2021

Figure 5: General Goverment Debt in Two Developed and Two Developing Countries btw. 2000-2021



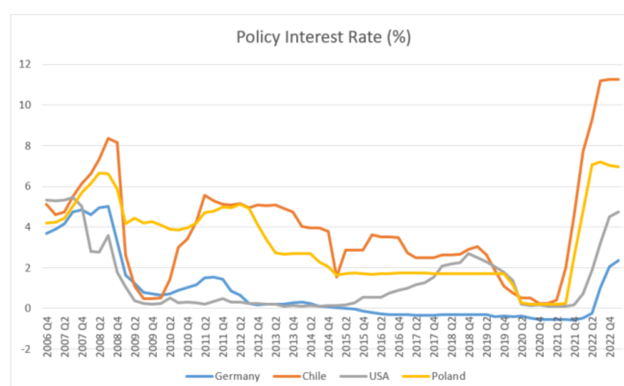


Source: IMF

Figure 4 illustrates that during the Great Recession of 2008, the amount of central government debt has increased. Tax reductions and greater government spending are to accountable for this. Following the 2008 financial crisis, there will be another increase in 2020, during the "Covid-19" pandemic. The enormous "Fiscal Stimulus" packages primarily funded social safety nets and infrastructural improvements, with other packages focusing on directly impacted and crisis-hit industries (Padoan, 2009). Despite the size of the fiscal stimulus, the indicators didn't start to demonstrate evidence of improvement until 2010 (including the final quarter of 2009), and even then, they were mainly a technical matter. In terms of the real sector, especially in terms of worker welfare, countries that started 2010 with technically positive growth (see USA, Germany, Chile, Malaysia, etc.) are however quite fragile and volatile (Verick, Islam, 2010). The biggest production gap in the real sector was reported in many OECD member countries that had positive GDP growth at the end of the decade since 1970. (Padoan, 2009).

The central banks of the crisis-affected nations experienced an unanticipated expansion during the crisis. The real sector was severely impacted by this crisis, thus monetary policy tools and fiscal policy instruments combined to follow the expansion that had already started. The FED made its first significant purchases in the US, where the crisis started, just after it. These purchases, as distinguished to an OMO transaction, were made in order to purchase mortgage bonds and restore the shattered financial system (Mulligan, 2021).Because of this expansion, the FED had to temporarily lose power over monetary policy because it was unable to sell the mortgaged assets it had accumulated (Mulligan, 2021). This was chiefly because the crisis began in the "American Mortgage Markets," which housed the mortgaged assets the FED had collected. To the greatest extent imaginable, central banks adjusted interest rates by carefully observing economic data and waiting for the appropriate time. With the FED's decision to raise interest rates in the US, the crisis' main focus, the progressive increase in interest rates that began in 2010 came to an end in 2015. The FED's assets, which totaled $4.5 trillion by the end of 2014 (qq v Figure 6), show just how much this crisis and these policies have cost. This was six times the amount that existed before the crisis (Mulligan, 2021) and the FED was in charge of a monetary expansion that it had only partially took control over.

Figure 6: Policy Interest Rate (%) Two Developed and Two Developing Countries between 2006-2023



Source: OECD

The globe had to deal with a new crisis just as preparations were being made for a soft landing (although this expansion should have had a soft landing after the crisis). The Covid-19 virus was discovered for the first time in China before spreading globally and causing a pandemic. The fact that this circumstance emerged when the impacts of the prior crises were still being felt and that it presented a risk to human life had the most impact. In the Great Recession of 2008, the global GDP decreased by 1.3%, even during this crisis, it reduced by 3.1%. Since the Great Depression, this recession has been the biggest (Yeyati, Filippini, 2021).

These particular causes can be described as follows;

i) The interruption of production

ii) Disruptions in international trade and supply chain processes

iii) A loss in global cooperation

iv) Worker health issues

v) Investors' reduced risk appetite and gloomy future prospects

Governments adopted the "Social State" role and boosted spending on security and health care in an environment where human health was obviously in danger. There was a global trend of financial stimulus since household income was at threat in a setting where output was at a standstill. The objective was to maintain the "Aggregate Demand" of financially and medically supported households and prevent the Great Recession of 2008. (Akbulaev, Mammadov, Aliyev, 2020). Financial expansion had to be continued due to the additional cost of healthcare and households receiving financial assistance. The weight of subsidies and in-kind/cash benefits has become clear, as shown in Figure 3.2.1, and the public burden on the government has increased. An example of this is the Covid-19 Aid Package prepared by the US Senate. In addition to supporting families in need, this package was created to secure the survival of small businesses and support hospitals that were pushed beyond their capacities (Das, Roy 2020).

