

DOI: <https://doi.org/10.36719/2706-6185/52/145-150>

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The Role of the Dollar in the Turkish Economy

Abstract

Turkey's economy has faced challenges due to political instability, geopolitical tensions, and the volatility of the Turkish lira. The crises of the late 1990s and early 2000s, as well as the financial crises of 2008 and 2018, caused sharp devaluations in the lira, weakened investor confidence, and led to capital outflows. The Central Bank of the Republic of Turkey's (CBRT) unconventional monetary policies have increased inflation and currency volatility. Foreign debts denominated in dollars have created a "dollar trap" and raised the costs of debt repayment. For long-term financial stability, Turkey needs to reduce its dependence on foreign debt, stabilize the lira, and implement structural economic reforms.

Keywords: *economy, finance, inflation, monetary policy, foreign exchange reserves*

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Türkiyə iqtisadiyyatında dolların rolu

Xülasə

Türkiyə iqtisadiyyatı siyasi qeyri-sabitlik, geosiyasi gərginlik və türk lirəsinin dəyişkənliyi səbəbindən çətinliklərlə üzləşib. 1990-cı illərin sonu və 2000-ci illərin əvvəllərindəki böhranlar, eləcə də 2008 və 2018-ci illərin maliyyə böhranları lirədə kəskin devalvasiyalara səbəb olub, investorların etimadını zəiflədib və kapital axınına yol açıb. Türkiyə Respublikasının Mərkəzi Bankının (TCMB) qeyri-ənənəvi pul siyasəti inflyasiyanı və valyuta dəyişkənliyini artırıb. Dollarla ifadə olunan xarici borclar "dollar tələsi" yaradıb və borcun ödənilməsi xərclərini artırıb. Uzunmüddətli maliyyə sabitliyinin təmin edilməsi üçün Türkiyə xarici borclardan asılılığını azaltmalı, lirəni sabitləşdirməli və iqtisadi islahatlar həyata keçirməlidir.

Açar sözlər: *iqtisadiyyat, maliyyə, inflyasiya, pul siyasəti, valyuta ehtiyatları*

Introduction

The Turkish lira has changed significantly over the years due to the country's complex social, economic, and political circumstances. In the late 1990s and early 2000s, hyperinflation (over 70%) caused people to lose confidence in the national currency (Muhammad et al., 2024). The *New Turkish Lira (YTL)* was introduced following the 2005 redenomination, which removed six zeros and provided the economy with short-term stability (Geldi, 2018).

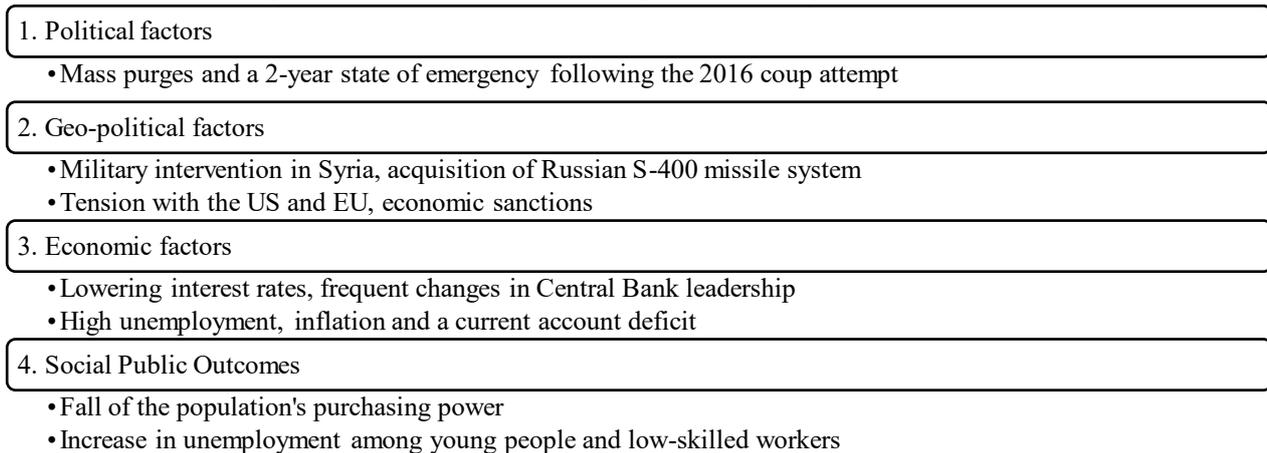
Research

The 2008 global financial crisis, however, revealed how heavily the Turkish economy depended on external capital. Since 2015, the lira has been depreciating sharply (Hassan et al., 2017). This decline has also been driven by domestic political instability and international tensions (Yılmaz, 2019). As a result, the lira lost more than 40% of its value against the U.S. dollar in 2018, triggering a major economic crisis characterized by high inflation and rising unemployment.

