

ECONOMIC RELATIONS BETWEEN TURKEY AND IRAN
FROM 1990 TO 2010:
A TURKISH PERSPECTIVE

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ABSTRACT

ECONOMIC RELATIONS BETWEEN TURKEY AND IRAN FROM 1990 TO 2010: A TURKISH PERSPECTIVE

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This study aims to analyze the transformation of Turkey's relations with Iran in the 1990s and 2000s from the perspective of "trading state" in a historical framework. In this context, the political and economic relations between Turkey and Iran are discussed by taking into consideration the internal transformation of Turkish economy. This thesis argued that the course of Turkey's relations with Iran in the 1990s is mainly shaped by the military-political considerations. Not only political but also economic relations between Turkey and Iran were negatively affected by tensions and rivalry between the parties during the 1990s. Despite the counter-efforts of some of the business circles and the political parties, neither the economic nor the political relations did improve. Unlike the 1990s, Turkey's relations with Iran in the 2000s are largely shaped by economic and commercial considerations. Increasing dialogue and developing cooperation at the political level are positively reflected in the economic relations. As a result of the eagerness of Turkish businessmen towards the development of economic relations with Iran and the intensive support of the political elites, economic relations substantially improved in the 2000s. However, rising foreign trade relations between the parties created an asymmetric dependence to the detriment of Turkey, rather than mutual interdependence as Iran benefits more from this relationship due to its oil and natural gas exports. The increasing relationship between Turkey and Iran supports the argument that Turkey is emerging as a "trading state" in the 2000s.

Keywords: Turkey, Iran, Trading State, Foreign Trade, Economic Relations.

ÖZ

1990'DAN 2010'A TÜRKİYE-İRAN EKONOMİK İLİŞKİLERİ: TÜRKİYE PERSPEKTİFİ

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Bu çalışma, Türkiye'nin İran ile olan siyasi ve ekonomik ilişkilerinde 1990'larda ve 2000'lerde yaşanan dönüşümü "ticaret devleti" perspektifinden tarihsel bir çerçevede incelemektedir. Bu kapsamda, Türkiye'nin İran ile olan siyasi ve ekonomik ilişkileri, Türkiye ekonomisinin içsel dönüşümü göz önünde bulundurularak ele alınmaktadır. Bu tez göstermiştir ki, 1990'larda Türkiye'nin İran ile olan ilişkileri temel olarak askeri ve siyasi mülahazalar çerçevesinde şekillenmiş; yaşanan gerilimler ve rekabet sadece siyasi ilişkileri değil ekonomik ilişkileri de olumsuz yönde etkilemiştir. İş çevrelerinin ve siyasetin belirli bir kanadının aksi yönde çabalarına rağmen ne ekonomik ne de siyasi ilişkiler gelişmiştir. 2000'lerde ise 1990'ların aksine Türkiye'nin İran ile olan ilişkileri temel olarak ekonomik ve ticari mülahazalar çerçevesinde şekillenmiş; siyasi düzlemde artan diyalog ve gelişen işbirliği ekonomik ilişkilere olumlu bir şekilde yansımıştır. 2000'lerde iş çevrelerinin ekonomik ilişkilerin geliştirilmesi yönündeki istekliliği, siyasi iradenin yoğun desteği ile birleşmiş; bunun sonucunda ekonomik ilişkiler dikkat çekici bir biçimde artmıştır. Ancak taraflar arasında artan ticari ilişkiler, karşılıklı bağımlıktan ziyade, Türkiye aleyhine asimetric bir bağımlılık yaratmış, İran petrol ve doğal gaz ihracatına bağlı olarak ticari ilişkilerden daha çok faydalanmıştır. Son on yılda Türkiye'nin İran ile ilişkilerinde yaşanan bu dönüşüm ve ilerleme, Türkiye'nin 2000'lerde bir "ticaret devleti" ne dönüştüğü yönündeki savı desteklemektedir.

Anahtar Kelimeler: Türkiye, İran, Ticaret Devleti, Dış Ticaret, Ekonomik İlişkiler.

To My Sweet Mom...

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LIST OF ABBREVIATIONS

AKP	Justice and the Development Party
ANAP	Motherland Party
ASKON	Anatolian Lions Businessman Association
ASO	Ankara Chamber of Industry
BEC	Classification by Broad Economic Categories
BOTAŞ	Petroleum Pipeline Corporation
BRICS	Brazil, Russia, India, China and South Africa
BTC	Baku-Tbilisi-Ceyhan
CBRT	Central Bank of the Republic of Turkey
CENTO	Central Treaty Organization
D-8	Developing Eight
DEİK	Foreign Economic Relations Board
DİSK	Confederation of Revolutionary Trade Unions
DP	Democrat Party
DSP	Democratic Left Party
EC	European Community
ECO	Economic Cooperation Organization
ECOTA	Economic Cooperation Organization Trade Agreement
EEC	European Economic Community
EU	European Union
FDI	Foreign Direct Investments
FTA	Free Trade Agreement
G-20	The Group of Twenty
G-8	The Group of Eight
GATT	General Agreement on Tariffs and Trade
GCC	Gulf Cooperation Council
GDP	Gross Domestic Product
GNP	Gross National Product

IAEA	International Atomic Energy Agency
IMF	International Monetary Fund
ISI	Import Substitution Industrialization
ISIC	International Standard Industrial Classification
JEC	Joint Economic Commission
MESS	Turkish Employers' Association of Metal Industries
MFN	Most Favored Nation
MHP	Nationalist Action Party
MÜSİAD	Independent Industrialists and Businessmen Association
NATO	North Atlantic Treaty Organization
NGO	Non-Governmental Organization
OECD	Organization for Economic Cooperation and Development
OEEC	Organization for European Economic Cooperation
OIC	Organization of the Islamic Conference
PJAK	The Party of Free Life in Kurdistan
PKK	The Kurdistan Workers' Party
RCD	Regional Cooperation and Development
SEE	State Economic Enterprise
SME	Small and Medium-sized Enterprises
SNA	System of National Accounts
SPO	State Planning Organization
TAI	Turkish Aviation Industry
THY	Turkish Airlines
TİKA	Turkish International Cooperation and Development Agency
TİM	Turkish Exporter's Assembly
TİSK	Turkish Confederation of Employer Associations
TOBB	Union of Chambers and Commodity Exchanges of Turkey
TPAO	Turkish Petroleum Corporation
TPP	True Path Party
TURKSTAT	Turkish Statistical Institute
TUSKON	Confederation of Businessmen and Industrialists of Turkey

TÜPRAŞ	Turkish Petroleum Refineries Co.
TÜRK-İŞ	Confederation of Turkish Trade Unions
TÜSİAD	Turkish Industrialists' and Businessmen's Association
UFT	Undersecretariat for Foreign Trade
UN	United Nations
US	United States of America
USSR	Union of Soviet Socialist Republics
UT	Undersecretariat of Treasury
WB	World Bank
WP	Welfare Party
WTO	World Trade Organization

CHAPTER 1

INTRODUCTION

In the 2000s, the course of Turkish-Iranian relations has undergone a noticeable change when compared to the 1990s. The relations in the 1990s were characterized with conflict and tension. The 2000s on the other hand witnessed a relatively positive atmosphere and increasing cooperation. Under these circumstances, not only political but also economic, cultural and even military relations have found a chance to improve and strengthen. In the 2000s, the conflictual characteristic of relations have faded away and hence paved the way for a cooperative attitude on both sides.

The 1990s witnessed the escalation of tensions, the rupture of dialogue, and the decline of cooperation in bilateral relations. In this context, ideological confrontation, PKK terrorism, and competition in the Central Asia and Caucasus constituted main stress points in the bilateral relations during the 1990s. First of all, ideological controversy between the secular Turkey and the theocratic Iran negatively affected the bilateral relations. The rise of political Islam and radical Islamists in Turkey and the assassination of some prominent Turkish intellectuals were perceived by Turkey as a part of Iran's efforts to destabilize Turkey's regime and export its revolution. Secondly, the intensification of PKK terrorism and the Kurdish question adversely affected bilateral relations. Continued PKK attacks in areas adjacent to the Turkish-Iranian border have frequently brought tensions between the two countries. Turkey constantly accused Iran of giving the PKK training, health and logistic support, sheltering the PKK militants and encouraging its attacks inside Turkey. Thirdly, the end of bipolarity and the collapse of the Soviet Union drove Turkey and Iran into a fierce competition over the Central Asia and Caucasus and produced a conflictual atmosphere in bilateral relations. In addition, Turkey's growing ties with Israel and deterioration of its relations with Syria - ally of Iran - further alienated the two countries. All of these developments posed a huge

obstacle for the expansion of economic relations and adversely affected the foreign trade between Turkey and Iran in the 1990s.

On the contrary, the 2000s witnessed the rise of dialogue and cooperation in many aspects of bilateral relations as a consequence of the revival of pragmatism in Turkish foreign policy towards Iran. First of all, the AKP's rise to power, its "zero problem, limitless trade with neighbors" strategy, the increasing influence of the industrialists and exporters in determining the course of foreign policy have created an environment conducive to advance bilateral relations. Secondly, the Iraq War and its repercussions, profoundly and positively affected Turkish-Iranian relations. Commonalities of interests and threat perceptions concerning Iraq and the Kurdish issue paved the way for the emergence of a common ground for cooperation between the parties. In addition the rise of the PKK in Turkey and PJAK in Iran further brought the two countries together. The rise of cooperation in the security issues created a positive atmosphere between the parties and facilitated further cooperation in other areas of the bilateral relations. Thirdly, Turkey's increasing energy demand and Iran's rich natural gas and crude oil reserves have provided a strategic common ground for cooperation. In addition, Turkey has tried to cooperate with Iran in new joint investment projects in the energy field. Furthermore, Turkey's willingness to serve as an energy corridor between Western markets and Iranian hydrocarbon resources has constituted an important area of cooperation. Another reflection of the Turkish-Iranian rapprochement has been the nuclear issue. In the 2000s, Turkey pursued a compromising attitude towards Iran in the nuclear issue and involved in facilitation or mediation efforts between Iran and the West. In addition, Turkey's deteriorating relations with Israel, limitations on its relations with the US, growing relations with Middle Eastern countries and the AKP's pro-Islamic discourse has generated a positive atmosphere in which Turkey and Iran started to cooperate closer. Consequently, all of these developments positively affected the economic relations between Turkey and Iran during the period and the further bilateral political relations improved, the further economic relations gained momentum and *vice versa*.

With a view to have a better understanding of this sea change in Turkish-Iranian relations, a great deal of studies has been conducted from a wide range of theoretical perspectives by researchers. This literature has definitely contributed to our knowledge and enriched our understanding of what drives Turkish foreign policy towards Iran. However, the role of economic factors in shaping the course of Turkish-Iranian relations has not been examined adequately. Therefore, this thesis aims to analyze the reasons behind this change in Turkish-Iranian relations from the 1990s to 2000s, by looking at the economic dimension of the relationship mainly from a Turkish perspective. It will use the conceptual framework presented by Richard Rosecrance -“trading state”- to discover the impact of economic considerations in determining and shaping Turkish foreign policy towards Iran. In this respect, the studies of Kemal Kirişçi who has also taken the “trading state” argument to explain the transformation in Turkish foreign policy have been very significant for this study.

In this context, this thesis started with the question of what drives Turkey to pursue closer economic relations with Iran in the 2000s and how and why it changed from the 1990s. In addition, this study tries to answer the questions whether the economic considerations affected the foreign policy of Turkey towards Iran, to what extent and through what channels the economic considerations affected Turkish foreign policy towards Iran.

In this context, this thesis questioned the idea that Turkey is increasingly becoming a “trading state” and leaving the “military-political state” behind in the 2000s. In line with this thought, it finds out that economic considerations - increasing exports, search for new export markets, attracting investments- the role of businessmen and their interests are gaining importance in the foreign policy making. In this context, this thesis argues that what lies behind the change in Turkish-Iranian relations from the 1990s to the 2000s is this change in Turkish foreign policy from a “military-political state” to a “trading state”.

By the early 1980s, Rosecrance argued that there are two worlds in the international system; one is the “military-political world” and the other one is the “trading world”.¹ From the beginning of the modern period, the pendulum has swung between these two worlds, but none of them dominated the course of international relations on its own, rather they both had an impact on the relations simultaneously. According to Rosecrance, in “military-political world” nations are ranged in terms of power and territory.² In this world, the primary objectives of the states have been to increase their territories and maintain them against other states. As a natural result, in this system war and threat of war have been pervasive features of interstate relationships. In contrast, the “trading world” is composed of nations differentiated in functions and specializations.³ Since different nations supply different products and services, they come to depend upon each other and each country may seek to improve its position in a “trading world”. Trade has been the natural result of this differentiation in functions and growing interdependence. In this framework, “trading states” recognize that they can do better through internal economic development sustained by an open worldwide market for their goods and services than by trying to conquer new lands. Contrary to the “military-political world”, the primary objectives of the “trading states” have been to improve national welfare and the allocation of resources through internal development and trade with other states.⁴

In the contemporary world, each state has characteristics of both the “trading state” and the “military-political state” at the same time, because, no state can totally disregard its territorial defense and stake its livelihood solely on trade. At this point the choice that states make between placing their primary emphasis whether on the “military-political state” or the “trading state” become crucial and influenced by a number of factors. The first option is based on the military capabilities, territorial control and power struggle in international relations, while the second one is based

¹ Richard Rosecrance, *The Rise of the Trading State: Commerce and Conquest in the Modern World*, New York, Basic Books, 1986, p. 22.

² *Ibid.*, p. 23.

³ *Ibid.*, p. 24.

⁴ *Ibid.*, pp. 26-28.

on the grounds of interdependence, foreign trade, cooperation and dialogue. Rosecrance also notes that the leadership plays an important role in making a choice between these two strategies through “social learning”. He explained that the choice of leaders is partly shaped by the theories and past experiences that they bring with them.⁵

Rosecrance argued that, today increasing number of states choose to improve their position in world politics through economic development and trade. In other words, trading system has been increasingly replacing the military-political system. The growing preference of states for a trading strategy in international relations stems not only from the benefits of commerce but also from the costs of waging war and seizure of territory, so to say of being a “military-political state”.⁶ In addition to these, growing population, progress in education, improvements in technology, communication and transportation, increase in production capacity, soaring energy demand and limited resources not only facilitate but also compel states to trade more and pave the way for increasing interdependence among them. Further increase in interdependence is required in diminishing the barriers to trade and will probably lead to raising the cost of war. However, as Rosecrance emphasized, one should not place too much emphasis upon the existence of interdependence *per se*.⁷ As experienced in the World War I and II, interdependence did not prevent political crises or wars which led to breakdown of the international system. The emerging trading world of international relations only offers the possibility of escaping from a vicious cycle of conflicts or wars and finding new grounds of cooperation among states.

Within the scope of Rosecrance’s notion of the “trading state”, it can be deduced that in the process of becoming a “trading state” the share of foreign trade in GDP increases and its importance in the economic growth rises. In other words, as the foreign trade steadily develops, it comes to constitute a growing proportion of economy. As a result, not only domestic but also the foreign policy of state becomes

⁵ *Ibid.*, pp. 41-42.

⁶ *Ibid.*, pp. 155-160.

⁷ *Ibid.*, p. 141.

increasingly shaped by economic considerations. Moreover, with the emergence of the “trading state”, a wide range of actors come to participate in foreign policy-making process and the interests or priorities of these actors are quite different from the actors of the “military-political state”. Indeed, the trading system depended on setting free the productive and trading energies of the peoples and merchants who would find markets for their goods and services overseas.⁸ Furthermore, as Kirişci noted, the rise of the “trading state” has transformed and is transforming traditional foreign policy-makers as well. In this sense, they are increasingly coming to recognize that national interest cannot be solely determined in terms of a narrowly defined national security, and that economic considerations such as the need to trade, diversify export markets and attract foreign direct investment are just as important.⁹

However, it is important to underline that there is a strong correlation between the emergence of “trading state” and the improvement of security conditions. In that sense, the emergence of the “trading state” is dependent on a secure, predictable and stable environment. It is true that the rise of the “trading state” positively contributed to creating a secure environment for states but the “trading state” cannot emerge without a sufficiently secure environment. Not to mention the fact that, when states have to make a choice between security and trade, they choose security. In other words, under compelling conditions the “trading state” retreats in favor of the “military-political state”. Since the foreign policy choices between the “military-political” and the “trading state” are constrained by the escalation of security concerns and threat perceptions, the sustainability of the emergence or the rise of the “trading state” becomes problematic.