The circumstance of the previous crises was repeated by central banks, who wished to maintain their long-term careful and conservative attitude, and they once more demonstrated the reflex of cooperating with fiscal programs. But, due to the always growing money supply and the circulating assets, the cost of this cooperation would continue to rise. As seen in Figure 3.2.3 with the Senate's Aid Package, the FED ended the process with assets worth roughly to $8 trillion (Mulligan, 2021).

The long-peroid lockdown concluded with a few exceptions, with the opening up process that began in 2021Q3. Opening up resulted in new socializing and financial practices. The world was not the same before Covid-19, just as it was not the same before the Great Recession of 2008. Companies that started up again as a result of the opening tried to compensate out the excess demand by hiring more people. This not only helped to lower unemployment but also start the flame of fashioned "Expansionary" policies. This triggered the well-known "Demand Inflation" effect (Figure 8). At this moment, Central Banks rapidly raised interest rates, having run out of time and patience for a "Soft Landing" and converted it into a "Hard Landing" (Figure 3.2.3). The cost of borrowing increased significantly as a result of these interest rate increases, and investors' appetite for risk decreased as well as their preference for "Equity" investments in the real estate market. Companies "downsized" the volume and pace of their production as a result of rising financing costs and reduced investor returns. The biggest issue, in our opinion, is that everyone did this at the same time and therefore by coincidence (!). Due to this, we now referred to a "recession" rather than a "stagflation". I hope you didn't hit the brakes when the car suddenly rushed out in front of us as we were driving slowly on the ice. The world economy, which is unprepared for all of this, is represented by the icy road. Public expenditure is symbolized by the car that suddenly pulls out in front of us, and the "we" in the driver's seat are the central banks. We will crash the wall the moment we quit practicing care and "crash" on the brakes, but what if we have to?

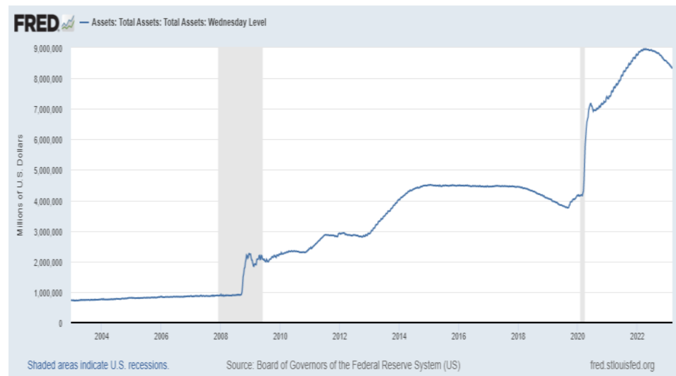


Figure 7: Total Assets Held by the FED; FRED 2023

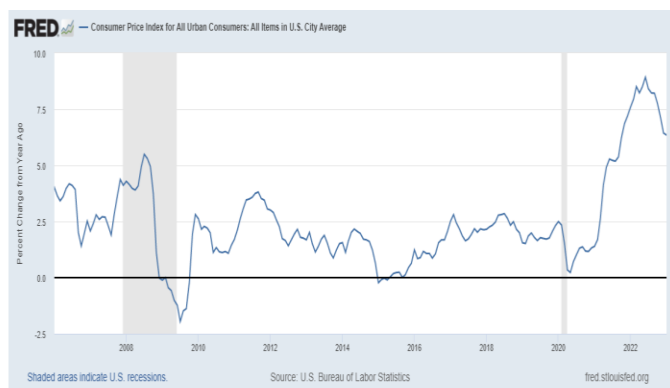


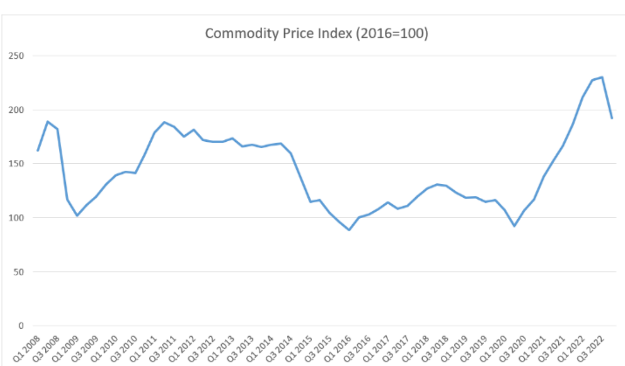
Figure 8: FRED, Consumer Price Index (CPI) in USA between 2006-2023

2.3. "Increasing Energy and Commodity Prices"

A long-standing threat came to pass in February 2022, and the Russian-Ukrainian war indemnified started. After the Russian government annexed Crimea and recognized the Donetsk-Luhansk People's Republics in 2014, Ukraine-Russian relations, which had been tense for a while on the basis of international relations, reached a breaking point. The war between the two states began on February 24 with the Russian operation in the Donbas region (Ece, 2022). So many social and economic issues in Ukraine happened as a result of the war.