1. Factors Affecting the Stability of the Turkish Lira

In recent years, political instability, geopolitical tensions, and structural economic problems have heightened the volatility of the lira (Muhammad et al., 2024; Kyriazis & Economou, 2022; Yılmaz, 2019). Foreign policy decisions and sanctions have accelerated the lira’s devaluation, while interest rate cuts and changes in the Central Bank’s leadership have deepened investor distrust (Atlantic Council, 2020; Hassan et al., 2017; Geldi, 2018). High unemployment, rising inflation, and a persistent current account deficit have increased prices, reduced purchasing power, and limited investment (Muhammad et al., 2024; Kyriazis & Economou, 2022; Yılmaz, 2019).

Figure 1.1 Factors Influencing the Stability of Turkish Lira



Source: Kyriazis & Economou, 2022; Yılmaz, 2019.

2. The 2001 Turkish Economic Crisis

The economic crisis that occurred in Turkey between 2000 and 2001 had a profound impact on the country’s financial system. In 2001, foreign debt reached 181 billion U.S. dollars. As a result of the lira’s devaluation, 20 banks were placed under administrative control by the *State Savings Deposit Insurance Fund (TMSF)*. Dependence on high levels of dollar-denominated debt and ongoing political instability reduced investor confidence, causing foreign investment to decline by nearly 50% and deepening economic instability. Between 2000 and 2001, the value of 1 U.S. dollar rose from 620,000 TL to 1,500,000 TL, further increasing inflation and driving interest rates upward.

Table 1. WPI (Wholesale Price Index), CPI (Consumer Price Index), GNP per capita (Gross National Product per capita), and Growth Rate Indicators between 1990–2001.

Year	WPI %	CPI %	GNP per Capita \$	Growth Rate %
1990	48,6	60,4	2.710	9,4
1991	59,2	71,1	2.666	0,3
1992	61,4	66,0	2.776	6,4
1993	60,3	71,1	3.093	8,1
1994	149,6	125,5	2.195	-6,1
1995	64,9	78,9	2.841	8,0
1996	84,9	79,8	3.005	7,1
1997	91,0	99,1	3.110	8,3
1998	54,3	69,7	3.247	3,9
1999	62,9	68,8	2.836	-6,1
2000	32,7	39,0	2.986	6,3
2001	88,6	68,5	2.103	-9,5

Source: Central Bank of the Republic of Turkey

Foreign investments and tourism revenues have increased since the crisis. In 2005-2006, foreign direct investments exceeded 20 billion dollars, and in 2002-2014, they reached 154 billion dollars.

Table: 2 – Tourism, Foreign Investment, and Portfolio Income (Billion USD) 2005-2012.

Year	Tourism Income	Foreign Direct Investment	Portfolio Investment
2005	20.3	10.03	14.7
2006	18.6	20.19	11.4
2007	20.9	22.05	2.8
2008	25.4	19.85	-3.8
2009	25.1	8.59	2.9
2010	24.9	9.1	19.6
2011	28.1	16.18	19.5
2012	29.0	13.28	38.4

Source: Central Bank of the Republic of Turkey

Foreign Trade and Inflation Dynamics

Foreign trade has shown significant growth. Between 2000 and 2014, exports increased from **\$27.7 billion** to **\$157.6 billion**, while imports rose from **\$54.5 billion** to **\$242.2 billion**. As a result, the trade balance deficit reached **\$105 billion**.

3. Inflation, Imports, and Domestic Consumption

A depreciation of the lira against the dollar raises inflation in the Turkish economy by increasing import costs and affecting food, energy, and raw material prices. Consequently, purchasing power declines, and living standards deteriorate (CBRT, 2023; Yılmaz, 2019).