Thus, this study questioned the profound shift in Turkish foreign policy towards Iran from the 1990s to 2000s and tries to explain this sea change through using the “trading state” as a conceptual framework by bearing in mind the shortcomings of the concept.

⁸ *Ibid.*, p. 27.

⁹ Kemal Kirişci, “The Transformation of Turkish Foreign Policy: The Rise of the Trading State,” *New Perspectives on Turkey*, No. 40 (2009), pp. 33-34.

This thesis consists of three major chapters. The first chapter analyzes the historical developments in the Turkish-Iranian relations from 1923 to 1990. This chapter divides this long period into two sub periods: one is the period between 1923 and 1979 and the other one is the 1980s. The period from 1923 to 1979 can be characterized as a period of limited economic relations between the two countries. Although political relations were not very conflicted and the two countries were at the same camp in the Cold War bipolarity, economic relations remained limited as a result of the state-led growth strategies and ISI policies pursued by Turkey. In fact, as developing countries on the way of industrialization, both Turkey and Iran were not able to produce mutually complementary products, other than oil and agricultural commodities.

This research gives a special emphasis to the 1980s, in which the process of becoming a “trading state” has started. In this framework, initially the general features of the Turkish economy, the profound change in the economy policies following the abandonment of the ISI and adoption of the export oriented industrialization policies by the January 24 Decisions, the impact of this change on the business class and its relations with the state, in short, the process of becoming a “trading state” are analyzed. Afterwards, the study concentrated on Turkish-Iranian political relations in general and on the bilateral economic relations in particular. Foreign trade relations between Turkey and Iran examined thoroughly with a view to understand how the process of becoming a “trading state” affected the bilateral relations. This part assumes Turkey started to become a trading state from the 1980s onwards, however the “military-political” characteristic also continued in the period due to security issues, mainly the PKK issue.

After examining the historical background of Turkish-Iranian relations, the study goes on to analyze the focal periods of this thesis: the 1990s and 2000s. In both chapters, firstly the general features of Turkish economy, major economic indicators, shifts in the economy policies, and their impacts on the business class and the relations of the business class with the state are examined. Secondly, the political determinants of the Turkish-Iranian relations are studied. In this context, parameters of the relations are determined and major positive (cooperation grounds) and

negative factors (stress points) are examined closely in terms of global, regional and bilateral relations. Thirdly, economic relations between Turkey and Iran for both periods – the 1990s and 2000s- are addressed in detail and the main features of the economic relations are clarified.

These two chapters try to demonstrate how the political relations have affected the economic relations and *vice versa*. Furthermore, in background the study tried to elucidate the changes in the relationship due to Turkey's process of becoming a "trading state" which has started in the 1980s, was disrupted in the 1990s and is revived in the 2000s.

During the process of writing this thesis, I used both secondary and first-hand sources. For writing the developments in the bilateral political relations, I used secondary sources such as books, articles, journals, etc. However for writing the general features of Turkish economy, I used both the secondary and first hand sources. In addition, for writing the economic relations between Turkey and Iran, I used only the first-hand sources. Actually this stage was very difficult, because these sources consisted of a wide range of raw data on Turkey's foreign trade, world trade, foreign direct investments, tourism, GDP, debt, etc. During this process, I heavily used the databases of the Turkish Statistical Institute, Ministry of Economy, Central Bank of Turkey, Undersecretariat of Treasury, World Trade Organization and International Monetary Fund. All of these raw data were analyzed profoundly in terms of value, change, and share on the basis of product, country, country-group, sector and company. And finally, all the relevant raw data were processed, calculated and then turned into tables, graphs and figures personally in order to provide a clear picture. Furthermore, my area of expertise and professional network gave me the chance to reach the data of the first 50 years of the trade relations between Turkish Republic and Iran, which was not available in the publicly open databases of the aforementioned agencies and has been very significant in providing profound insight about economic relations and the theme of this study.

CHAPTER 2

HISTORICAL BACKGROUND: 1923-1989

2.1. General Features of the Turkish Economy from 1923 to 1979

When the Turkish Republic was established in 1923, it inherited a quasi-colonial economic structure from the Ottoman Empire which was positioned in the world economy as a raw materials exporter and an industrial goods importer.¹⁰

Boratav described the last fifteen years of the Ottoman Empire by “timid first steps towards a national capitalism”.¹¹ However there were obstacles before these steps. Probably the most important bottleneck was the puniness of the Turkish bourgeoisie. Certainly, there was an “Ottoman” and a “Turkish” bourgeoisie within this backward economic structure. Ottoman bourgeoisie, the stronger one, was mainly consisted of non-Muslim elements (Greeks, Armenians, Jews and Levantines) of the society which was specialized in trade and especially in foreign trade rather than industry and thus had a comprador character. Turkish bourgeoisie, the delicate one, with its small and medium sized capital, was consisted of Muslim Turks who were focused on domestic commerce. This class was mainly dependent on the Ottoman bourgeoisie and had a scattered and unorganized structure.¹²

On the other hand, decades of war and destruction caused severe and long lasting demographic, social and economic changes.¹³ One of these changes was the dramatic decline in the Greek and Armenian population, one of the main pillars of the economy. This decline meant that many commercialized, export-oriented merchants, farmers, artisans, and money lenders had departed.¹⁴ Therefore, first years

¹⁰ Korkut Boratav, *Türkiye İktisat Tarihi: 1908-2002*, 9th ed., Ankara, İmge Kitabevi Yayınları, 2005, pp. 19-20.

¹¹ *Ibid.*, p. 21.

¹² *Ibid.*, pp. 23-24.

¹³ Roger Owen and Şevket Pamuk, *A History of Middle East Economies in the Twentieth Century*, London, I.B. Tauris & Co Ltd, 1998, p. 11.

¹⁴ *Ibid.*, p.11.

of the republic, passed with the efforts to fill the vacuum left by the non-Muslim Ottoman bourgeoisie. Muslims began to acquire the land and other assets of the departing Greeks and Armenians and eventually this group has constituted the nucleus of national bourgeoisie in the following years. In other words, this traditional fabric of the economy and the perishing of the Ottoman bourgeoisie paved the way for a period of creating a national Muslim Turkish bourgeoisie in care of the state after the foundation of the new Republic and during this period, the state played a critical role in determining the roadmap of the economy. Another change was a sharp decline in the levels of production. Agriculture, historically the backbone of the Turkish economy¹⁵, industry and mining were all adversely affected by the loss of human capital and by deterioration of crops, animals, equipment and manufacturing plants during the war years.¹⁶

As a result of these, the leadership that inherited such a decayed economy, embarked on an ambitious program for national development and state assumed the leading role in this process from then on. The first challenge emerged with the signing of Lausanne Peace Treaty which described the position and capabilities of the new Republic, in the international political and economic system. Despite its success in the political arena, Lausanne included some concessions that affected the economic policies. Firstly, the Ottoman external public debt was renegotiated and apportioned between the successor states. The Turkish government assumed two thirds of the total to be paid in gold sterling beginning in 1929.¹⁷ Secondly, free trade agreements which had been renewed periodically during the 19th century were discontinued but it was agreed that the existing structure of low tariff rates and restrictions against quotas would continue until 1929, when the new republic would be free to pursue its own commercial policies.¹⁸ All of these provisions prevented the leadership from an effective political shift that would lead to the increasing of tariff revenues or protecting the national economy from international competition.

¹⁵ Oktay Yenal, *Cumhuriyet'in İktisat Tarihi*, İstanbul, Homer Kitabevi, 2003, p.25.

¹⁶ Owen and Pamuk, *op.cit.*, p. 11.

¹⁷ Yenal, *op.cit.*, p. 57.

¹⁸ Owen and Pamuk, *op.cit.*, p. 13.

The political leadership was aware of the reality that the political independence was necessary but not sufficient for the economic independence.¹⁹ Thus, Turkey broke the chains of political dependency with the past in 1923 with Lausanne and economic dependency with the past in the 1930s, by the implementation of import substitution industrialization (ISI) policies.²⁰

Another important development in 1923 was the Izmir Economic Congress which was held shortly after the end of the Turkish War of Independence and while the negotiations was continuing in Lausanne Conference. The economic policy of the 1923-1929 period became evident in the Izmir Economic Congress in February-March 1923. In his opening speech in the Congress Atatürk said “There can be no political independence without economic independence and the national sovereignty has to be supported by economic sovereignty”. Actually this awareness and mentality reflected to the decisions taken at the Congress. Political leadership from Ankara, businessmen from Istanbul, agrarian landowners from Izmir and its surrounding, merchants and artisans from Anatolia and finally laborers mostly led by the industrial business circles participated to the Congress. The main purpose of the congress was to reach a compromise about the economy policies among these different interest groups. In other words, the Congress constituted a vital platform for the military-bureaucratic administrative cadres to actively and effectively communicate with the wealthy class of the society and to strengthen their political power via good relations and common vision with aforementioned portion of the society.²¹ According to the principles of the Congress, the economy was decided to be open, national capital was promoted and supported, foreign capital permitted as long as it contributed to economic development and a moderate protectionism directed to facilitate the national elements to get a grip of the economy.

¹⁹ Boratav, *op.cit.*, p. 23.

²⁰ Baskın Oran, “TDP’nin Kurumsal Çerçevesi”, in Baskın Oran, (Ed.), *Türk Dış Politikası: Kurtuluş Savaşından Bugüne Olgular, Belgeler, Yorumlar (1919-1980)*, Vol. I, 8th ed., İstanbul, İletişim Yayınları, 2003, p. 39.

²¹ Yahya Sezai Tezel, *Cumhuriyet Döneminin İktisadi Tarihi: 1923-1950*, 4th ed., İstanbul, Tarih Vakfı Yurt Yayınları, 2001, pp. 148-149.

Since the industrialization and creation of a Turkish bourgeoisie were viewed as key ingredients of the national economic development, an active policy of intervention was pursued in order to favor the private sector. In this framework, state took many steps to reach its aforementioned goals during the period between 1923 and 1929. First of all, not only some of the foreign owned enterprises, notably the railroads, started to be nationalized, but also new railroads that would connect the different parts of the Anatolia to each other was started to be built by the state. These steps can be considered crucial for the creation of an integrated domestic market within the borders of the new nation state.²² Second, state monopolies were transferred to private firms under favorable terms. This policy was considered as the most effective and prevalent method of creating national bourgeoisie.²³ Third, Turkey's first national bank, İşbank, was established in 1924 as a result of the urgent need for a national bank and a banking system that was capable of the financing means to back up economic activities, trigger industrial production, manage accumulated funds and extend resources. İşbank played an outstanding active role in the process of integration of the national and international capital with the political power. In addition, it constituted an effective pressure group to shape economic policy decisions in the view of capital circles.²⁴ Fourth, the government adopted a positive approach towards foreign capital, especially in the form of a partnership with domestic companies, with a view to increase investments and production. The then Minister of Economy, Mahmut Esat Bozkurt emphasized that "We will not hand over Turkey, or the Turkish Economy, as a country of slaves to foreign capital. However, we are prepared to recognize every kind of facility, even more than shown by other nations, to foreign capital, willing to live and earn in a legitimate manner, on condition that it conforms to our laws and regulations and is not granted more privileges than Turks."²⁵ Fifth, the burdensome and semi-feudal tithe was abolished

²² Owen and Pamuk, *op.cit.*, pp. 13-14.

²³ Boratav, *op.cit.*, p. 40.

²⁴ Boratav, *op.cit.*, p. 41.

²⁵ Coşkun Can Aktan, "Turkey: From Inward Oriented Etatism to Outward-Looking Liberal Strategy," *Turkish Public Administration Annual*, Vol. 17-19, 1991-1993, pp. 57.

in 1925. The tithe provided the means by which the state paid its debts and met its financial needs. For this reason, abolishing the tithe and liberating the peasants would have required restructuring of the taxation system.²⁶ Sixth, in 1927, the government enacted the Law for the Encouragement of Industry to foster and initiate private sector activities and provide financial support for investments. This Law offered a wide variety of incentives and subsidies to the industrial establishments.²⁷

Despite all these steps taken in an attempt to increase the industrial investments and production, the weak industrial structure of the Ottoman period was mainly preserved and continued without a structural change and state's industrial investments were almost non-existent.²⁸ Aforementioned restraints on the economy led to a limited success in this period. However, economy policies started to change profoundly after 1929. As mentioned before, Lausanne's limitations on customs tariffs come to an end in 1928 and hence implementing more protectionist customs policies and foreign trade regime became possible in 1929. Besides, Ottoman debts started to be paid in the same year. Apart from these developments, The Great Depression began in 1929 in the United States (US) and lasted until about 1939. It was the longest and most severe depression ever experienced by the industrialized Western world. Although the Depression originated in the US, it resulted in drastic declines in output, severe unemployment, and acute deflation in almost every country of the globe. The Great Depression affected the Turkish economy in a negative way largely through international trade. On the one hand foreign demand for Turkey's exports of raw materials and agricultural products sharply reduced; on the other hand the supply of industrial goods to Turkey fell dramatically during this period. As Keyder revealed that "turning points of the world economy are crucial, because at such junctures, particular local social groups and their political projects gain greater importance and help to determine the subsequent balance of forces."²⁹ Actually that

²⁶ Feroz Ahmad, *The Making of Modern Turkey*, London & New York, Routledge, 1993, pp. 42-43.

²⁷ Gülten Kazgan, *Tanzimattan 21. Yüzyıla Türkiye Ekonomisi: Birinci Küreselleşmeden İkinci Küreselleşmeye*, İstanbul, İstanbul Bilgi Üniversitesi Yayınları, 2002, p. 56.

²⁸ Boratav, *op.cit.*, p. 62.

²⁹ Çağlar Keyder, *State and Class in Turkey: A Study in Capitalist Development*, London & New York, Verso, 1987, p. 3.

was exactly what happened in the 1930s, in the case of Turkey. It was due to the Great Depression that economic reconstruction and retreatment of the merchant bourgeoisie, allowing bureaucratic control to achieve centrality.

These developments, influenced, enabled and also compelled Turkey to alter its economic policies and measures, to put an end to the period of “economic reconstruction in relatively open economic conditions”³⁰ and to enter a new period of “protectionist and etatist industrialism”³¹ until the Second World War. Under these harsh international conditions the Turkish bureaucracy took significant steps to put the state to the forefront of the economy.

Within this context, ideas supporting a state led industrialization gained prevalence and, state started to play an active role in the economy through an etatist policy.³² The radical changes in the international economic system and the backward structure of the national economy forced the bureaucracy to implement the import-substitution industrialization policies. Through this strategy, Turkey aimed at building national industrial capacity to replace imported goods with locally produced ones and this goal required a protected domestic market under higher customs walls. During this period, state assumed both the roles of investor, producer and manager and took on many tasks traditionally performed by the industrial fraction of the capitalist class.³³ Nevertheless, the etatist policies did not exclude the private sector, but rather encouraged and went hand in hand with the national, indigenous capitalist groups.³⁴

After 1930, the attitude towards the foreign capital started to change and a relatively negative mood was gained prevalence. As a result of this, most of the foreign investments, such as the main railways, utilities, transportation and port facilities, dozens of mines and factories were nationalized during 1930s. As Berberoglu stated, “the nationalization policy of the 1930s and early 1940s played an

³⁰ Boratav, *op.cit.*, p. 48-49.

³¹ *Ibid.*, p. 59.

³² Meliha Benli Altunışık and Özlem Tür, *Turkey: Challenges of Continuity and Change*, London, Routledge, 2005, p. 68-69.

³³ Boratav, *op.cit.*, p. 68.