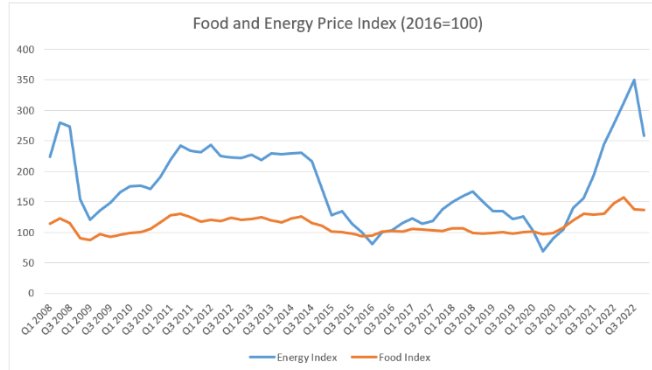
The world economy has "riveted" from the negative impacts of the 2008 "Monetary Expansion" trend, which started to recover in 2015 but restarted with the Covid-19 pandemic. The "Inflation" phenomena was the main cause of this. Since the Great Recession of 2008, price increases in developed countries have increased by 8.7% (Irtyshcheva and Friends, 2022), it is the top point for price increases. Moreover, many developed nations have lately experienced record inflation rates. Due to their involvement in international trade, Russia and Ukraine, two significant economic players, have put pressure on the global economy by raising the cost of their export goods. Energy items for Russia and grain (food) supplies for Ukraine in particular have placed tremendous pressure on the market, disturbed the supply chain, and upset the equilibrium of global prices (Arce and Friends, 2023) in global commerce.

Although the administration has selected "taxation" as a means of maintaining the income balance, the Ukrainian economy has undergone a very dramatic instability, and this has not prevented a drop in tax collections. The budget requirement for the Ukrainian government, according to the relevant ministry, is $5 billion for one month, which indicates both how severely the Ukrainian economy h as been damaged and how much it depends on international partners for development costs in the post-war period (Irtyshcheva and Friends, 2022). Also, the loss of Donbas, the center of substantial industrial investment (Iwaski 2014) , and the massive port blockades that started with the conflict have resulted in a significant decline in Ukraine's GDP (Irtyshcheva and Friends, 2022).



Source: IMF

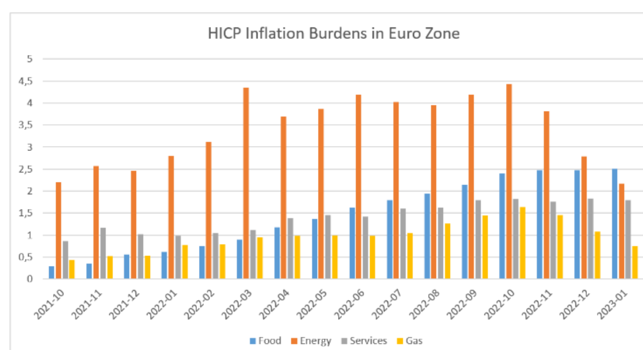
Figure 9: All Commodity Price Index includes Fuel and Non-Fuel Price Index between 2008-2022.



Source: IMF

Figure 10: Food and Energy Price Index between 2008-2022.

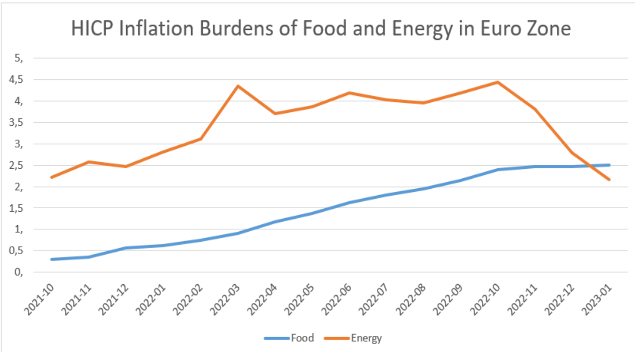
Despite a general rising trend in commodity prices since the start of the war, "Energy" and "Food" commodities have seen the most growth. Particularly, the "European Union" and the "Eurozone" region have suffered economically the most from the war. The EU nations developed strong ties and trade networks with both sides of the war in terms of geographical proximity and economic ties. Figure 11 shows how food and energy costs have a considerable impact on inflation. This is mostly because, before the war, Russia provided the majority of the Eurozone's energy imports and Ukraine was a big supplier of food and fertilizer to the Eurozone (Arce and Friends, 2023).



Source: Eurostat

Figure 11: HICP Inflation Burdens in Euro Zone between 2021/10- 2023/01.