The weakening of the lira against the dollar further elevates import costs, thereby intensifying inflation. Inflation stood at **36% in 2021** and **69.9% in 2022**, as the lira's depreciation exceeded **40%**. Energy prices rose by **over 25% in natural gas** and **more than 30% in oil**. Studies indicate that a **1% depreciation** of the lira against the dollar increases the **CPI (Consumer Price Index)** inflation rate by **approximately 0.5%**.

Table: 3 - Macroeconomic Analysis of Food and Energy Prices 2020-2023.

Year	Inflation Rate (%)	Energy Import Costs (USD Billion)	Wheat Import Price (USD/ton)	Average Fuel Price (TRY/Liter)	Bread Price Increase (%)	Food Price Increase (%)
2020	14.6	45.1	250	6.6	8	12
2021	36.1	54.3	300	7.4	15	22
2022	69.9	58.9	350	10.2	30	40
2023	52.5	65.2	400	12.3	25	35

Source: Central Bank of the Republic of Turkey (CBRT, 2023), Ministry of Energy, Turkey (2023), Open METU (2022)

High import dependency and rising dollar prices increase domestic prices and reduce purchasing power. In 2022, the price of gasoline rose by **50%**, while the price of bread increased by **30%**. Low-income households are disproportionately affected by inflation, as the majority of their expenditures are allocated to food and energy.

Table: 4 - Price Changes of Food and Commodities in 2021-2022.

Commodity	Price Increase (%)	2021 Average Price (TRY)	2022 Average Price (TRY)
Gasoline (per liter)	50	7.4	12.3
Bread (per loaf)	30	4.0	5.2
Wheat (per ton)	17	300	350
Cooking Oil (per liter)	40	20.0	28.0
Rice (per kg)	28	7.5	9.6

Source: Central Bank of the Republic of Turkey (2023), Yilmaz (2019).

Although the government has introduced energy subsidies, price controls, and transfer programs, inflation has not been completely eradicated, as the main problem — the devaluation of the lira — has not yet been resolved.

4. Foreign Investment

Foreign capital has played a crucial role in Turkey’s economic growth. Most of it has come in the form of portfolio and direct investments (Karluk, 2001). After the *Foreign Direct Investment Law* was enacted in 2003, the inflow of foreign capital increased rapidly. **FDI rose from \$1.7 billion in 2000 to \$15.8 billion in 2006.** Improved macroeconomic indicators, ongoing negotiations with the **European Union (EU)**, structural reforms, and interest in privatization all contributed to this growth.

Most foreign investments were directed toward the **service sector**, with transportation, communication, and financial services accounting for **78% of total inflows**. However, investments in tourism remained relatively low. This concentration underscores the dominant role of the service sector in Turkey’s economy.

Table: 5 - Foreign Capital Inflows in the Services Sector by Years (Million USD).

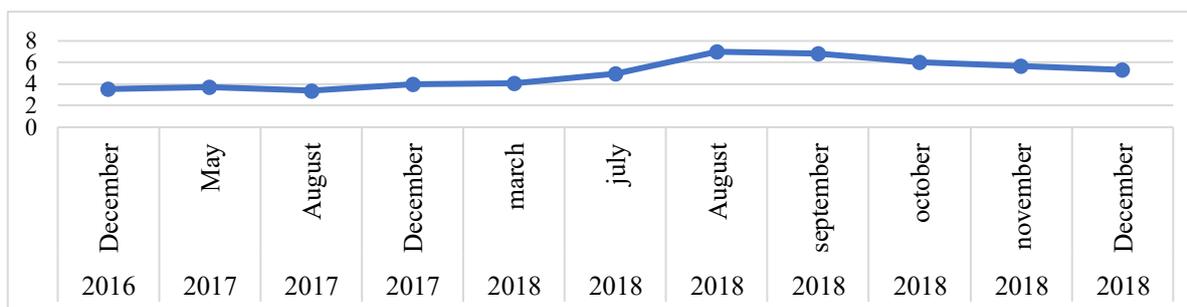
Years Sector	2003	2004	2005	2006
Electricity, Gas, Water	86	69	4	60
Construction	8	23	100	403
Wholesale, Retail Trade	92	103	68	62
Hotels, Restaurants	4	1	42	15
Transport, Communication	2	639	3250	6271
Financial Intermediation	51	69	4016	6115
Real Estate Rental	6	3	29	35
Other	33	89	177	1657
Total Services	282	996	7686	14618
Grand Total	745	1291	8519	15867

Source: Undersecretariat of Treasury. International Direct Investment Data Bulletin, General Directorate of Foreign Capital. 2007, Ankara