³⁴ Altunışık and Tür, *op.cit.*, p. 69.

important role in strengthening the Turkish economy. It virtually ended the outflow of capital, hence improving the country's balance of payments, and, with the expansion of the state into different branches of the nation's industrial economy, it opened the way to state planning to increase production and to accelerate the process of independent capitalist industrialization".³⁵ In addition to the nationalization of foreign owned investments, the policy of transferring some state monopolies to privileged companies, as it happened in the 1920s, was abandoned. State entrepreneurship mainly took the form of establishment of new productive enterprises, but from time to time nationalization of the privately owned enterprises took place.³⁶

In this context, the first five-year industrialization plan came into effect in 1934. This document consisted of a detailed list of investment projects to be undertaken by the state economic enterprises but did not provide a macroeconomic framework.³⁷ The first plan aimed to substitute imports of consumption goods by domestic production. In this framework, priority given to textile, mining, paper, chemistry, glass and cement sectors. As a result, the industrial production mainly based on agricultural products and natural resources. By 1936, a second five-year industrialization plan was designed but it could not be implemented because of the Second World War. Unlike the first one, this plan gave priority to the production of intermediate and investment goods³⁸ which was produced in the second phase of the import-substitution industrialization.

During the 1930s economic growth gained momentum and the economy experienced major structural changes in comparison with the 1920s. State's intervention in the economy, not only as regulator but also as producer, grew substantially. A number of State Economic Enterprises (SEEs) were established and production activities were started. Turkey achieved a brilliant success during this

³⁵ Berch Berberoglu, *Turkey in Crisis: From State Capitalism to Neo-colonialism*, London, Zed Press, 1982, p. 37.

³⁶ Boratav, *op.cit.*, p. 70-71.

³⁷ Owen and Pamuk, *op.cit.*, p. 18.

³⁸ Altunışık and Tür, *op.cit.*, p. 69.

period. Despite very tough conditions, Turkey developed swiftly and steadily on the basis of its own sources without getting any external debt or aid, while discharging its share of Ottoman debts.³⁹ As a result of the protectionist and etatist policies, the dependency of Turkish economy on the world economy decreased in the 1930s. However, the situation changed dramatically after the Second World War.

The beginning of the Second World War signalled an end to the state-led import substitution industrialization period. Although Turkey did not enter the war, full-scale mobilization had maintained during the entire period. The sharp decline in imports and the canalization of large resources for the maintenance of the army placed enormous strains on both industry and agriculture.⁴⁰ Because of the insufficiency of necessary inputs, the industrial and agricultural production declined.⁴¹

Under these circumstances, the priorities and concerns of etatism were quickly pushed aside; planning efforts and industrial investments were utterly postponed. In this context, wartime years can be described as an “interruption” of industrial development and growth process.⁴² Thus, the five-year industrialization plans were discontinued and the struggle with wartime scarcities, shortages and profiteering became the order of the day.⁴³ During the Second World War, commercial bourgeoisie and capitalist large landowners accumulated enormous capital and wealth through profiteering, speculation and black market.⁴⁴

In 1942, against these ill-gotten gains, high inflation and to create revenue, the government imposed Wealth Levy, a one-off tax without the right of objection, on leading merchants, industrialists and other businessmen in the large urban

³⁹ Kemal Kurdaş, *Bitmeyen Gaflet ve Türkiye Ekonomisinin Çöküşü*, Ankara, METU Press, 2003, p. vii.

⁴⁰ Owen and Pamuk, *op.cit.*, p. 24.

⁴¹ Morris Singer, “The Economic Performance of the Turkish Republic,” *Middle Eastern Studies*, Vol. 20, No. 4 (October 1984), pp. 156-157.

⁴² Boratav, *op.cit.*, p. 81.

⁴³ Owen and Pamuk, *op.cit.*, p. 25.

⁴⁴ Baskın Oran, “Dönemin Bilançosu: 1939-1945”, in Baskın Oran, (Ed.), *Türk Dış Politikası: Kurtuluş Savaşından Bugüne Olgular, Belgeler, Yorumlar (1919-1980)*, Vol. I, 8th ed., İstanbul, İletişim Yayınları, 2003, pp. 388-392.

centers.⁴⁵ Although the text of law prepared on the basis of non-discrimination, more than half of the tax collected from the non-Muslim groups of the bourgeoisie.⁴⁶ Consequently, Wealth Levy can be summarized as a liquidation operation of non-Muslim bourgeoisie and as an unjust and rapidly enrichment of the Turkish bourgeoisie; in other words relocation of capital in accordance with the nationalization of the economy. Although the tax revenue was remained nearly half of the Wealth Levy, state imposed another emergency tax -Agricultural Products Tax- to acquire the rapidly increasing agricultural profits in 1944.⁴⁷ In conjunction with the existing class structure, wartime developments caused extraordinary changes in income distribution. As a matter of fact, these transformations played a determining role on the economic, social and political developments after the war. The last years of the war witnessed further instances of alienation between the state bureaucracy and bourgeoisie, especially the industrial bourgeoisie voiced its discontent at the earliest opportunity.⁴⁸

After the Second World War, domestic and international forces combined to bring about radical political and economic changes in Turkey.⁴⁹ Domestically, a new group of trading entrepreneurs arose during the wartime and this group with the large landowners formed the core of new political elite that established the Democrat Party (DP) in 1946 and came into power in 1950. In other words, changes in the economic and social structures and power relationships required shifts in the political power structure. The commercial bourgeoisie, the large landowners, the small-town merchants and the small private-sector industrialists made up the social bases of the DP which was formed internally from within the ruling elite. As Pamuk and Owen put forward clearly, this commercial and industrial bourgeoisie, as well as the larger, market-oriented producers in the countryside many of whom had benefited from the wartime opportunities, began searching for alternatives to etatism and government

⁴⁵ Faik Ökte, *Varlık Vergisi Faciası*, İstanbul, Nebioğlu Yayınevi, 1951, pp. 35-38.

⁴⁶ Oran, *op.cit.*, p. 392.

⁴⁷ Boratav, *op.cit.*, p. 85.

⁴⁸ Keyder, *op.cit.*, pp. 113-114.

⁴⁹ Owen and Pamuk, *op.cit.*, p. 104.

interventionism⁵⁰ and searching for ways to come into power with increasing desire.⁵¹ Besides domestic factors, international pressure also played an important role in the shaping of new policies. The emergence of the US as the hegemonic power after the Second World War shifted the balance of power to a more liberal and open economic model with a more open political system.⁵²

Thus, 1946 became a turning point in the political and economic history of the modern Turkey. After the end of Second World War, widely criticized single-party rule came to an end and multi-party electoral system was adopted in the same year. In this framework, one of the main debates revolved around the role of the state in the economy and the discussion resulted in a redefinition of etatism.⁵³ Within this context, policies which were based on a closed, protectionist, inward-looking economy and were implemented continuously since the 1930s, eased gradually. Imports increased via liberalization of import regime, foreign trade deficits started to become chronic and therefore foreign aid, loans and investments became crucial for the survival of the economy. During this period, as a result of a liberalized foreign trade regime, an outward looking industrialization program based on agriculture, mining and construction sector was adopted.⁵⁴

Turkey became a member of the International Monetary Fund (IMF), the World Bank (WB) and the Organization for European Economic Cooperation (OEEC) in the framework of the Marshall Plan in 1947. As a part of the “free world”, Turkey became eligible for grants and aid in exchange for political and military dependence with economic liberalization. When the DP came into power, for the first time in the history of the republic, international credit and aid was accrued in the budget through the Marshall Plan.⁵⁵ After these memberships a new

⁵⁰ *Ibid.*, p. 26.

⁵¹ Cem Eroğul, *Demokrat Parti: Tarihi ve İdeolojisi*, 2th ed., Ankara, İmge Kitabevi, 1990, p. 46.

⁵² Owen and Pamuk, *op.cit.*, p. 105.

⁵³ Altunışık and TÜR, *op.cit.*, pp. 69-70.

⁵⁴ Boratav, *op.cit.*, p. 94.

⁵⁵ Altunışık and TÜR, *op.cit.*, p. 70.

thinking of impossibility to develop without foreign aid started to gain prevalence in the bureaucratic circles day by day.⁵⁶

Contrary to popular wisdom, DP's coming into power in 1950 did not change the policies and the orientation of the economy or the foreign economic relations. In fact, the real turning point came in 1947 when the Republican People's Party decided to implement the third five year plan which began to move in the direction of greater reliance on private capital and greater emphasis on agriculture.⁵⁷ But the DP pursued the same path with greater enthusiasm once they came into power. As indicated in the party program, the DP tried to reduce the state involvement in the economy in general and in the production in particular and the priority given to the agriculture, infrastructure and the private sector.⁵⁸ Furthermore, DP's Minister of Economy and Trade said that the government would take all basic economic decisions in collaboration with the business circles in one of his first statements.⁵⁹

During 1946-1953 period, Turkey tried to integrate into the world economy on the basis of agricultural and raw materials specialization, economic growth mainly stemmed from agricultural growth. During this period the DP governments introduced a series of regulations with respect to open up the economy and to support the industrial sector. For example, in order to facilitate long term internal and external credits and technical assistance for private sector, Industrial Development Bank was founded by the government in 1950.⁶⁰ In the early years of the 1950s, foreign capital was encouraged and the integration of the domestic capital with foreign capital via joint ventures was supported. In 1954, the Law for the Encouragement of Foreign Capital made it possible for foreign capital to invest in Turkey with virtually no restrictions and to enter into joint ventures with Turkish companies. According to this Law, all areas of the economy, which were already opened to Turkish private initiative, were also opened to foreign capital; foreign

⁵⁶ Boratav, *op.cit.*, p. 96.

⁵⁷ Owen and Pamuk, *op.cit.*, p. 106.

⁵⁸ Eroğul, *op.cit.*, p. 13.

⁵⁹ Altunışık and Tür, *op.cit.*, p. 70.

⁶⁰ Altunışık and Tür, *op.cit.*, p. 70.

investors was not obliged to go into partnership with native capital; foreign corporations operating in Turkey may repatriate all of their profits to their home country, add to their principal investment, or invest in another corporation of their own choice.⁶¹ Moreover, with the introduction of the Petroleum Law, oil exploration activities in Turkey were opened up to both domestic and foreign private companies in 1954.

During the second term of the DP rule, economy policies started to change. In Owen and Pamuk's words, with the balance of payments crisis of the mid-1950s, the move towards a more open economy came to an end. Amidst the shortages and bottlenecks, domestic industry began to produce some of the goods, especially the consumer goods, which had been imported a few years ago. As a result, while the share of consumer goods in imports was decreasing, the shares of investment and intermediate goods increased during this period. Although implemented implicitly, the 1950s witnessed a return to the ISI policies which arose from necessity.⁶²

Because of high current account and budget deficits, the difficulties in gaining external aid or loans and challenges of financing the deficits, foreign trade regime started to be controlled and protected. Concordantly, the accumulation of private capital and the creation of a national bourgeoisie continued strongly. Although the party committed exactly the opposite during elections, in addition to private investments, public investments increased rapidly under a relatively closed economy. From then on, indicators marked industrial sector instead of agriculture. As Zürcher emphasized, the DP succeeded in modernizing Turkish agriculture to a certain extent and they vastly increased the industrial base of the country.⁶³ The majority of the large industrial firms of present-day Turkey have their roots in the 1950s.

Throughout the 1950s, as a natural consequence of these policies, Turkish private sector developed considerably. In other words, the 1950s witnessed, *inter*

⁶¹ Kazgan, *op.cit.*, p. 83.

⁶² Owen and Pamuk, *op.cit.*, p. 109.

⁶³ Erik Jan Zürcher, *Modernleşen Türkiye'nin Tarihi*, 16th ed., İstanbul, İletişim Yayınları, 2003, p. 326.

alia, to the increasing political differentiation of the capitalist class and its growing independence from the state bureaucracy or the bureaucratic bourgeoisie. Thus in 1952, The Union of Chambers and Commodity Exchanges of Turkey (TOBB) was established. Private sector organized and came together under the TOBB and it became the highest legal entity in representing the private sector and submitting the private sector's opinions and comments to the political power. Besides, developing private business, the labor force also increased during this period. Confederation of Turkish Trade Unions (TÜRK-İŞ) was established in 1952, at a time when the right to strike and voluntary collective bargaining were not yet exercised in the country despite the promises of the DP during the elections.⁶⁴

By the late 1950s, Turkey's economic situation gradually deteriorated; agricultural production declined, prices and inflation began to rise, imports increased while the exports were decreasing, as a result trade gap widened, foreign and gold reserves decreased, increasing foreign debt and interest burden led to a balance of payment crisis. Being caught in a trap and not being able to find a solution, in 1958 the DP government could not even pay the debts and carry out foreign trade. By this way, the government obliged to ask for assistance from the IMF and adopted the stabilization program, a forerunner of the IMF packages of the 1970s and 1980s, imposed by the IMF in exchange for the extension of additional credits.⁶⁵

Together with the worsening economic crisis, increasingly repressive methods of the DP government, mounting social discontent and unrest led to a military coup on 27 May 1960 and adoption of a new constitution subsequently. Since the crisis of the late 1950s stemmed from the absence of long term perspective, planning and coordination in the economy, the 1960s started with planning. This urgent need was also recognized in the 1961 constitution. As designated by the Article 129 of the new constitution, from then on economic, social and cultural development is to be carried out within plans and development is to be realized according to this plan.⁶⁶ As a result, in 1960 the new regime quickly established the

⁶⁴ Altunışık and Tür, *op.cit.*, p. 71.

⁶⁵ Altunışık and Tür, *op.cit.*, p. 72.

⁶⁶ Yenal, *op.cit.*, p. 86.

State Planning Organization (SPO) in order to materialize planning activities in a professional and a more technocratic way. In this regard SPO started to work on development plans without delay and in 1963 first five-year development plan was introduced. In this first development plan Turkish economy was named as a mixed economy where the state and the private sector work together and the ISI was adopted and institutionalized as the main strategy for development and industrialization.⁶⁷ Thus the new regime embarked on an economic development strategy of inward-oriented growth based on protectionism and import substitution.⁶⁸

Just like the 1920s and 1930s, in order to replace imported goods, especially consumer goods, with locally produced ones, import-substitution industrialization was implemented behind protectionist walls. But unlike the 1920s and 1930s, this time durable consumer goods such as refrigerators, ovens, consumer electronics and cars, started to be produced rather than basic consumer goods such as flour, sugar and weaving, namely “three whites”.⁶⁹ In fact, as a result of the division of labor between the state and the private sector, large-scale intermediate goods investments was done by the state and the relatively low-tech and profitable consumer goods investments was done by private sector under high protection.⁷⁰

State intervention in the accumulation process materialized in the forms of tariffs or subsidies. Moreover, through supplying intermediate goods that was produced by the state economic enterprises like iron and steel, copper, aluminum, petro-chemicals and chemicals to the private sector at lower prices, state contributed to the national economic development as well.⁷¹ Thus, the state was playing a crucial role in the ISI and it was giving great power to the state officials or the bureaucratic bourgeoisie regarding the allocation of resources. On the other hand, contrary to industrial sector, agricultural sector was mainly left aside in the development plans. For example, in the second five year development plan (1968-1973) industrialization

⁶⁷ Altunışık and Tür, *op.cit.*, p. 73.

⁶⁸ Boratav, *op.cit.*, p. 118.

⁶⁹ Boratav, *op.cit.*, p. 119.

⁷⁰ Altunışık and Tür, *op.cit.*, p. 73.

⁷¹ Boratav, *op.cit.*, p. 120.

was equaled to economic development. As a consequence, the traditionally agricultural economy started to shift towards industry and during this period industry sector developed faster than agriculture.⁷²

In the 1960s, as a result of the ISI policies, high rates of growth could be achieved and high rates of growth especially in the industrial production were accompanied by an increase in the size of the working class. 1960s and 1970s became a milestone in the working class movement in Turkey, not only in terms of many legal obtained rights, but also in terms of growing class-consciousness and unionization. This process and the rising dissatisfaction with the policies and actions of the TRK-İŞ leadership and militancy in the working class movement in particular led to establishment of Confederation of Revolutionary Trade Unions (DİSK) in 1967.