Figure 12 shows that whereas energy items were the focus of inflationary pressures at the beginning of the war, they have recently turned their attention to food (Arce and Friends, 2023). The underlying cause of this is that food production utilizes an energy-intensive manufacturing process, and at the same time, Ukraine does not supply a necessary raw material known "fertilizer," which has caused an increase in input costs in the agricultural sector, and although gradually, as seen in the distribution of inflation (Arce and Friends, 2023). The increasing costs in various sectors and the Eurozone's reliance on energy imports, in general, have a negative effect on the region's terms of trade and threaten to cause a significant loss of real income (Arce and Friends, 2023).



Source: Eurostat

Figure 12: HICP Inflation Burdens of Food and Energy in Euro Zone between 2021/10- 2023/01.

In order to eliminate energy import dependency, the European Union has resorted to various means such as diversifying energy supply sources. With the start of the war, the main objective of the EU Energy Markets has been to diversify supply sources and ensure security of supply (Ciucci, 2022). As of May 2022, the "RepowerEU" plan was put forward to prevent dependence on Russian fossil fuels and to increase the use of sustainable energy, and measures such as energy saving and diversification of energy sources began to be implemented (Ciucci, 2022).

The "Eurozone," which contains 14% of the world economy's deposits in its accounts and includes 4 of the top 15 largest economies, was severely shaken by the war. It is one of the major players in the global economy. The "inflation" phenomena brought on by the 2008 Recession and the monetary growth that was unable to be stopped by the 2019 Covid-19 Epidemic and resulted in a loss of real income has already been worsened by this circumstance. Cost inflation took the place of the "Demand Inflation" phenomenon and deepened the overall inflation phenomenon. By suddenly raising interest rates in coordination with the FED, as shown in Figure 13, the ECB set up the conditions for a "Hard Landing," as we saw in the previous chapter. How strongly the markets sensed the recession and prepared for it can be seen in the impact of Silicon Valley Bank's bankruptcy on the US economy and the rise in Credit Suitte and Deutsche Bank CDS Premiums in the EU region over the past year.

European Union Central Bank (ECB) Interest Decisions

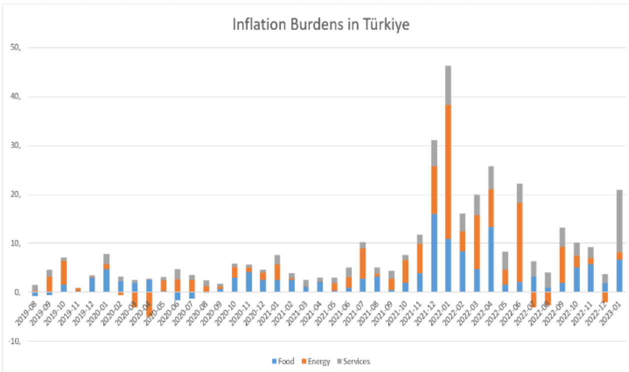
Date;	*% Change*	*Last and Actual*
July 21, 2022	0,50%	0,00 to **0,50 %**
September 08,2022	0,75%	0,50% to **1,25%**
October 27,2022	0,75%	1,25% to **2,00%**
December 15,2022	0,50%	2,00% to **2,50%**
Februrary 02,2023	0,50%	2,50% to **3,00%**
March 16, 2023	0,50%	3,00% to **3,50%**

Figure 13: ECB Policy Interest Rate Decisions between July-2022 and March-2023

When unexpected interest rate increases are contemplated, there is a real investment catastrophe because of the cost of borrowing as well as the decline in risk appetite that will happen as investors turn to safe-haven government bonds. The key topic to be covered in this discussion is the amount of real income loss brought on by the inflation that interest rate hikes avoid. The essential thing to compare at this point is that both have an adverse effect on incomes, and it is best to choose the adverse effect that is less expensive. Sharp interest rate increases to combat inflation can result in considerably more expensive bankruptcies and sectoral contractions, as seen in the recent bankruptcy of the Silicon Valley Bank (SVB). The primary cause of this is the active role played by government bonds in the financial markets as OMO (Open Market Operation) securities. Banks that concentrate their investments on these assets are placed in tough positions in terms of liquidity as a result of interest rate increases, the values of government bonds that have been auctioned and sold in the recent past falling, and. The key question at hand is whether the decline in the money supply should be abrupt or steady and gradual in reaction to inflation. Is a sharply decreasing investment and production sector significantly more expensive than a moderate and managed inflation up to a certain point? It wouldn't be incorrect to suggest that this question lies at the heart of the entire situation. Given this information, the Eurozone, one of the biggest economic players in the globe, was once again faced with a challenging scenario following 2008 and the epidemic, and it was forced to deal with the bad consequences of the war. The Eurozone is getting more and more at risk of a recession as a result of these unfortunate circumstances, especially given that it is carrying two major crises and the ensuing inflation issue on its back.