5. Andrew Craig Brunson Crisis and Its Impact on Turkey’s Currency and Foreign Trade

The arrest of Andrew Craig Brunson in 2016 severely strained relations between Turkey and the United States, triggering a financial crisis. The Turkish lira lost nearly 40% of its value as a result of U.S. sanctions, with the exchange rate peaking at 7.21 TL per dollar. Companies heavily dependent on foreign currency debt and imports faced serious difficulties, leading to a surge in bankruptcies. Although Brunson was released in October 2018, causing the exchange rate to temporarily fall to 5.29 TL, the overall economic repercussions persisted and could not be resolved immediately (The Guardian, Bloomberg, CNBC, The Telegraph, USA Today, & Hürriyet, 2018).

Table: 6 – Changes in the exchange rate during the Pastor Brunson crisis.



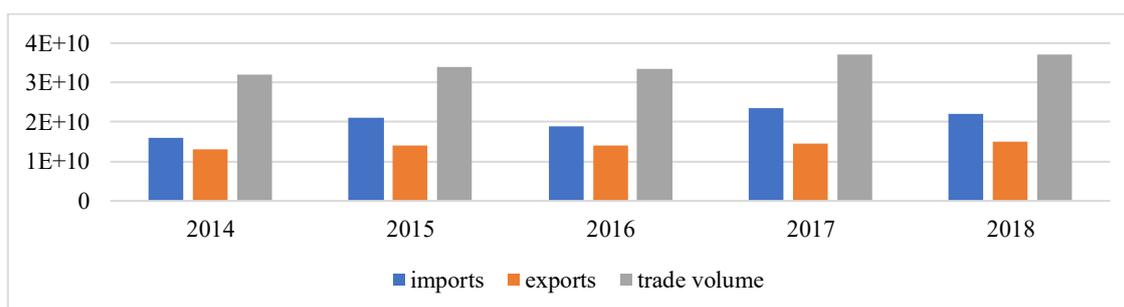
Source: Turkish Statistical Institute.

5.1 The “Jet” Crisis Between Turkey and Russia

The Turkish Air Force shot down a Russian military aircraft on November 24, 2015, triggering a major political and economic crisis in Turkish–Russian relations (Özdal & Darıcılı, 2017; *The Guardian*, 2018). The sanctions imposed by Russia negatively affected trade in the food, construction, tourism, and healthcare sectors. As a result, bilateral trade volume dropped from \$31 billion in 2014 to \$16 billion in 2016 (Çopuroğlu & Karpuzcu, 2017).

Although trade recovered to \$25 billion in 2017, specific trade flows showed sharp declines — falling from \$3.36 billion in 2015–2016 to \$1.5 billion in 2016–2017, and from \$18 billion in 2015–2016 to \$13.8 billion in 2016–2017.

Table 7: Annual Trade Data for Russia (USD).



Source: Turkish Statistical Institute.

6. Debts and Foreign Credits

Turkey’s economy has become increasingly reliant on borrowing from abroad—primarily in U.S. dollars—to finance key sectors such as energy, construction, and telecommunications (Ceyhun, 1992; Yılmaz, 2019). When the lira lost 30% of its value during the 2018 financial crisis, the cost of debt servicing surged, triggering inflation and reducing real incomes. By 2023, approximately 70% of Turkey’s \$500 billion external debt was denominated in dollars, while the debt-to-GDP ratio had risen from 40% in the early 2000s to 100%. This mounting debt burden has constrained business profitability, limited investment, and raised serious concerns about the long-term sustainability of Turkey’s debt-dependent growth model.

Conclusion

Turkey's reliance on foreign debt denominated in U.S. dollars poses significant risks to its financial stability. The depreciation of the lira increases the cost of servicing debt, placing heavy pressure on both the public and private sectors. Simultaneously, inflation and current account deficits further exacerbate financial vulnerabilities. Highly indebted firms in construction, energy, and telecommunications sectors struggle to repay their loans, leading to bankruptcies and debt restructurings that negatively impact the broader economy.

To mitigate these risks, the government should promote borrowing in the national currency, encourage domestic investment, and diversify debt sources. Strengthening the lira and reducing inflation would support both businesses and consumers. Furthermore, adopting a sustainable debt policy would enhance long-term economic growth and stability.

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Received: 22.04.2025

Accepted: 15.09.2025