In parallel with workers activities towards organization, employer associations have been organized in real terms only after the 1961 Constitution. In this context, in 1961 six employer associations of Istanbul (Metal, Glass, Wooden Products, Textile, Printing and Food Industry Employers' Associations of Istanbul) were organized under the title of Union of Istanbul Employer Associations. One year later, after completing its nationwide organization, the name of the Union was changed to the Turkish Confederation of Employer Associations (TİSK) in 1962. From the very beginning, TİSK sought to work as a pressure group through monitoring the activities of the legislative, executive and judicial bodies of the state and establishing relations with the political parties, opposing groups, the press and universities. In order to protect the interests of the industry, to influence the bureaucracy and to accomplish these objectives, TİSK transferred its headquarters from Istanbul to Ankara in 1965.⁷³ In such an environment, Turkey's elite industrialists and key conglomerates⁷⁴ were also came together and established

⁷² Altunışık and Tr, *op.cit.*, p. 74.

⁷³ <http://www.tisk.org.tr/hakkinda.asp?id=498>, internet access: 18.10.2011.

⁷⁴ Vehbi Koç, Sakıp Sabancı, Nejat Eczacıbaşı, Osman Boyner, Selçuk Yaşar, Raşit Özsaruhan, Ahmet Sapmaz, Feyyaz Berker, Melih Ozakat, İbrahim Bodur, Hikmet Erenyol were the founders of the TUSIAD.

Turkish Industrialists' and Businessmen's Association (TÜSİAD) in 1971.⁷⁵ The foundation of TÜSİAD was a milestone in the sense that it represented the first voluntary association of businessmen in Turkey.⁷⁶ Previously, the whole of the business community, regardless of size, had been represented solely by a semiofficial organization, TOBB. Since the TOBB was designed according to corporatist aims as a mechanism of the state, it was trying to balance the business and the working sectors' interests. In a similar vein with the establishment of DİSK, TÜSİAD was established as a reaction to the failure of the TOBB to protect the interests of business segments. Furthermore, the foundation of TÜSİAD marked the emergence of big business as a crucial political actor in Turkey in terms of both defending its collective interests against other segments of society and for the first time expressing a collective concern about the political, economic and social problems of the country as a whole.⁷⁷ By this way, the big industrial bourgeoisie substituted for the big commercial bourgeoisie concerning the leadership of the capitalist class through ISI.

The country achieved a rapid growth in the industry in particular and in the economy in general. However, the dependency of economic growth on imports remained unchanged and this structure of the economy led to the bankruptcy of ISI. Since this rapid economic growth required high levels of energy consumption and oil imports, the twin oil crises of the 1970s further worsened the situation. Heavy reliance on imports and disequilibrium between imports and exports caused a high current account deficit.

Because of the protective measures inherent in the ISI, like extensive import restrictions, high protective tariffs and an artificially overvalued Turkish Lira, the industry did not face with a competitive pressure. Because of an easygoing bourgeoisie in a domestic market under heavy protection without foreign competition and export impetus from within, exports could not be raised during the period and remained minimal. Throughout the period, the ratio of imports covered by exports

⁷⁵ <http://www.tusiad.org/tusiad/founders-of-tusiad/>, internet access: 18.10.2011.

⁷⁶ Ziya Öniş and Umut Türem, "Entrepreneurs, Democracy, and Citizenship in Turkey," *Comparative Politics*, Vol. 34, No. 4 (July 2002), p. 442.

⁷⁷ *Ibid.*, p. 442.

decreased steadily while imports were increasing. In fact, while the structure of the production was shifting from agriculture towards industry, the traditional structure of exports which was mainly relied on agricultural products remained unchanged during the period.⁷⁸ In other words, economy could not achieve the “takeoff” phase of the ISI.

Therefore, in order to meet the foreign currency demand and manage balance of payments problems, the government chose to search for external financing instead of increasing exports. During the 1960s, as a result of the positive course of international economy, the Cold War and the privileged status of the country, external financing could be possible, but with the deterioration of the international economy, borrowing became harder and harder. In addition, as one of the most important external source of the economy and item of narrowing the foreign trade gap, remittances started to decrease by the late 1970s. Actually, rising remittances through the early 1970s cut both ways. Despite the positive effects of remittances on narrowing the trade gap and budget deficit; it also paved the way for neglecting and underestimating the importance and necessity of policies directed to increase exports. Besides, increase in military spending, economic and political incubus of Cyprus operation, arms sale embargo and cutting off military aid by the US put an additional burden on the balance of payments.⁷⁹ Thus, by the late 1970s the government fell into the vicious cycle of short-term borrowing and external financing. As a consequence the economy’s ability to earn foreign exchange became the Achilles’ heel of the ISI.

Moreover, as the financial dependence on external sources increased, economic and social decay gain prevalence. Since the foreign reserves were held and allocated largely by the government, rather than industrial and commercial qualities, the influential contacts or access to the right bureaucrats in the state apparatus became vitally important in order to get the necessary funds to continue the production and to survive. In addition, the gap between supply and demand led to the

⁷⁸ Boratav, *op.cit.*, pp. 120-136.

⁷⁹ Baskın Oran, “Dönemin Bilançosu: 1960-1980”, in Baskın Oran, (Ed.), *Türk Dış Politikası: Kurtuluş Savaşından Bugüne Olgular, Belgeler, Yorumlar (1919-1980)*, Vol. I, 8th ed., İstanbul, İletişim Yayınları, 2003, pp. 663-664.

exacerbation of already high inflation, deep-rooted income inequalities and rural to urban migration resulted in unrest and arduous problems in the labor market.

By the late 1970s, ISI was in deep trouble and the IMF programs for the ailing Turkish economy brought no cure. All the government changes and measures taken were not enough to provide the necessary economic, social and political conditions for getting the ISI back on the rails. The combination of the structural deficiencies of the ISI and the inefficiencies of the rapidly changing governments to bring solutions signalled the end of a period. Between 1977 and 1979, economic crises deepened and crystallized rapidly. Foreign trade indicators swiftly deteriorated, internal and external channels of financing came to a deadlock, economic growth almost stopped, scarcity and black market gained prevalence, inflation exacerbated, in such an environment broker-commercial profits and ill-gotten gains rose, wage-profit relation in the industry turn in private capital's favor and distribution of income worsened.⁸⁰ The economic crisis coupled with the continuing political turmoil brought the country to the brink of a civil war.⁸¹ Under these circumstances, the real package that would restructure the whole economy, society and policy came along with 24 January 1980 Decisions and 12 September 1980 coup d'état.

2.2. Turkey's Political and Economic Relations with Iran from 1923 to 1979

Political relations between Turkey and Iran started while the War of Independence was continuing and Iran recognized Turkey on June 1922. Despite Iran was among the first countries that recognized Turkey, the relations between Turkey and Iran remained problematic for a long time.

The regimes, which were established by the leadership of Atatürk in Turkey and by the leadership of Reza Khan in Iran, were very similar concerning their objectives and this created a positive environment in both countries. Atatürk's Turkey was a kind of a model for the Shah's Iran. Despite this positive atmosphere, it

⁸⁰ Boratav, *op.cit.*, pp. 139-147.

⁸¹ Owen and Pamuk, *op.cit.*, p. 115.

was not possible to paint a rosy picture for all affairs between Turkey and Iran. There existed a border issue which was the real problem between the two neighboring countries. Border dispute grew out not because of territory demand, but because of security problem that was created by the Kurdish groups living in the common border line.⁸² After the foundation of the republic in Turkey and the Pahlavi dynasty in Iran, in order to dissolve border disputes and arrange the bilateral relationship in accordance with the new circumstances, a friendship and security agreement was signed between Turkey and Iran in April 1926. Because of being the first legal document signed between parties and setting ground for subsequent agreements, the 1926 Agreement was of great importance. However it could not solve the problems and this problem almost led to the rupture of diplomatic relations. Therefore, an additional protocol to the 1926 Agreement was signed between parties in 1928. For the first time, through this document the purpose of developing economic relations between parties was included in a legal document.⁸³ Within the scope of the one of these protocols, parties agreed to arrange and develop the economic relations between them as soon as possible and recognized the freedom of transit over their territories.⁸⁴ The other protocol covered the policy and security issues. Despite these two protocols, the border dispute remained unsolved until 1932 when parties finally reached an agreement. Two different agreements a friendship agreement and a security, neutrality and economic cooperation agreement were signed in 1932. Through the second agreement, which came into effect in July 1935, the two countries gave the most favored nation (MFN) status to each other.⁸⁵ This MFN clause had positive implications not only on political but also economic issues. Following the signing of the 1932 Agreement, the most shining era of the relations started and the way for signing the Sadabad Pact was opened. After prolonged

⁸² Atay Akdevelioğlu and Ömer Kürkçüoğlu, “İran’la İlişkiler: 1923-1939”, in Baskın Oran, (Ed.), *Türk Dış Politikası: Kurtuluş Savaşından Bugüne Olgular, Belgeler, Yorumlar (1919-1980)*, Vol. I, 8th ed., İstanbul, İletişim Yayınları, 2003, pp. 360-363.

⁸³ Melek Fırat, *İran İslam Devrimi ve Türk-İran İlişkileri: 1979-1987*, Unpublished M. Sc. Thesis, Ankara, Ankara Üniversitesi Sosyal Bilimler Enstitüsü, p. 49.

⁸⁴ **22.04.1926 Tarihli Türkiye-İran Muahedenet ve Emniyet Muahedenamesine Merbut Protokol**, <http://ua.mfa.gov.tr/detay.aspx?826>, internet access: 26.10.2011.

⁸⁵ Akdevelioğlu and Kürkçüoğlu, *op.cit.*, p. 363.

negotiations, Turkey, Iran, Iraq and Afghanistan signed the Sadabad Pact in 1937. This pact is a friendship and non-aggression pact in essence. Nevertheless, this positive atmosphere deteriorated as the war stepped up and the pact could not survive the challenge of the Second World War. From the Anglo-Soviet occupation of Iran in 1941 to the 1947, the relations between Turkey and Iran was *de facto* frozen and both of them had to deal with their own strategic problems at regional and international levels. After the invasion, Reza Shah was obliged to leave his throne on behalf his son Mohammed Reza Pahlavi.

From the establishment of the Republic to the end of the Second World War, despite some problems, political relations between Turkey and Iran were generally cordial; but economic relations during the same period were very limited. These limited economic relations can be easily observed from the trade figures. From 1923 to 1945, Turkey's trade with Iran displayed a downwards tendency. Throughout these years fluctuations were observed together with significant rise in the second half of the 1920s, yet these did not change the general downward tendency of bilateral trade between Turkey and Iran. Exports which were around \$35 thousand in 1923 came to a halt in 1945, whereas imports shrunk from \$381 thousand to \$7 thousand. In the period, Iran's share in Turkey's total foreign trade remained limited. During 22 years, Iran's share in Turkey's exports was 0.03% whereas Iran's share in Turkey's imports was 0.34%. Except for a few years, there was always a deficit in favor of Iran. Goods that were subject to trade between Turkey and Iran reflected the structure of Turkish economy; Turkey was exporting agricultural goods and limited amounts of minerals to Iran whereas Iran was exporting a single item -oil- to Turkey.

In the same period, Turkey's total imports and exports increased despite fluctuations. In this context, between 1923 and 1945, exports increased 5 times from \$51 million to \$168 million and imports increased from \$87 million to \$97 million. Continual current account deficit from 1923 started to give surplus from 1930 to 1945 except for \$4 million deficit in 1938. Together with statist-protectionist policies, imports and exports experienced a reduction in the first half of the 1930s and the lowest import and export figures are observed in 1932. That year, exports decreased to \$48 million whereas imports decreased to \$41 million. However,

towards the verge of World War II, both imports and exports increased. Within this period, the highest figures were observed in 1943; exports and imports reached to \$197 million and \$155 million respectively.

The new international environment which was formed after the Second World War and rising interests of the US in the region had their reflections on Turkish-Iranian relations. Although the entire Middle East was affected by the Cold War, the first states of the region to be drawn into superpower rivalry were Turkey and Iran, the immediate neighbors of the Soviet Union.⁸⁶ As a part of its policy of containment, the US provided economic and military assistance to Turkey and Iran and gained force in the domestic and foreign policy considerations of these countries.

The disappearance of the residues of the war paved the way for revival of bilateral relations in 1948. However, following Mohammed Musaddeq's came into power in 1950 led to a further cooling of relations between Turkey and Iran. From 1949 on, sentiment for nationalization of Iran's oil industry grew and this sentiment culminated in the nationalization of the oil industry in 1951 under the leadership of Musaddeq, but this initiative created discontent in Turkey. During this process Turkey took side with Britain in particular, with West in general and even abided by the decision of the Britain to impose worldwide embargo on the purchase of Iranian oil.⁸⁷ As a result, during this short period, mutual criticism in the press of both countries was a repeated feature of the period⁸⁸ and bilateral relations continued at its lowest ebb. Nevertheless, after the overthrow of Musaddeq in a coup d'état orchestrated by the British and American intelligence agencies in 1953, bilateral relations mended again. In this framework, Iran participated into the Baghdad Pact which was signed by Turkey and Iraq in February 1955. Great Britain acceded to the agreement just over a month later, while Pakistan and Iran joined in September and November, respectively. The United States supported but did not join

⁸⁶ William L. Cleveland, *A History of the Modern Middle East*, 3rd ed., Colorado & Oxford, Westview Press, 2004, p. 275.

⁸⁷ Atay Akdevelioğlu and Ömer Kürkçüoğlu, "İran'la İlişkiler: 1945-1960", in Baskın Oran, (Ed.), *Türk Dış Politikası: Kurtuluş Savaşından Bugüne Olgular, Belgeler, Yorumlar (1919-1980)*, Vol. I, 8th ed., İstanbul, İletişim Yayınları, 2003, p. 650.

⁸⁸ Gökhan Çetinsaya, "Essential Friends and Natural Enemies: The Historic Roots of Turkish-Iranian Relations," *Middle East Review of International Affairs*, Vol. 7, No. 3 (September 2003), p.126.

the alliance to draw reaction from neither Israel nor Egypt. However, the pact which was established with a view to protect and defend Middle Eastern countries against the USSR, did not come up with expected results and did not live long. This alliance took first death blow in 1958 and the second in 1979. After the revolutionary coup d'état in Iraq and overthrow of the pro-western regime in 1958, Iraq formally withdrew from the Baghdad Pact in 1959 and the pact was reconstructed as an alliance of Britain, Turkey, Iran and Pakistan, under the name of Central Treaty Organization (CENTO) in the same year.⁸⁹

Despite being in the same defense organization, the relations between Turkey and Iran could not reach sufficient levels. Because both of them took part in the same organization with a view to get more assistance and support from the West rather than developing and strengthening the bilateral relations on the grounds of long term common interests or goals. For this reason, bilateral relations were shaped largely by the guidance of US and Western Block.⁹⁰

Bilateral trade figures with Iran also reflected the pattern of limited and insufficient relations between 1946 and 1959. During this period, Turkey's exports remained stable while the imports from Iran jumped 31 times. Between 1948 and 1951, imports increased to \$4.5 million level on an annual average basis. In the same years, according to the disequilibrium between imports and exports, trade deficit has surged to its highest levels. However, in the rest of the period, imports were almost nonexistent like exports. Throughout the period bilateral trade developed to the detriment of Turkey and trade deficit bounced from \$77 thousand in 1946 to \$3 million in 1959. When the share of Iran in Turkey's trade is considered, like 1923-1945 period, its share in total imports and exports was little if any. During these years, Iran's share in total exports did not change from the previous period and realized in 0.03%, and although increased 0.2%, its share in total imports limited

⁸⁹ William M. Hale, *Turkish Foreign Policy: 1774-2000*, London, Frank Cass, 2000, p.127.

⁹⁰ Rouhallah K. Ramazani, *The Northern Tier: Afghanistan-Iran-Turkey*, Princeton, Van Nostrand, 1966, pp. 60-62.

with 0.52%. During the 1950s, nearly all of the Turkey's imports from Iran composed of oil.⁹¹

In the same period both total imports and exports of Turkey increased due to the attempts of opening up the economy. Since the rate of growth in imports exceeded the growth in exports, a persistent foreign trade deficit can be seen from 1947 to the end of the period. Throughout the period, exports doubled and increased from \$215 million to \$354 million; imports quadrupled from \$119 million to \$470 million, thus \$96 million trade surplus turned into a \$116 million deficit by 1959.