2.4. “Turkey's Potential Position in Light of the Facts”

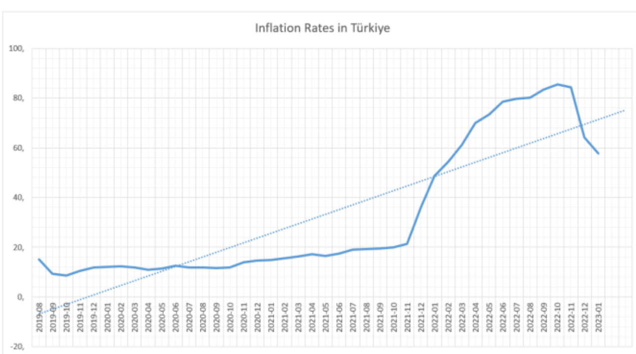
One of the most outstanding developing market nations is Turkey. The main cause of this is the lengthy period of "Economic success" it has previously experienced, in contrast to many other developing markets. The Turkish Economy has always been a "Special" economic sector both in terms of its structure and the eras it has gone through in the past. Between 2002 and 2009, the Turkish Economy enjoyed extremely high levels of wealth and managed to increase its GDP per capita from $3,608 to $12,582. When the pre-crisis macroeconomic data are evaluated, it is clear that the situation was not very "bright," as the Turkish economy had to face the crisis in an extended position in terms of its overall condition and position.Turkey, one of just two G-20 nations to have positive GDP growth at the end of 2020, joined China as the only country to do so. Turkey only experienced negative GDP growth (-9%) during the Covid-19 period in 2020Q2, but it saw positive growth in the two following quarters. It would be inaccurate to indicate that this growth was intended to increase household welfare, as this growth model was largely based on the period's low interest rate policy and the consequent credit expansion (Sertkaya, Baş 2021), which resulted in a pronounced "Inflation" phenomenon in the years that followed.



Source: EVDS

Figure 14: Inflation Burdens in Turkey between 2019/08-2023/01.

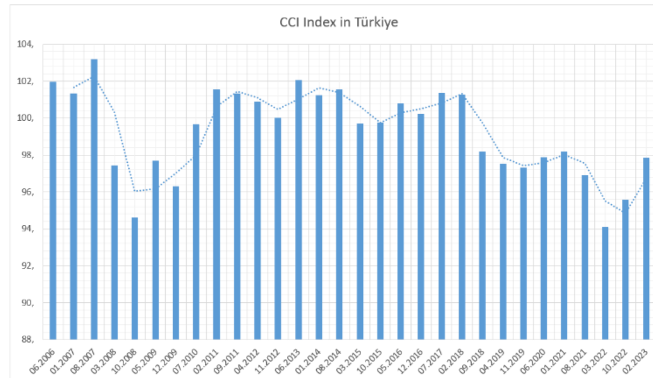
As many other nations, Turkey attempted to tolerate the bad consequences of the virus during the Covid-19 era by made multiple rescue and support programs. The primary goal of the tax benefits was to delay payments such as tax debts, which are a barrier to household and business incomes, and to generate income for them through cash payments and loans, whereas the primary goal of the monetary measures was to stabilize the financial market, which had been shaken (Sertkaya, Baş 2021).



Source: TÜİK

Figure 15: Yearly Change Inflation Rates in Turkey between 2019/08- 2023/01.

As seen in Figure 15, the inflation caused by the lifting of the "Home Quarantine" resulted in a rise in "Demand" inflation as a result of households' increased economic mobility as a result of the removal of the limitations and prohibitions. With the onset of the war, "Cost Inflation" replaced the rates that had been rising due to "Demand Inflation". Figure 14 shows how the "reopening" process following the removal of restrictions has manifested itself in rising demand and the weight of inflation in the "Services" sector. In terms of both higher demand and increasing expenses during the "Opening Up" process, the "Services" sector has been constantly high in the weights of inflation items, as can be shown at this time. The recent fall depicted in Figure 15 contains a "Base Effect" in nominal terms, which shouldn't be ignored. Price hikes continue to be a major issue for the Turkish economy and have the potential to bias expectations. In addition to all these facts, the "Unorthodox" Monetary Policy of the Central Bank of the Republic of Turkey (CBRT) and the ongoing interest rate decreases despite the persistence of the inflation phenomenon promote the persistence and sudden increase in



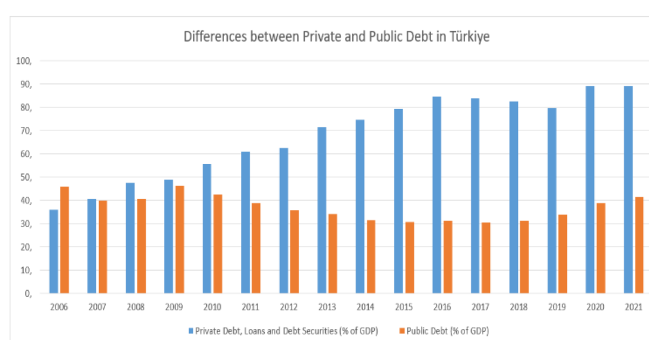
Source: OECD

inflation expectations.