After coup d'état of 1960 in Turkey, bilateral relations with Iran progressed further. As a result of the detente in the international system and positive atmosphere in the bilateral relations, the economic and cultural aspects of CENTO came to the fore, while the political and military aspects of the organization were declining. In this context, the three member states of the CENTO, Turkey-Iran and Pakistan had also attempted to give their relationship a stronger economic dimension by setting up an organization for Regional Cooperation and Development (RCD) in 1964, the forerunner of the Economic Cooperation Organization (ECO).⁹² After the establishment of RCD, relations were developed via this channel rather than CENTO. Under the RCD, parties decided to import products from each other rather than elsewhere, if the other's products were proper in terms of price and quality. Moreover, proposals such as establishment of a joint oil company, a joint shipping company, and joint factories were brought forward in the framework of RCD, but as a result of disagreements, these projects could not be realized. In addition, through bilateral meetings of RCD, Pakistan and Iranian Airlines decided to start Istanbul flights in 1966⁹³ and the obligation of holding passport was lifted and passengers started to use tourist cards in the same year.⁹⁴ Although the parties strived to develop new projects or produce mutually complementary products, the volume of trade did not improve as it was expected. So much so that, Iran did not supply its foodstuff

⁹¹ *Milliyet*, 02.08.1957, <http://gazetearsivi.milliyet.com.tr>, internet access: 27.10.2011.

⁹² Hale, *op.cit.*, p. 127.

⁹³ *Milliyet*, 02.12.1965, <http://gazetearsivi.milliyet.com.tr>, internet access: 28.10.2011.

⁹⁴ *Milliyet*, 03.02.1966, <http://gazetearsivi.milliyet.com.tr>, internet access: 28.10.2011.

demand from Turkey which was both its immediate neighbor and a prominent exporter of agricultural commodities.⁹⁵ Since the RCD put the emphasis on developing common policies regarding the resource allocation, making joint investments and realizing domestic industrialization in a mutually complementary way and did not deal with the tariff and non-tariff barriers to trade⁹⁶, the volume or composition of the bilateral trade did not change considerably. In short, during 1960s, despite the “traditional friendship” between Turkey and Iran was frequently emphasized, this friendship did not reflected on the political and economic relations literally.

During 1960s, despite increases in Turkey’s total exports and imports, bilateral trade with Iran followed an undulant trend. In 1960 and 1961, exports to Iran rose to \$4 million and \$5 million respectively, but in 1962 and 1963 exports nearly stopped and again increased to \$7 million and \$5 million in 1968 and 1969. The same pattern can be seen in the imports. In 1960 imports were almost nonexistent, but increased sixfold to \$3 million and fivefold to \$14 million in 1961 and 1962 respectively and reached its highest levels in 1963 with \$15 million. After this year imports started to decrease and between 1965 and 1968 imports were nearly halted, but again in 1969 it rose to \$1 million. In this framework, the highest volume of trade was reached in 1963 with \$15.2 million, while the lowest figures occurred in 1967 with \$248 thousand throughout the 1960s, the average share of Iran in Turkey’s foreign trade increased slightly and its share in both exports and imports reached 0.7%. As a result of the ISI policies implemented during the 1960s, Turkey’s energy consumption and demand started to increase. In this framework, neighboring Iran came to the fore to satisfy Turkey’s demand for energy, but rising energy prices boosted Turkey’s import bill. Nevertheless, bilateral trade could not be step up and a sustainable and steady increase in exports and imports could not be achieved.

In the same period, Turkey’s total exports and imports showed steady increases and both of them doubled. Exports rose from \$321 million to \$537, while imports rose from \$468 million to \$801 million. Consequently, volume of foreign

⁹⁵ Firat, *op.cit.*, p. 55.

⁹⁶ *Milliyet*, 10.07.1970, <http://gazetearsivi.milliyet.com.tr>, internet access: 28.10.2011.

trade increased and for the first time in republic's history exceeded \$1 billion. However, the average rate of imports covered by exports decreased from 82% in the 1945-1959 period to 69% in the 1960s. Besides the traditional structure of the exports based on agricultural sector was largely preserved, exports of industrial goods started to increase slowly. According to the International Standard Industrial Classification (ISIC) of all economic activities, during the 1960s, the share of agriculture in exports was 75%, the share of industry was 20% and the share of mining was 5% on an annual average basis. On the imports side, according to the Classification by Broad Economic Categories (BEC), during the period, the annual average share of industrial supplies in imports was 49%, the share of capital goods was 44% and the share of consumer goods was 7%, in parallel with the ISI policies.

During the last period of Pahlavi dynasty, the relations between Turkey and Iran were usually positive and at least they came together on the common grounds of anti-communism and Western Block. Despite this common ground there also existed serious problems such as, Iran's support of the Kurdish oppositional groups in Iraq, Iran's target of being main the regional power in the Middle East and Persian Gulf, Iran's dissatisfaction regarding CENTO and accusation of Turkey for putting CENTO into the back burner, rising criticism in the public opinion as a result of incompatibility between democracy and monarchy and the waste of the economic cooperation efforts under the RCD.⁹⁷ All of these problems also gave rise to heated polemics and mutual accusations in the Turkish and Iranian press.⁹⁸

Along with the economic problems that already existed, the twin oil crisis of the 1970s put additional burden on not only Turkish economy but also its policy and military. On the other hand, the same crisis and consequent hikes in oil prices led to a sharp surge in revenues of Iran. As a result, not only economic but also military and political power of Iran rapidly increased. In parallel with these developments, the balance of power between Turkey and Iran deteriorated in favor of Iran and bilateral relations strained and did not developed so much. In other words, by the mid-1970s

⁹⁷ Atay Akdevelioğlu and Ömer Kürkçüoğlu, "İran'la İlişkiler: 1960-1980", in Baskın Oran, (Ed.), *Türk Dış Politikası: Kurtuluş Savaşından Bugüne Olgular, Belgeler, Yorumlar (1919-1980)*, Vol. I, 8th ed., İstanbul, İletişim Yayınları, 2003, pp. 801-804.

⁹⁸ Çetinsaya, *op.cit.*, p. 127.

the combination of windfall oil profits, massive arms acquisitions and the Shah's ambitions propelled Iran into the position of a regional power and its assertive foreign policy provoked suspicion in Ankara.⁹⁹ Nevertheless Shah was content with the change in the relative power situation between Turkey and Iran, and sought to turn it to his advantage. His rejection of Ankara's requests for cheap oil and other needs of the Turkish economy led to resentment among the Turkish political elite.¹⁰⁰

On business side, Turkish industrialists tried to gain profit from Iran's rapid development. In this respect, under the leadership of industrialists, some merchants and the representatives of the two Turkish banks held a business trip to Iran in the mid-1970s for the first time in years.¹⁰¹ During the period, Turkish businessmen anticipated to gain profit from Iran's rapid development and increase in imports, especially in the infrastructure sector. They tried to enhance exports of construction products to Iran and persuade Iran to supply its demands from Turkey or via Turkey. Furthermore, they tried to develop economic relations through joint investments in the food, agriculture and livestock, natural resources and mining, construction, banking and petro-chemicals sectors.

Despite the eagerness of the Turkish business class, many of the above mentioned opportunities could not be taken. Turkey could not get a noteworthy share from the investments in Iran and Iran did not invest in Turkey as well. Thus many of the projects could not be realized. A few years later, at a time when internal and external conditions were worsening for Turkey, a new project was initiated with Iran: border trade. The economical bottleneck emanating from sharp increase in oil prices during the 1970s following the twin oil crises and shortage of foreign exchange compelled Turkey to find alternatives and utilize new methods for trade. For this reason, border trade has started to be carried out in 1978 together with the aim of increasing regional prosperity and development as an alternative mechanism.¹⁰²

⁹⁹ John Calabrese, "Turkey and Iran: Limits of a Stable Relationship," *British Journal of Middle Eastern Studies*, Vol. 25, No. 1 (May 1998), p. 77.

¹⁰⁰ Çetinsaya, *op.cit.*, p. 127.

¹⁰¹ *Milliyet*, 10.03.1975, <http://gazetearsivi.milliyet.com.tr>, internet access: 28.10.2011.

¹⁰² Osman Z. Orhan, *Sınır Ticaretinin Türkiye Ekonomisine Etkileri*, Yayın No. 2000-27, İstanbul, İstanbul Ticaret Odası, 2000, p. 19.

Border trade is a special trade regime and its scope and rules are determined by the agreements between neighboring countries. Border trade covers certain products, in certain quantities. In the imports of these products customs tariffs are either eliminated or reduced. In addition, red tape in foreign trade is cut and import surveillance is reduced under the border trade method. Border trade method was firstly utilized between Turkey and Iran in 1978. In Iranian case, border trade was implemented through selling goods in return for oil.¹⁰³ According to some researches, Turkish merchants who involved in trading goods for oil have turned into importers and exporters as they were given a high profit range by state and as they have culminated a capital stock.¹⁰⁴ Although the rule of mutuality was in effect at the beginning, this was gradually abandoned and the border trade turned in to “borderless” trade in the course of time.¹⁰⁵ The tough and hard-to-control geographical conditions together with the profitability of smuggled oil doomed the legal border trade. Moreover, borderless trade not only affected tax income of the Turkish state but also interrupted agriculture and stockbreeding, decreased production and harmed domestic producers and ended up with significant unjust enrichment.¹⁰⁶ In the following years, further regulations were put into effect on border trade; in this context border trade was envisaged to be done by some of the border regions in 1979 and Ağrı-Gürbulak border gate was legalized to carry out border trade with Iran in 1980. This method started to become a more common practice in the region.¹⁰⁷

By the late 1970s, both of the countries got tied up with internal political, social and economic problems. In this context radical transformations were

¹⁰³ *Ibid.*, p. 19.

¹⁰⁴ Nurettin Öztürk, “Türkiye’de Sınır Ticaretinin Gelişimi, Ekonomik Etkileri, Karşılaşılan Sorunlar ve Çözüm Önerileri,” *ZKÜ Sosyal Bilimler Dergisi*, Vol. 2, No. 3 (2006), p. 110.

¹⁰⁵ *Ibid.*, p. 107.

¹⁰⁶ Orhan Deniz, “Türkiye-İran Sınırında Akaryakıt Kaçakçılığı ve Etkileri,” *Örgütlü Suçlar ve Yeni Trendler*, p. 99., http://www.utsam.org/images/upload/attachment/utsas_2010_secilmis/T%C3%BCrkiye-%C4%B0ran%20S%C4%B1n%C4%B1r%C4%B1nda%20Akaryak%C4%B1t%20Ka%C3%A7ak%C3%A7%C4%B1l%C4%B1%C4%9F%C4%B1%20ve%20Etkileri.pdf, internet access: 29.10.2011.

¹⁰⁷ Mustafa Tan and Fuat Altundal, “Türkiye’de Sınır Ticaretinin Gelişimi ve Mevcut Durumu,” Yayın No. 2008-26, İstanbul, İstanbul Ticaret Odası, 2008, p. 21.

experienced in Iran and Turkey one after another in 1979 and 1980. The 1979 Iranian revolution presented the first major challenge to the stability of Turkish-Iranian relations. Although, Turkey changed its mind later and contrary to expectations, Turkey welcomed the new regime in the beginning. Two days after the regime change, Turkey accepted and officially recognized the new regime.¹⁰⁸ Initially this shift did not bother Turkey's economic policies, because there was already a discontent about the Shah's regime and economic policies towards Turkey and this shift created new expectations. In addition although the new regime withdrew from CENTO and Western Block politically, it remained in the capitalist economic system and carried on its membership in RCD. At the same time, this move showed the importance which was given by the new regime to bilateral economic relations with Turkey. All of these developments were satisfied Turkey to accept the regime change. The second challenge came from Turkey this time with the coup d'état in 1980. However, rather than deteriorate, bilateral relations and especially trade relations between Turkey and Iran developed after the coup with the beginning of the Iran-Iraq War in 1980 and lasted until 1988.

The political and economic relations between Turkey and Iran started to change after 1979. Despite the political incompatibilities and tensions, trade and economic issues were tried to give prominence and political problems were given secondary importance consciously. The first high-level official visit to Iran which made by the Turkish Minister of Foreign Affairs represented this new style of relations which will be prevailed during the 1980s and beside its political importance, this visit had also commercial and economic purposes.¹⁰⁹

Bilateral trade figures also reflect the political and economic developments of 1970s. Beginning with 1970s, bilateral trade volume between Turkey and Iran has rapidly increased. Trade volume that was around \$5 million in 1970, rose up to \$188 million in 1979. The increase in bilateral trade was mainly based on the rapid increase in imports from Iran rather than the increase in exports to Iran. This growth in imports was mainly based on the imports of mineral oils and mineral fuels which

¹⁰⁸ Çetinsaya, *op.cit.*, p. 127.

¹⁰⁹ *Milliyet*, 11-12.06.1979, <http://gazetearsivi.milliyet.com.tr>, internet access: 28.10.2011.

escalated in the 1970s. Bilateral trade balance which was in favor of Turkey until 1970 has started to deteriorate swiftly after 1970 and the gap between imports and exports have widened. Correspondingly, while Turkey had a \$5 million surplus of foreign trade in 1970, the trade figures indicated a deficit of \$164 million in 1979. Throughout the period, Turkish exports more than doubled and increased from \$5 million to \$12 million whereas imports increased by 38 times from \$5 million to \$176 million. Actually, the imbalance in trade relations between Turkey and Iran was a reflection of the general disparities between imports and exports that prevailed in Turkey's foreign trade with the rest of the world in the 1970s.

Throughout the 1970s, Iran's share in Turkey's foreign trade did not show an impressive outlook at all. Iran's share in total exports increased from 1% in 1970 to its highest 3% in 1977 and decreased to 0.5% in 1979 by the impact of Islamic Revolution. During the period, Iran's average share in exports was limited with 1.4%. On the imports side, Iran's share in total imports showed a rapid increase in parallel with the upsurge in mineral fuels and oils imports. In the first half of the 1970s, Iran's share in total imports was less than 1%, but in the second half of the 1970s, its share surge to 11%, its highest, and then diminished to 3% in 1979 like exports. During the period, Iran's average share in imports was limited with 2.3%. 1978 was the most imbalanced year in bilateral trade during 1970s. In this year exports were \$45 million, whereas imports jumped to \$488 million and as a result, \$444 million trade deficits occurred. In other words, imports from Iran were 11 times more than exports to Iran and one-five of the current account deficit stemmed from the imbalance in bilateral trade with Iran in 1978.

As a result of the economy policies carried out in the 1960s and 1970s, the structure of exports started to change and items that were subject to exports started to diversify after mid-1970s. Until the second half of the 1970s, major items in Turkey's exports to Iran were live animals, meat, fruits, vegetables and sugar, but from this time on the share on industrial products in exports started to increase. In this framework, besides traditional export goods, cement, cotton and yarn, chemicals, glass, iron and steel, aluminum and machinery exports started to increase gradually. In other words, throughout the 1970s while the number of goods subjected to exports

increased and diversified; thus relatively high value added products began to be exported increasingly together with the low value added products. During 1970s, contrary to exports, the structure of imports barely changed or diversified. In this period, mineral fuels and mineral oils was the only and major import item from Iran. When the imports in mineral fuels and oils are considered, a moderate increase was observed between 1971 and 1975. Imports of minerals fuels and oil increased rapidly after 1975 and the peak point was reached in 1978. In 1978, Iran became the number one supplier of mineral fuels and oils for Turkey with its share of 34% and made \$488 million worth exports to Turkey. In the year of Islamic Revolution, Iran supplied 10% of the total imports of Turkey, corresponding to \$176 million and drew back to 4th rank. Nevertheless, this fallback did not last long and by the beginning of 1980s imports of mineral fuels and oils from Iran began to increase again.