Figure 16: Consumer Confidence Index (CCI) in Türkiye between 2006-2023.

Figure 16 shows that the CCI Index, which started to fall in late 2018 and is continuing trending downward, peaked in February 2023 at 97.8409. This shows that consumers, especially households, do not have a "good" degree of confidence in the economy because it is below the normal average of 100. Yet, the index does not rise above 100 points, showing that consumers still have a propensity to save money. This criterion, along with others (particularly in the post-war era), may show that inflation combines both a "Cost" and a "Demand" focus.

Together with all of these issues, the Turkish economy has long been mired in a cycle we refer to as "Twin Deficits" since it always goes in the same direction. The Turkish economy had a large "Current Account Deficit" and "Foreign Trade Deficit" even when economic indicators were at their healthiest.

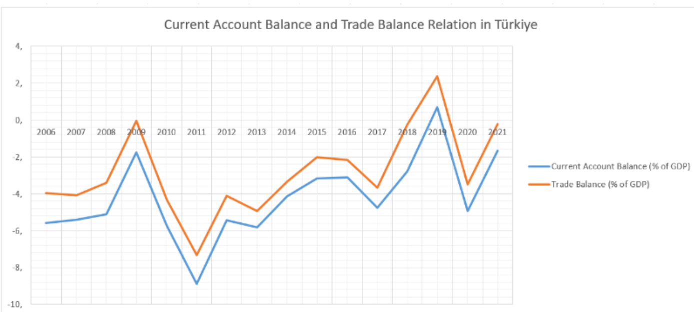


Source: IMF

Figure 17: Current Account Balance and Trade Balance Relation in Türkiye between 2006-2021.

The interpretation that the Turkish economy has been dealing with this persistent issue for quite some time and that it was caught off guard for both the "Russia-Ukraine War" and the "Covid-19" crises as a result of this situation will be taken for granted given the "Base Effect" observed in the post-crisis periods.

Regarding its financial responsibilities, Turkey has likewise been changing roles for a while. After the Great Recession of 2008, this handover took place, as shown in Figure 18, with private sector borrowing surpassing public sector borrowing and the gap growing wider with each passing year. With the "Covid-19" crisis, public borrowing in this series, in which the private sector borrowed more and more, also grew. Following the "Double Earthquake" on February 6, the Republic of Turkey issued a new resource budget for the reconstruction and relocation of the ten affected regions and faced a significant burden in terms of public borrowing and current account deficit.



Source: IMF and TÜİK

Figure 18: Differences between Private and Public Debt in Türkiye between 2006-2021.

When the median ratios of the latest polls are observed, it is observed that the National Alliance (Millet İttifakı) candidate "Kemal Kılıçdaroğlu" prevails in both multi-candidate and two-candidate (second round) projections (Morgan Stanley, 2023). In the pre-election period, the Turkish economy carries many concerns in terms of macroeconomic indicators. These agendas (Morgan Stanley, 2023);

1- Corporate demand for foreign currency, which has been suppressed by various market interventions.

2- Efforts to keep the nominal exchange rate stable through fiscal and credit stimulus in the face of negative real interest rates, leading to significant deficits in both the trade deficit and the central bank's net foreign exchange positions.

3- The Central Bank's lack of "Room Space (Friedman, 2003)", the tight Net Foreign Exchange Position (about -$58 billion) and the Central Bank's dwindling resources in terms of expendable foreign exchange reserves (about -$32 billion).

4- An environment of insecurity about the interest and repayments of CLD (Currency-Linked Deposit) accounts, which were created as a financial asset, and a budgetary burden with an uncertain future.

Although interventions by government-led institutions may seem to provide a solution in the short run period, in the long run period they lead to both a budget burden and a deterioration in expectations. Although the USD/TRY exchange rate has been brought under control by market interventions, the USD/TRY exchange rate is positioned to rise due to potential pent-up demand for foreign exchange by firms, the payment of CLD and liquidity challenges (Morgan Stanley, 2023). These situations gradually lead the Turkish Economy to the phenomena of "USD/TRY increase" and "Monetary and Fiscal Tightening" regardless of the election results.

At this point, we create two scenarios based on the outcome of the election in favor of the "National Alliance" and the "People's Alliance". We review the possible scenarios by explaining the economic impacts and expectations from various perspectives.