After analyzing the bilateral trade between Turkey and Iran, it will be illuminating to show the general outlook of Turkey's foreign trade. The 1970s have been the beginning of unprecedented and huge imbalances regarding the foreign trade of Turkey. In those years, the most negative data was observed in 1977. Within a decade, exports quadrupled from \$588 million to \$2.4 billion, imports increased 5 times from \$948 million to \$5.1 billion, whereas foreign trade deficit increased 8 times from \$358 million to \$2.8 billion and volume of foreign trade increased 5 times from \$1.5 billion to \$7.3 billion. Within this period, exports increased by 17% and imports increased by 23% in average. The rate of imports covered by exports dropped to 47% in this decade from an average of 69% in the 1960s. When we consider the composition of most imported and exported goods within aforesaid era, there is no noteworthy change. Five preceding items in exports are composed of cotton, fruit, tobacco, mineral ores and cement which are either agricultural products or natural resources that were relatively lower value-added. On the other hand, first five items in imports are composed of machinery, mineral oils and fuels, iron and steel, land vehicles and chemicals which are also classified as intermediate and investment goods that were higher value-added.

In a nutshell, until the 1980s, the role of foreign trade in determining the course of bilateral relations remained minimal. Indeed, throughout the first 60 years

of the Republic, Turkey's foreign trade relations with Iran were very limited in itself and Iran's share in Turkey's foreign trade did not show an impressive outlook at all. During the 1923-1979 period, Iran's average share in Turkey's total exports and imports were 0.4% and 0.8% respectively.

2.3. General Features of the Turkish Economy in the 1980s

The economic and social crunch of the late 1970s was tried to be overcome with a sudden and fundamental policy change of transforming the Turkish economy from an inward-looking economy based on import substitution industrialization to an outward-looking economy based on export oriented industrialization in the 1980s. Although, it is commonly used in literature as “export oriented industrialization”, it is probably more suitable to use the term “export oriented economic policies”, because it is still widely discussed whether or not there was a consistent industrialization and investment policy throughout the period. The metamorphosis of the economy started with the 24 January 1980 Decisions which was announced by the newly installed minority government of Demirel. In fact, the architect behind the January 24 measures was the Undersecretary of the State Planning Organization, Turgut Özal, who had been assigned to that position by Demirel, the then Prime Minister. As Boratav emphasized, Özal who had been an economist at the World Bank, the General Coordinator for the Sabancı Group and the President of Turkish Employers' Association of Metal Industries (MESS)¹¹⁰, the powerful association of employers, had already gained respect and esteem from the business community in the pre-1980 years of class clashes.¹¹¹

January 24 measures had been taken in the direction of the prescriptions and demands of IMF and WB and the bourgeoisie (mainly TÜSİAD) to alleviate the

¹¹⁰ Turkish Employers' Association of Metal Industries (MESS) was founded in 14 October 1959, and is active in the metal industry such as iron and steel, basic metal industries, fabricated metal products, machinery, electrical machinery, electronics and automotive.

¹¹¹ Korkut Boratav, “The Class Content of the September 12 Regime in Turkey,” 19 September 2007, http://www.sendika.org/english/yazi.php?yazi_no=13255, internet access: 09.10.2011.

economic bottleneck experienced after 1977.¹¹² As a natural consequence, these measures were a kind of mixture of the previous stability policy programs of IMF and structural adjustment programs of the WB and from the very beginning, this program abundantly benefited from the financial resources of the two pillars of the Bretton Woods system, as well as international banks. As Aydın and Aras clearly puts it, the decision was taken in a changing international political and economic environment, after debates about Turkey's future political and economic place in the world. In other words, the final move to adopt the January 24 measures was a result of not only economic necessities but also political considerations.¹¹³

The January 24 measures were implemented as a result of liberalization and were taken with a view to managing the economy according to the rules of free market from then on. As a result, these significant steps influenced not only economic, but also political, social and institutional structures of the country and constitute a turning point in the history of modern Turkey.

Although Demirel government was unable to gain the political support necessary for the successful implementation of the package, the military regime that came to the power after September 12 of the same year endorsed the new program and appointed Özal as the Deputy Prime Minister responsible of economy.¹¹⁴ With the September 12 coup d'état, Demirel was arrested and Özal became the Deputy Prime Minister in charge of the economy and then in December 1983 he became the Prime Minister and six years later, in November 1989 he became the President of Turkey. At this point, in order to clarify the power of bourgeoisie, it is important to note that a week after the government was formed, Vehbi Koç, one of the founders of the TÜSİAD, wrote a letter to the head of the military junta, Kenan Evren, and asked him to "keep Turgut Özal".¹¹⁵ Actually, Turkish industrial bourgeoisie explicitly started to calling for a change in the system, control of the workers' unions and

¹¹² Boratav, *Türkiye İktisat Tarihi: 1908-2002*, pp. 148-149.

¹¹³ Mustafa Aydın and Damla Aras, "Ortadoğu'da Ekonomik İlişkilerin Siyasi Çerçevesi: Türkiye'nin İran, Irak ve Suriye ile Bağlantıları", *Uluslararası İlişkiler*, Vol. 1, No. 2 (Summer 2004), p. 107.

¹¹⁴ Owen and Pamuk, *op.cit.*, p. 117.

¹¹⁵ Boratav, "The Class Content of the September 12 Regime in Turkey".

syndicates and restoring a secure environment required for capital and investments by 1979.¹¹⁶ So to speak, with the September 12 coup, Özal became not only *de facto*, but also *de jure* “master of the economy” and throughout the 1980s, he played the leading role in determining the economy policies.

On the verge of this sea change, the optimum environment, in which the January 24 Decisions could be enforced without making any concessions, was created by the September 12 coup d'état.¹¹⁷ Consequently, with the namely “24+12 Formula”¹¹⁸, Turkey abruptly abandoned the import substitution industrialization, which has been implemented since the establishment of the Republic, and started to integrate with the world economy via export oriented economic policies and opening up its economy. Most observers agree that without military rule, an elected government couldn't have carried out the January 24 package to its conclusion.¹¹⁹

Although January 24 Decisions looked like previous IMF and WB programs, actually it was more than the mere sum of them; because the all decisions constituted a package together with the economic measures implemented after September 12, so the real importance of the decisions lies behind this reality.¹²⁰ After January 24 Decisions, a profound economic reform process started with the liberalization of the foreign trade regime, continued with the financial sector and culminated in the capital accounts.¹²¹

Through January 24 Decisions, the government, together with the IMF and WB, tried to formulate a neo-liberal prescription that would, *inter alia*, solve the balance of payment problems, limit inflation and transform ISI into an export-oriented strategy. The continuous devaluation of the Turkish lira, gradual liberalization of import regime, opening the economy to international competition,

¹¹⁶ Boratav, *Türkiye İktisat Tarihi: 1908-2002*, p. 146.

¹¹⁷ Tülin Öngen, “Yeni Liberal Dönüşüm Projesi ve Türkiye Deneyimi,” in Ahmet H. Köse, Fikret Şenses and Erinc Yeldan, (Eds.), *Küresel Düzen: Birikim, Devlet ve Sınıflar*, İstanbul, İletişim Yayınları, 2003, p.176.

¹¹⁸ Oran, *op. cit.*, p. 668.

¹¹⁹ Owen and Pamuk, *op.cit.*, p.118.

¹²⁰ Oran, *op. cit.*, p. 665.

¹²¹ The Central Bank of the Republic of Turkey, *The Impact of Globalization on the Turkish Economy*, Ankara, 2002, p. 4.

encouraging foreign capital and investments, making exports a national priority, abolishing of price controls and subsidies, narrowing the domestic demand and scaling down the state sector were the key elements of this prescription.

On the export side, export incentive schemes were quickly expanded and consolidated within the framework of the export mobilization process. Foreign trade companies were promoted through a series of instruments. First, the exchange rate was allowed to depreciate in real terms with an aim to make Turkish exports more competitive in global markets on the one hand, and to make imported goods expensive and to decrease the domestic demand on the other hand. Second, direct payments were made to the exporters. The initial costs of exporters were covered by the government's budget and extra budgetary funds. Third, preferential and subsidized export credits were provided to the exporters. Central Bank, Turkish Development Bank, the newly found Export Promotion Fund, and Turk Eximbank, which was founded in 1987, provided subsidized export credits. Another important step was the tax exemptions which were provided on imported inputs. Under this system, imported goods, which are used as input in the production of export goods, were exempted from import taxes. Fifth, the Free Trade Zones Law was issued in 1985 with the purpose of increasing export oriented investment and production.

Taken all together, these measures would lead to the promotion of export-led growth, transformation of the traditional structure of exports as well as the explosion of exports. However, generous incentives along with corruption, bribery and nepotism paved the way for fictitious or imaginary exports.¹²² Furthermore, although the free trade zones was symbolized as the annihilation of the state in terms of taxation and bureaucratic audit, syndicates in terms of strike and lock-out and a full existence of state in terms of incentives and tax reduction, during the 1980s both national and foreign capital did not show interest to free trade zones at all.¹²³

On the import side, the structure of the protection was changed and import regime was progressively liberalized. In 1980, as a first step, import regulations were simplified and the stamp duty on imports was decreased. In 1981, the Quota List (a

¹²² Boratav, *loc. cit.*, p. 155.

¹²³ Kazgan, *op. cit.*, pp. 161-162.

list of imported goods subject to quantitative limits) was abolished and a large number of items were transferred from the Liberalized List 2 (including all items whose importation required a license) to the less restrictive Liberalized List 1 (including all goods that could be freely imported). Four years after the January 24 Decisions, almost whole of the import regime was revolutionized. In this framework, the two lists were abolished and three new lists were introduced, namely The Prohibited List, the List of Imports Subject to License, and the Fund List.¹²⁴ Under this new regime, all commodities that were not explicitly prohibited could be imported. The reductions in quantitative restrictions were coupled by cuts in the rates of customs duties. During the liberalization process, the Prohibited List was phased out; banned commodities were reduced from 500 to 3 items: weapons, ammunition, and narcotics. In 1989, import liberalization gained further momentum. The number of goods subject to licenses was reduced, while tariffs and levies on imports were substantially diminished. In the same year, in order to protect the domestic production from unfair competition, the Government introduced an “anti-dumping law”.

With these measures taken regarding the imports, the existing ISI structure of the domestic market began to open up to international competition for the first time.¹²⁵ The response of the private sector to the import liberalization process was mixed. While the export oriented groups and sectors supported it, the protected ISI industries of the previous period, especially the large scale conglomerates such as the Koç Group whose products included consumer durables and automobiles, continued to lobby for protection.¹²⁶

During the 1980s, in parallel with the liberalization processes of export and import regimes, in order to increase the capital accumulation, to integrate into the international economic system and to strengthen the linkages between Turkey and its new markets the government initiated the financial liberalization process through a number of economic, legal and institutional reforms. As a first step, fixed exchange

¹²⁴ The Central Bank of the Republic of Turkey, *op. cit.*, p. 9.

¹²⁵ Owen and Pamuk, *op. cit.*, p. 118.

¹²⁶ Owen and Pamuk, *op. cit.*, pp. 118-119.

rate regime was superseded by a more realistic and flexible exchange rate policy in 1980. Interest rates were deregulated gradually throughout the period and finally all kinds of deposit interest rates were freed in October 1988. However, the removing of controls and restrictions on interest rates led to a severe competition between the small banks and the bankers and this competition ended up with a financial turbulence. In 1982 bankers collapsed and trailed some small banks after them. As the next step, Özal and some other ministers had to resign.¹²⁷ In Boratav's words, this was the first big fiasco of the liberal economic policies.¹²⁸ At the beginning of 1983, the Central Bank, thus the government, regained the authority to determine the interest rates and consequently, all kinds of deposit interest rates were freed in 1988. In this context, with a view to promote the development of the securities markets in Turkey which aimed at regulating, promoting and supervising the capital markets and protecting the rights and benefits of investors through the secure, transparent and stable functioning of the capital markets, the Capital Markets Law enacted in 1981 and subject to the provisions of this law, Capital Market Board was established to regulate primary markets in 1982.¹²⁹ After the banker crisis, in 1986, the Istanbul Stock Exchange was opened and inter-bank money market began operating with the intermediation of Central Bank. As a result, an attractive alternative and secure investment area -since interest rates of these instruments were determined under market conditions- was provided to the financial and non-financial institutions.

Capital account liberalization in Turkey was initiated in conjunction with the process of economic and financial reforms that started in 1980, and was fully completed in 1989. Gradual liberalization of capital accounts started after 1980, with the Decrees No. 28 and 30 and was fully completed in August 1989 with the issuance of the Decree No. 32. With this Decree and amendments on it, capital movements were fully liberalized and the major steps for convertibility were taken¹³⁰. Capital

¹²⁷ Zürcher, *op. cit.*, p. 426.

¹²⁸ Boratav, *loc. cit.*, p. 154.

¹²⁹ Onur A. Koska, "Financial Liberalization Era in Turkey: Critique on Decree No.32" 2005, p. 8, <http://129.3.20.41/eps/mac/papers/0506/0506016.pdf>, internet access: 08.10.2011.

¹³⁰ The Central Bank of the Republic of Turkey, *op. cit.*, p. 15-16.

account liberalization increasingly forged the economy to become dependent on the newly emerging financial cycles and arbitrage-seeking (hot money) inflows and outflows started to constitute a rising share within capital movements, and contributed to rising external and domestic instability.¹³¹

Aside from relatively good export performance, the impact of the neo-liberal policies on the real economy was rather mixed. Most importantly, the new policies were unable to mobilize the level of private investments necessary for long-term growth. In manufacturing industry, high interest rates and political instability were the most important impediments.¹³² As a result of these impediments, fixed investments in manufacturing barely increased during the period. In Yeldan's words, Turkish economy turned towards exports, but it could not industrialize towards exports.¹³³

Furthermore, high levels of unemployment and unequal distribution of income became an important feature of the 1980s.¹³⁴ Salaries and wages of civil servants and workers dropped considerably. Subsidies were either decreased or terminated, price regulations were abandoned so to speak, the agriculture sector; farmers and peasants were also left aside during the period. TOBB and TİSK were very influential in the decision making process concerning wages, and the government with military regime took side with the capital in its struggle against labor.¹³⁵ In short, the losers of the 1980s and the neo-liberal policies of the government were workers, civil servants and peasants.

On the other hand, the winners of the 1980s were the exporters in general. As a result of the generous incentives granted to exporters, a conflict of interest also emerged between exporters (not necessarily producers themselves), who grasped the

¹³¹ Korkut Boratav and Erineç Yeldan, "Turkey, 1980-2000: Financial Liberalization, Macroeconomic (In)-Stability and Patterns of Distribution", 2001, p. 7, <http://www.bilkent.edu.tr/~yeldane/B&YCEPA2002.PDF>, internet access: 13.09.2011.

¹³² Owen and Pamuk, *op. cit.*, p. 120.

¹³³ Erineç Yeldan, *Küreselleşme Sürecinde Türkiye Ekonomisi: Bölüşüm, Birikim ve Büyüme*, 7th ed., İstanbul, İletişim Yayınları, 2003, p. 47.

¹³⁴ Altunışık and Tür, *op. cit.*, p. 80.

¹³⁵ Boratav, *Türkiye İktisat Tarihi: 1908-2002*, p. 150.

main benefits of the new economic strategy during the 1980s, and TÜSİAD, which embodied a significant group of inward-oriented industrialists.¹³⁶ Despite being among the winners, TÜSİAD was disappointed because they thought that excessive incentives granted to exporters that penalized industrial production and industrialists. Other winners of the 1980s were the big family holdings. Some of these families' roots were tracing back to 1920s like Koç and Eczacıbaşı (first generation), and some of them started to climb during the 1950s like Sabancı and Çukurova Groups (second generation), and finally some of them got to the stage during 1980s like ENKA and STFA (third generation), which were the conglomerates providing services mainly in the construction, construction equipment and construction chemicals not only in Turkey but also increasingly in Middle East and North Africa.¹³⁷ Another striking phenomenon in the 1980s (and especially in the 1990s) was the emergence and rise of the Anatolian Tigers or Islamic capital.¹³⁸ Anatolian tigers, small scale family businesses which concentrated on the export of manufactured goods in certain Anatolian cities¹³⁹ like Gaziantep, Konya, Denizli, Kayseri and Eskişehir provided a powerful economic base to political Islam and strengthened its position in the bourgeoisie towards the end of the 1980s. Starting with this period, small- and medium-scale enterprises (SMEs) at local levels have formed a new business community by improving their business practices, learning technology, and searching new markets.¹⁴⁰ In short, liberalization policies of Özal period had a transforming and accelerating impact over the formation of Anatolian capital, which was highly promoted and became visible after the 1980s.¹⁴¹ As a result of the power obtained in the economic and political arenas, Anatolian tigers founded the Independent Industrialists and Businessmen Association (MÜSİAD) in 1990. In general, in the

¹³⁶ Öniş and Türem, *op. cit.*, p. 443.