Scenario 1; *"If the National Alliance Policymakers Take Over the Economic Management,"*

"The superiority of the Millet Alliance, which represents the likely scenario with the results observed from the surveys, will put the Turkish Economy into a phase of various structural reforms. The applications planned to be realized in the first stage will be to remove "Market Interventions". Emphasizing the independence of the Central Bank, eliminating interventions contrary to the floating exchange rate policy, interventions applied to banks, etc. The Millet Alliance staff, who aim to eliminate many situations, also desire to re-enter the "Orthodox Economics" framework. According to the Morgan Stanley projection, although inflation is tried to be prevented with interest rate hikes up to 30%-35% in the first place, the possible effects of this situation for the USD/TL level cannot be avoided. In this case, even if the Millet Alliance wins, there will be a noticeable increase in the USD/TL level. In this case, Turkish households and economic actors should be reminded that the Millet Alliance staff do not have a magic wand. The Millet Alliance staff will try to implement these practices amid the tight foreign exchange balances and positions of the Central Bank."

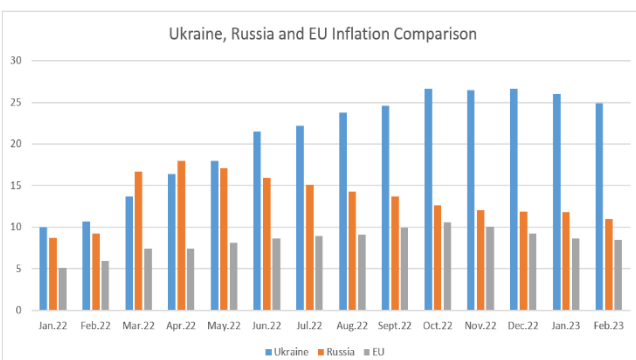
Scenario 2; *"If the People's Alliance Policymakers Take Charge of Economic Management,"*

"If the People's Alliance, which currently holds the government, prevails in the elections, the Turkish Economy will deepen the concerns it already harbors. Inflation, stripped of its base effect, will continue its upward trend. In the light of the Morgan Stanley projection, the USD/TL level will start to trend upwards by 2023Q4, even though various interventions are trying to keep it stable. Although the People's Alliance Economic Staff is pursuing a specific interest rate cut program, they may reverse their decision due to raging inflation. A slight increase in interest rates has been added to the projection. With these facts, it is observed that 2024 will pass with a "Recession" and this phenomenon (along with the deterioration of expectations) will become permanent as long as the concerns are not eliminated."

The "Ukranian War" is the one of the two cases stated in the article that is now on the news and whose effects have been seen. Two of Turkey's Black Sea neighbors engaged in combat. Turkey and both nations have close trading ties.

Following a bilateral economic partnership in agriculture and energy with Russia. Also Turkey has established a close trading relationship with Ukraine in industries like "defense industry" and construction, among others, thanks to the Crimean War in 2014. (Oktav, 2022).

When the conflict started, Turkey maintained its diplomatic cool-bloodedness and pursued a balanced foreign policy with both nations despite facing a severe security imbalance. Despite the fact that energy shortages appeared to be the first significant issue following the start of the war, this was actually a "Food Crisis" because of Ukraine's importance as a high-grain exporter. 95% of Ukraine's grain exports go through ports on the Black Sea, and the war has made these ports significantly less "safe" (Yenginar, 2022). Due to its sensible foreign policy at this period, Turkey concentrated on this problem and acted as a "mediator". The "Grain Corridor" arrangement and the transportation of the grain supply were secured as a result of the growth of this role and prestige. The agreement was signed on July 22, 2022, by the United Nations, Russia, Ukraine, and Turkey (*Yenginar, 2022*). By taking on a bridge position during a time of major crisis, the Republic of Turkey was able to strengthen its position within the conflict and raise its significance (Oktav, 2022).



Source: TradingView, ECB

Figure 19: Comparison of Inflation; Ukraine - Russia and EU Region between January 2022 – February 2023

We will analyze three scenarios for Turkey in the Russian-Ukrainian conflict in light of this knowledge. In light of the material we have already discussed, we will discuss these options and draw conclusions;

Good Scenario; *"Turkey Deepens its "Mediation" Role":*

By a number of agreements, Turkey broadens the meaning of its "Mediation" function, which it began with the Grain Corridor pact. The Ankara government, which is likely to seize these chances, can, as it has done in the past, turn crises into "opportunities" by significantly increasing trade with both nations, halting the spread of the conflict while also benefiting commercially. By adding new pipelines to its continuing energy cooperation with Russia, it may serve as a crossroads in the energy sector. It can also become a high-value exporter by concluding a range of agreements with Ukraine in the burgeoning defense industry. In this approach, the local parameters might look for a break from the bad impacts of the conflict as well as a positive balance in the economic equilibrium. The war must depart from the Acceptable Violence and enter a phase of slowness in order for this scenario to be realized.

Base Scenario; *"Turkey Maintans its "Mediation" Role":*

"Turkey continues to take the "Mediator" stance it adopted with the Grain Corridor accord. The balance policy is still in place, and both sides of the conflict are kept at equal distances. In this approach, Turkey is able to analyze the possibility of a widening of the conflict and use its "Mediator" position to prevent it. By experiencing a situation of market indifference in its domestic economic parameters, Turkey can mitigate the effects of the conflict to some extent. The war must continue at the level of Acceptable Violence, and tensions must not worsen, in order for this scenario to be implemented."

Bad Scenario; *"Turkey Tends to Take Sides and Loses its Position as a Mediator":*

"Because to the changing circumstances and progression of events, Turkey must deal with a move by one of the two sides to sabotage the "Mediator" position. Turkey consequently tends to pick a side and lose its function as a Mediator in order to defend its legitimate rights and interests. Developing Economies would be at risk of a new food crisis if the Grain Corridor accord failed. The negative externalities of the conflict would be felt more keenly in Turkey, and the country would experience severe economic aberrations and distortions. Under the strain of war, the Turkish economy may deviate from its projections, and financial institutions and organizations may experience a delay in investment, which would ultimately harm their nation's GDP. The deepening of the conflict and the Kiev-Moscow governments' abandoning of their pro-peace rhetoric should increase the possibility that this scenario will come to pass.

3. Conclusion

In this study, we've covered a variety of characteristics to explain why the global economy has been dragging itself into a "recession" for so long. The World Economy has been described as having entered a protracted era of instability beginning in 2008 and as continuing to this day in a cycle of self-stabilization.

Throughout this study, we have delved into various factors contributing to the prolonged state of recession in the global economy. Since the onset of the "Great Recession" crisis in 2008, we have witnessed the implementation of expansionary monetary policies, which persisted until 2015, only to be interrupted by the unprecedented "Covid-19" crisis in 2020. Additionally, the adverse effects of the pandemic further exacerbated the situation through the deterioration of public expenditures and fiscal incentives.

Our analysis shed light on the implications of increased money supply on the economy, as well as the consequential impact on inflation-related metrics due to fiscal incentives. By examining the Consumer and Business Confidence Indexes, we uncovered the burdensome costs and deficits that governments had to grapple with as a result of these crises. Furthermore, we offered insights into the detrimental consequences of unforeseen interest rate hikes, leading to what can be described as a "Hard Landing" effect.

We talked about the "Expansionary Monetary Policy" that began with the "Great Recession" crisis in 2008 and persisted until 2015 before being put on hold by the "Covid-19" crisis in 2020, as well as the "Public Expenditures and Fiscal Incentives" that significantly worsened as a result of "Covid-19" in 2020. We discussed the impact of money supply increases on the economy and the extent to which fiscal incentives increased various inflation-related metrics. With the use of the Consumer and Business Confidence Indexes, we looked at the costs and deficits that governments had to deal with as a result of the crises. With all of this information in mind, we made some comments regarding the "Hard Landing" effects brought on by unexpected interest rate increases.

In the subsequent section, we explored how the world economy, still reeling from the aftermath of the Covid-19 period, responded to the conflict between the governments in Kiev and Moscow, particularly in Eastern Europe. We scrutinized the repercussions of this conflict on Russia, an energy exporter, and Ukraine, a food producer, as well as its broader impact on the global economy. Emphasizing the two product categories directly affected by the conflict and the Eurozone, a significant economic player involved in the war, we unraveled the intricate relationship between the conflict and the global economy.

We looked at how the world economy—which is attempting to recover from the post-Covid-19 period's shaking and get rid of the burden on it—reacted to the conflict between the Kiev and Moscow governments that emerged in Eastern Europe. We saw what the conflict did to Russia, an exporter of energy, and to Ukraine, a producer of food, as well as how it impacted the global economy. Here, we concentrated on the two product categories impacted by the conflict and, in particular, the Eurozone, the European Union, which is one of the war's major economic actors. As a result, we got the chance to investigate how the conflict affected the global economy.

Finally, our attention turned to the distinctive position, policies, and attitudes of Turkey in relation to these variables. In a comparative analysis with other developing nations, we discerned Turkey's unique characteristics and observed how its economic conditions responded to these circumstances. Building upon our foundational assessment, we formulated a series of scenarios based on three distinct war scenarios and examined Turkey's potential attitudes towards them.

To sum up, as of 2023, the global economy finds itself mired in a protracted recessionary state that has persisted for a considerable duration. However, if the majority of predictions regarding these scenarios hold true, it is anticipated that the world economy will undergo a widespread recession phase commencing as early as the fourth quarter of 2023. Nevertheless, there is a possibility of achieving a soft landing and mitigating the severity of the recession if the global economy successfully navigates the arduous choices and circumstances it faces.

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