¹³⁷ Zürcher, *op. cit.*, p. 427.

¹³⁸ Ergun Özbudun and Fuat Keyman, "Türkiye'de Kültürel Küreselleşme: Aktörler Söylemler, Stratejiler," in Peter L. Berger and Samuel Huntington, (Eds.), Ayla Ortaç, (Translator), *Bir Küre Binbir Küreselleşme*, İstanbul, Kitap Yayınevi, p. 311.

¹³⁹ Altunışık and Tür, *op. cit.*, p. 82.

¹⁴⁰ Ömer Demir, Mustafa Acar and Metin Toprak, "Anatolian Tigers or Islamic Capital: Prospects and Challenges," *Middle Eastern Studies*, Vol.40, No.6 (November 2004), p. 168.

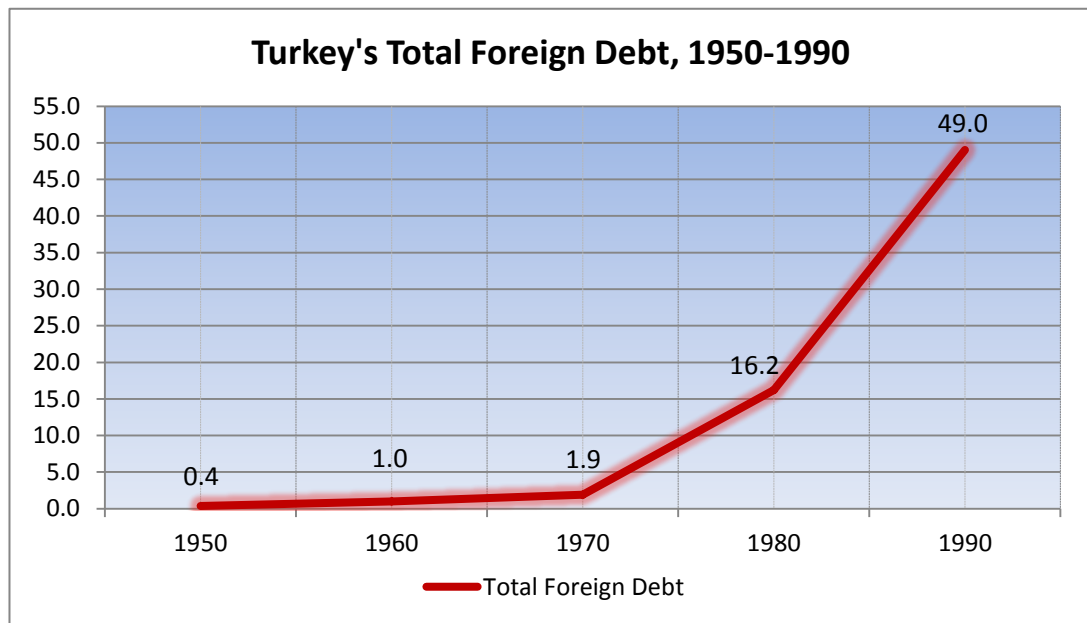
¹⁴¹ *Ibid.*, p. 169.

pursuit of integrating Turkey's economy with the world, Özal preferred the business community as his partner than the bureaucracy.¹⁴² As a natural consequence, business community emerged as an actor and increased its role in Turkey's foreign policy.

However, the initial success of the exports and economic liberalization program could not be sustained in the second half of the 1980s. This pattern appears to be a rather typical feature of Turkish economic development. There have been a number of such periods of unusual economic progress in the post-war era, however, these periods tended to be relatively short-lived and were followed by periods of stagnation and crisis.¹⁴³ Macroeconomic indicators started to deteriorate and imbalances with increasing indebtedness were seen again by the late 1980s. In fact the success of the economic program was heavily supported by the IMF, WB and international banks via generous loan opportunities. As Owen and Pamuk emphasized, these were undoubtedly vital ingredients for success of the neo-liberal program. Like the late 1970s, the aggravated deficit on the balance of payments necessitated more internal and external borrowing, thus leading Turkey into perpetual debt bondage again. If foreign flows were available, the economy runs smoothly, if not, serious problems arose. As can be seen from the graph below, reliance of economy to external sources has increased since the 1950s, but the real jump came after the 1970s.

¹⁴² Altay Atlı, "Businessmen as Diplomats: The Role of Business Associations in Turkey's Foreign Economic Policy," *Insight Turkey*, Vol. 13, No.1 (2011), p. 112.

¹⁴³ Ziya Öniş and İsmail Emre Bayram, "Temporary Star or Emerging Tiger? Turkey's Recent Economic Performance in a Global Setting," *New Perspectives on Turkey*, İstanbul, Homer Kitabevi, No. 39 (Fall 2008), p. 52.



Source: UT and CBRT, 1950-1990, Billion US \$.

Figure 1 Turkey's Total Foreign Debt, 1950-1990

Moreover, as the banned old politicians came to the fore of the domestic politics, the political system became more competitive and the government started to pursue populist policies increasingly. Real wages, salaries and agricultural income were raised sharply by using various means. In addition, an escalating war with PKK sharply and continuously increased the military spending, budget deficit and borrowing requirement which began to be financed by higher levels of internal and external borrowing as well as the printing of money.¹⁴⁴ Moreover, the end of the Iran-Iraq war and the outbreak of the Gulf War negatively affect the exports. Turkey's export performance benefited highly from the war between Iran and Iraq. During the years of war, Iran and Iraq emerged as the biggest markets of Turkey and the share of the Middle Eastern countries in Turkey's foreign trade increased in expense of European countries. But this trend did not last too long and changed after the War. And subsequent Gulf War also negatively affected the foreign trade, Turkey lost these profitable markets, and because of the political and economic

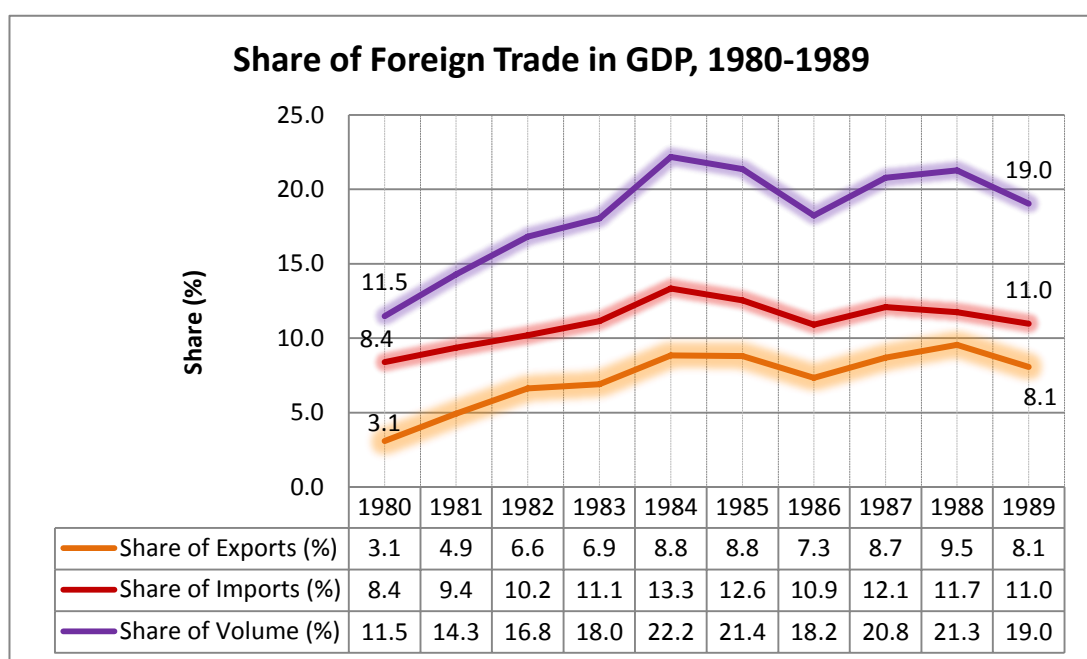
¹⁴⁴ Owen and Pamuk, *op. cit.*, p. 121.

instability European foreign investments to Turkey reduced. All of these developments put an additional burden on the already fragile and ailing economy.

In addition opening up the economy to short term foreign capital transactions increased the dependence on speculative capital, leading to high interest rates and overvalued currency.¹⁴⁵ High interest rates led to a decrease in investments. As a result of the overvalued currency already high imports increased on the one hand and exports were negatively affected by the diminishing price competitiveness on the other hand. Consequently, the gap between imports and exports, thus current account deficit widened and this situation accelerated the need of borrowing. In addition, because of the surge in inflation, the costs of the industries which used domestic inputs rise, while the costs of industries which used imported inputs decreased. These negative affects paved the way for a recession in real economy. Taking all the side effects and macroeconomic imbalances together, Turkey entered the 1990s with serious economic problems which resulted in 1994 crisis.

Everything aside, as a result of the liberalization process, the significance and magnitude of foreign trade substantially increased among the other determinants of the foreign policy. In a historical perspective, in parallel with the rise of the share of foreign trade volume in GDP, the concept of trading state gained prevalence. The more foreign trade increased, the more it determined the course of economy and the more it determined the course of economy, the more it determined not only internal, but also international politics. So to say, the process of becoming a “trading state” originally started during the reign of Özal.

¹⁴⁵ Altunışık and Tür, *op. cit.*, p. 82.



Source: TurkStat and IMF-World Economic Outlook Database-September 2011, Share (%).

Figure 2 Share of Foreign Trade in GDP, 1980-1989

As an indicator of international openness of an economy, a significant improvement in the share of foreign trade in GDP has been observed in the 1980s. The average share of exports in GDP in the 1980s exhibited an almost threefold increase, while the share of imports nearly doubled in the same period. As a result of aforementioned developments in foreign trade, the share of foreign trade in GDP gradually increased during the era first rapidly and then slowly. The share foreign trade in GDP jumped from 11.5% in 1980 to 22% in 1984 its highest during the period and then fell to the level of 19% in 1989.

As a result of the reforms implemented during 1980s, the exports quadrupled and rose from \$2.9 billion in 1980 to \$11.6 billion in 1989 in annual terms. With the gradual liberalization of the import regime during the 1980s, imports started to increase, albeit with a slower pace than exports, from \$7.9 billion in 1980 to \$15.8 billion in 1989. During the period, average growth rate of exports and imports was 19.3% and 13.1% respectively and despite following a fluctuating course, the trend was upside. As a result of the export mobilization efforts, during 10 years foreign trade deficit decreased by 17% from \$5 billion to \$4.2 billion while the volume of

foreign trade increased by three times from \$10.8 billion in 1980 to \$27.4 billion in 1989. More important, the rate of imports covered by exports jumped from 37% in 1980 to 74% in 1989. The average rate of imports covered by exports rose from 47% in the 1970s to 65% in the 1980s.

Table 1 Turkey's Foreign Trade, 1980-1989

Turkey's Foreign Trade, 1980-1989									
Years	Exports		Imports		Volume		Balance		Proportion of Imports covered by Exports (%)
	Value	Change (%)	Value	Change (%)	Value	Change (%)	Value	Change (%)	
1980	2.9	28.7	7.9	56.0	10.8	47.6	-5.0	78.0	36.8
1981	4.7	61.6	8.9	12.9	13.6	26.0	-4.2	-15.4	52.6
1982	5.7	22.2	8.8	-1.0	14.6	7.0	-3.1	-26.8	65.0
1983	5.7	-0.3	9.2	4.4	15.0	2.6	-3.5	13.3	62.0
1984	7.1	24.5	10.8	16.5	17.9	19.6	-3.6	3.3	66.3
1985	8.0	11.6	11.3	5.5	19.3	7.9	-3.4	-6.6	70.2
1986	7.5	-6.3	11.1	-2.1	18.6	-3.8	-3.6	7.8	67.1
1987	10.2	36.7	14.2	27.5	24.3	31.2	-4.0	8.8	72.0
1988	11.7	14.4	14.3	1.3	26.0	6.8	-2.7	-32.6	81.4
1989	11.6	-0.3	15.8	10.2	27.4	5.5	-4.2	55.9	73.6
1980-89		299.5		99.7		153.4		-16.6	

Source: TurkStat, 1980-1989, Billion US \$, Annual Change (%).

In addition, as a result of an active foreign trade diplomacy pursued by Özal, trading markets not only increased but also diversified. Target countries in exports also shifted from European markets to Middle Eastern and North African markets as a result of the huge amount of petro-dollars accumulated in these new markets after the petrol shocks.¹⁴⁶ In this respect, Özal initiated the practice of bringing ever larger delegations of business people with him to state visits.¹⁴⁷ During this period, the

¹⁴⁶ Zürcher, *op. cit.*, p. 429.

¹⁴⁷ Mustafa Aydın and Damla Aras, "Political Conditionality of Economic Relations between Patrimonial States: Turkey's Interaction with Iraq, Iran and Syria," *Arab Studies Quarterly*, Vol. 27, No. 1&2 (Winter/Spring 2005), p. 24.

number of exports and import markets increased also. The number of export market surged from 81 in 1980 to 131 in 1990. The number of import markets rose from 81 in 1980 to 130 in 1990. The share of Middle Eastern and North African countries in total trade increased considerably during the 1980s. This development was a result of not only expansion in the markets of oil-exporting countries but also Turkey's renewed political efforts in the region because of its political isolation in the West.¹⁴⁸ In addition, as mentioned earlier Turkey considerably benefited from the war between Iran and Iraq and increased its exports to these neighboring countries. Thus, the Iran-Iraq War also had an influence on the diversification of markets and shifting from Europe, the traditional market to the Middle East and North Africa, the emerging markets.

When we consider the composition of most imported and exported goods within aforesaid era, there was not a noteworthy change. During 1980s articles of apparel and clothing accessories, iron and steel, fruit and nuts, cotton and articles of leather were the first five most exported products while the mineral fuels, and mineral oils, electrical machinery and equipment and parts thereof, iron or steel, fertilizers and organic chemicals were the first five most imported products. However, the process was accompanied by a diversification of exports, involving a striking increase in the share of manufactured exports at the expense of agricultural exports.¹⁴⁹ The composition of exports changed considerably within the same period. According to International Standard Industrial Classification of All Economic Activities (ISIC Rev.3), the share of industrial products in total exports increased from 36% in 1980 to 81% in 1990; while the share of agricultural products and forestry in total exports decreased from 56% in 1980 to 16% in 1990. It is important to note that the increases in exports of manufactures since 1980 did not all take place in the Istanbul area or the Marmara region. The expansion of exports during the decade was accompanied by the rise of new industrial centers across Anatolia.¹⁵⁰

¹⁴⁸ *Ibid.*, p. 24.

¹⁴⁹ Öniş and Bayram, *op. cit.*, p. 52.

¹⁵⁰ Şevket Pamuk, "Globalization, Industrialization and Changing Politics in Turkey," *New Perspectives on Turkey*, İstanbul, Homer Kitabevi, No. 38 (Spring 2008), p. 268.

Turkey's new outward-looking business elite, or the so-called Anatolian Tigers, emerged during this period which could be argued as constituting the grassroots of current stars of emerging exporters.¹⁵¹

To sum up, in accordance with the export oriented economic policies of the 1980s, the significance of foreign trade and the business community (both traditional and emerging actors) increased not only in domestic but also in foreign policy. Turkey's political and economic relations with Iran during the 1980s were also influenced from these developments.

2.4. Turkey's Political and Economic Relations with Iran in the 1980s

As mentioned earlier, although the Shah Period often described as a "period of traditional friendship", it was impossible to talk about multi-dimensional and developed economic relations between Turkey and Iran. Since both of the countries came together on the common grounds of being part of the Western Block and anti-communism, problems usually did not put into words.

However, Islamic Revolution in Iran (1979) and subsequent Iran-Iraq War (1980-1988) stopped the monotony and led to a revival of relations. This revival covered not only political but also economic relations. Together with the changes in Iran, two important developments, 24 January 1980 Decisions and the coup d'état of 1980 in Turkey were also deeply effected bilateral relations. As mentioned before, with the January 24 Decisions, Turkey abruptly abandoned the ISI policies, which had been implemented since the establishment of the Republic, and started to integrate into the world economy via export oriented economic policies. This shift in economy policies necessitated Turkey to find new markets for selling its goods. In such an environment, the outbreak of Iran-Iraq War gave Turkey a golden opportunity to increase its exports and to achieve the objectives of export-led growth. Thus, the change in economic structure of Turkey positively affected the trade relations with Iran. Throughout a relatively long period of time, Turkish government

¹⁵¹ Mehmet Babacan, "Whither Axis Shift: A Perspective From Turkey's Foreign Trade," *SETA Policy Report*, No. 4 (November 2010), p. 7.

put commercial issues and interests before the political issues and this approach pressurized and delayed the emergence of political problems for some time. On the other hand, in conjunction with the Islamic Revolution and resultant ideological and political transformation in Iran, 1980 coup d'état, constituted a stress point in relations and political incompatibility between Iran and Turkey negatively affected the economic relations despite counter efforts. Even though the Turkish government tried to ignore and veil the political and ideological differences and problems, they spontaneously broke the surface in the course of time.

As a consequence of Turkey's oil dependence to Iraq and Iran, the danger of supply disruption emerged with the outbreak of war and this new conditions alarmed Turkey and forced it to put the political issues aside and bring up the economic and commercial issues on the top of the agenda. Actually, Iran-Iraq War turned to an opportunity in the hands of Özal who was a strong believer in the functionalist proposition that building economic links and networks would eventually promote the resolution of political problems.¹⁵² In such an environment, immediately after the outbreak of the war on 22 September 1980, Turkey declared its neutrality towards the belligerents on 2 October and continued its neutral stance throughout the eight-year-long war. As result of its "active neutrality" strategy, Turkey did show no favor to either party and became the major trading partner of both warring parties.¹⁵³ Since the war negatively affected the production in both countries, Iran and Iraq increasingly turned to Turkey to breath and satisfy their import needs through their oil incomes. As mentioned before, this was an unmissable opportunity for Turkey which was in dire need of exportation to sustain its national economic development. In addition, the international isolation of and the embargo imposed on Iran by the West because of the Islamic Revolution and the exclusion and criticism of Turkey by the West because of the 1980 coup d'état pave the for an economic convergence between Turkey and Iran.

¹⁵² Atilla Eralp, "Facing the Challenge: Post-Revolutionary Relations With Iran," in Henry J. Barkey, (Ed.), *Reluctant Neighbor: Turkey's Role in The Middle East*, Washington, United States Institute of Peace, 1996, p. 98.

¹⁵³ *Ibid.*, p. 99.

In order to take this great opportunity, Turkey started to search for ways to increase its exports. In this framework, during the 1980s official visits between Iran and Turkey increased more than ever. One of the reasons, probably the most important, behind this increase was the urgent needs of Iran and Turkey for foreign trade and the willingness to improve bilateral trade between them. In 1982, Özal visited Iran and approximately a hundred Turkish businessmen accompanied him for the first time. The main agenda of this visit was enhancing of cooperation in economy and trade. In this context, increasing the volume of bilateral trade, realizing of Ahvaz-İskenderun oil pipeline project, purchasing natural gas from Iran and the project of sending Iranian natural gas to Europe via Turkey were discussed and several export deals, nearly \$600 million worth were signed by the parties.¹⁵⁴ Another way for increasing exports was the instrument of Joint Economic Commission (JEC). The Turkish-Iranian JEC established in accordance with the Article 4 of the “Agreement between Turkey and Iran on Economic, Industrial and Technical Cooperation” signed on March 1982. During the 1980s, every year, the parties came together with these meetings in order to upgrade the level of bilateral economic cooperation in the fields of trade, banking, investments, transportation, industry and agriculture, etc. and several memorandum of understandings were signed, however the objectives could not be achieved totally. Actually, Turkey attached particular importance to JEC meetings with Iran from the beginning compared with other JECs and Turkey represented in these meetings by a large delegation which was consisted of not only bureaucrats but also representatives of business world such as DEİK (Foreign Economic Relations Board of Turkey - Dış Ekonomik İlişkiler Kurulu) an affiliate of TOBB, was established in November 1986 as a business association in order to develop Turkey’s economic, commercial, industrial and financial relations with foreign countries as well as international business communities. Like in many others, the mastermind behind the project of DEİK was Özal. In accordance with the principles of the export-oriented economic policies, DEİK has also undertaken the mission of the effective integration of

¹⁵⁴ *Milliyet*, 11.03.1982, <http://gazetearsivi.milliyet.com.tr>, internet access: 30.10.2011.

Turkey's economy into the global economy. Acting on this mission, finding new fields of cooperation in foreign markets and informing Turkish businessmen on the existing business opportunities abroad were constituted some of DEİK's major tasks.¹⁵⁵

During the first years of the war, trade was the main issue of the meetings and hardly any political issues or disagreements appeared or expressed. However, after 1984 political and also commercial problems started to come to surface. Turkey's developing relations with the Arab countries of the Middle East disturbed and made Iran suspicious about the stance of Turkey in the war. More importantly, Iran started increasingly to complain about low quality of Turkish products, Turkey's oil based imports from Iran and wanted to diversify its exports and sell non-oil goods to Turkey. Again in April 1984, Özal revisited Iran with leading Turkish businessmen such as Sakıp Sabancı, Rahmi Koç, Nejat Eczacıbaşı and Şarık Tara, the founder of the Enka Holding, to remove concerns, to sign new deals, to increase exports and to participate the meeting of Turkish-Iranian JEC.¹⁵⁶ Although the negotiations were continued in a positive atmosphere, the concerns of Iran could not be alleviated totally and this reflected as a decrease in exports. On the other hand worries, discontent and disturbance started to emerge in Turkey against Iran about the Kurdish issue. After the PKK (Kurdistan Workers' Party - Partiya Karkaren Kurdistan) which was founded by Abdullah Öcalan in 1974 as a Marxist-Leninist separatist organization, started its armed violence against the Turkish government in 1984, cold winds began to blow between Turkey and Iran. In other words, during 1984, both political and economic problems emerged and negatively affected the volume of trade. After these negative developments, Iranian Prime Minister visited Turkey in 1985 and parties agreed on an initial agreement of oil and natural gas pipeline. This agreement was of vital importance, since the realization of this long-term project will highly likely lead to a profound economic interdependence between Turkey and Iran.¹⁵⁷

¹⁵⁵ <http://www.DEİK.org.tr>, internet access: 31.10.2011.

¹⁵⁶ *Milliyet*, 26.04.1984, 30.04.1984, <http://gazetearsivi.milliyet.com.tr>, internet access: 30.10.2011.

¹⁵⁷ Fırat, *op. cit.*, p. 130.

During this brisk period, the need of carrying out the developing and diversifying economic relations under an institutional structure was emerged. In this framework, the organization of Regional Cooperation for Development (RCD) was restructured in parallel with the needs and the Economic Cooperation Organization (ECO) was founded in 1985 as the successor of the RCD by Turkey, Iran and Pakistan to promote economic, technical and cultural cooperation among the member states.¹⁵⁸ Differently from the RCD, in the 3rd article of the agreement, member states promised to lift the customs tariffs and other barriers to trade within a ten years period in order to establish a free trade area among them.¹⁵⁹ In this respect, the pressure coming from the business circles, some academicians and journalists towards a common market probably influential on this decision. During the 1970s and first half of the 1980s Turkish these circles called for a transformation of the RCD into a common market like the European Economic Community (EEC). However, ECO could not reach the level of efficiency that was expected by the member countries and aforementioned circles, because the rest of the 1980s was passed with the efforts of institutionalization efforts.¹⁶⁰ Since, it was evident that the member countries could not compromise on the political issues and could not come together around common political objectives, it was reasonable for Turkey, Iran and Pakistan to gather around the common economic objectives with a view to develop the relations. In addition, the establishment of ECO was well suited into the foreign policy perception of Turkey and Özal in terms of primacy of economic issues and interests over political issues. In fact this was a reflection of Özal's perception of increased interdependence with neighboring countries as an instrument to achieve conflict resolution.

¹⁵⁸ Richard Pomfret, "The Economic Cooperation Organization: Current Status and Future Prospects," *Europe-Asia Studies*, Vol. 49, No. 4 (Jun., 1997), p. 658.

¹⁵⁹ Atay Akdevelioğlu and Ömer Kürkçüoğlu, "İran'la İlişkiler: 1980-1990", in Baskın Oran, (Ed.), *Türk Dış Politikası: Kurtuluş Savaşından Bugüne Olgular, Belgeler, Yorumlar (1980-2001)*, Vol. II, 6th ed., İstanbul, İletişim Yayınları, 2003, p.155.

¹⁶⁰ Tschanguiz H. Pahlavan, "Turkish-Iranian Relations: An Iranian View," in Henry J. Barkey, (Ed.), *Reluctant Neighbor: Turkey's Role in The Middle East*, Washington, United States Institute of Peace, 1996, p. 90.

Nevertheless, this positive atmosphere in bilateral trade did not last long and political problems began to adversely affect the commercial relations. Mounting terrorist attacks in Turkey, assaultive attitude of Iran against secularism and Atatürk, Iran's criticism about the headscarf ban in universities, discourse of the export of revolution; Turkey's trans-border operations in Northern Iraq, suspicion over the increasing numbers of Iranian expatriates in Turkey were among the serious political problems between Turkey and Iran. In such an environment, in order to improve the decreasing economic relations Özal visited Iran again in 1986. As was the case before, Özal tried to smooth over the political cracks that strained Turkey's exports but this time he could not prevent exports from decreasing.

Towards to the end of Iran-Iraq War and especially after the end of the War in 1988, the economic and commercial relations between Turkey and Iran started to degrade as the mutual interdependence between parties diminished. At the same time, political disagreements which were not spoken out due to heavy interdependence began to be verbalized. As the political problems came to light, tension between the two was escalated and these tensions adversely affected the commercial relations. Ideological differences between Turkey and Iran, which were symbolized by the personalities of Kenan Evren and Ayatullah Khomeini, led to crises in the bilateral relations occasionally. Towards the 1990s, although the crises between Turkey and Iran were resolved in general, the distance between the countries was extended. By the 1990s, not only political, but also economic relations were deteriorated. Özal's vision of improving Turkey's bilateral relations with neighboring countries through economic interdependence was only partially attained throughout the 1980s. As the secessionist violence in Southeast Anatolia increased, along with intensifying political polarization and fragmentation, Turkey expectedly entered into a relatively stagnant period in foreign policy and economic transformation which diverted its energy on domestic struggles.¹⁶¹

During the 1980s, especially during the Iran-Iraq War, Turkey took the opportunity under the economic and political leadership of Özal and increased its

¹⁶¹ Sadık Ünay, "Economic Diplomacy for Competitiveness: Globalization and Turkey's New Foreign Policy," *Perceptions*, Volume XV, Number 3-4 (Autumn-Winter 2010), p. 26.

exports in short term. However, it is still controversial that whether this leadership and its policies change the fundamental characteristics of the economic and commercial relations between Iran and Turkey in the long-term. A profound analysis of the bilateral trade developments in the 1980s will show us the real success or failure of the policies concerning trade.

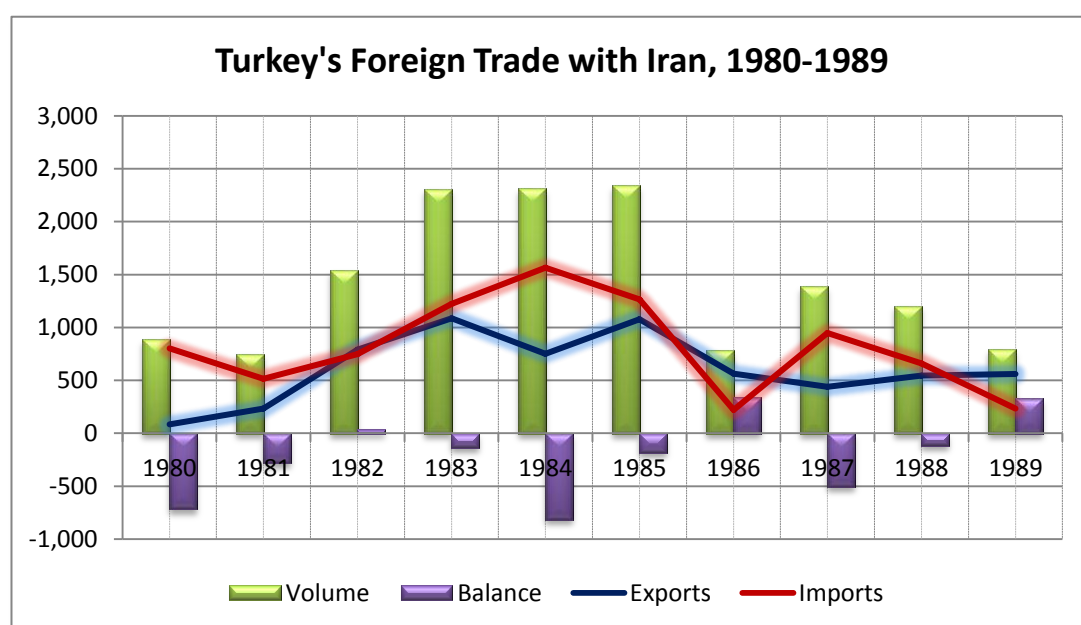
Table 2 Turkey's Foreign Trade with Iran, 1980-1989

Turkey's Foreign Trade with Iran, 1980-1989									
Years	Exports		Imports		Volume		Balance		Proportion of Imports covered by Exports (%)
	Value	Change (%)	Value	Change (%)	Value	Change (%)	Value	Change (%)	
1980	84.8	617.9	802.5	356.3	887.3	372.8	-717.7	337.5	10.6
1981	233.6	175.4	514.8	-35.8	748.4	-15.7	-281.3	-60.8	45.4
1982	791.1	238.7	747.7	45.2	1,538.8	105.6	43.4	-115.4	105.8
1983	1,087.7	37.5	1,222.1	63.4	2,309.8	50.1	-134.3	-409.8	89.0
1984	751.1	-31.0	1,565.7	28.1	2,316.7	0.3	-814.6	506.4	48.0
1985	1,078.9	43.6	1,264.7	-19.2	2,343.5	1.2	-185.8	-77.2	85.3
1986	564.4	-47.7	221.3	-82.5	785.7	-66.5	343.0	-284.6	255.0
1987	439.7	-22.1	947.6	328.1	1,387.3	76.6	-507.9	-248.1	46.4
1988	545.6	24.1	659.8	-30.4	1,205.4	-13.1	-114.2	-77.5	82.7
1989	561.0	2.8	233.5	-64.6	794.5	-34.1	327.6	-386.8	240.3
1980-89		561.4		-70.9		-10.5		-145.6	

Source: TurkStat, 1980-1989, Million US \$, Annual Change (%).

As can be seen from the table above, Turkey's exports to and imports from Iran fluctuated during the 1980s. Exports to Iran which were around \$85 million in 1980 rapidly increased in the first half of the period and came to a historical climax of \$1.1 billion in 1983 and then started to decrease and finally dropped to \$561 million in 1989. A similar trend prevailed also in imports. Imports from Iran which were around \$803 million in 1980, rapidly increased in the first half of the period and reached \$1.6 billion in 1984 and then started to decrease and finally dropped to \$233 million in 1989. In other words, the period of "sweet profit" for Turkey ended immediately after 1985.

In parallel with these developments, volume of bilateral trade rapidly increased in the first half of the 1980s and the Iran-Iraq War, and then began to shrink towards the end of period. The volume of trade which was around \$887 million in 1980, rapidly increased in the early 1980s and exceed \$1 billion and reached \$2.3 billion in 1985, but a year later sharply fell to \$786 million as a result of political tensions besides commercial tensions like price of imported oil, and the general decrease in global oil prices. In 1989, imports fell below the 1980 level and decreased to \$795 million. This fluctuation in the volume of trade during the 1980s demonstrates the conditionality of trade to this particular period of war.



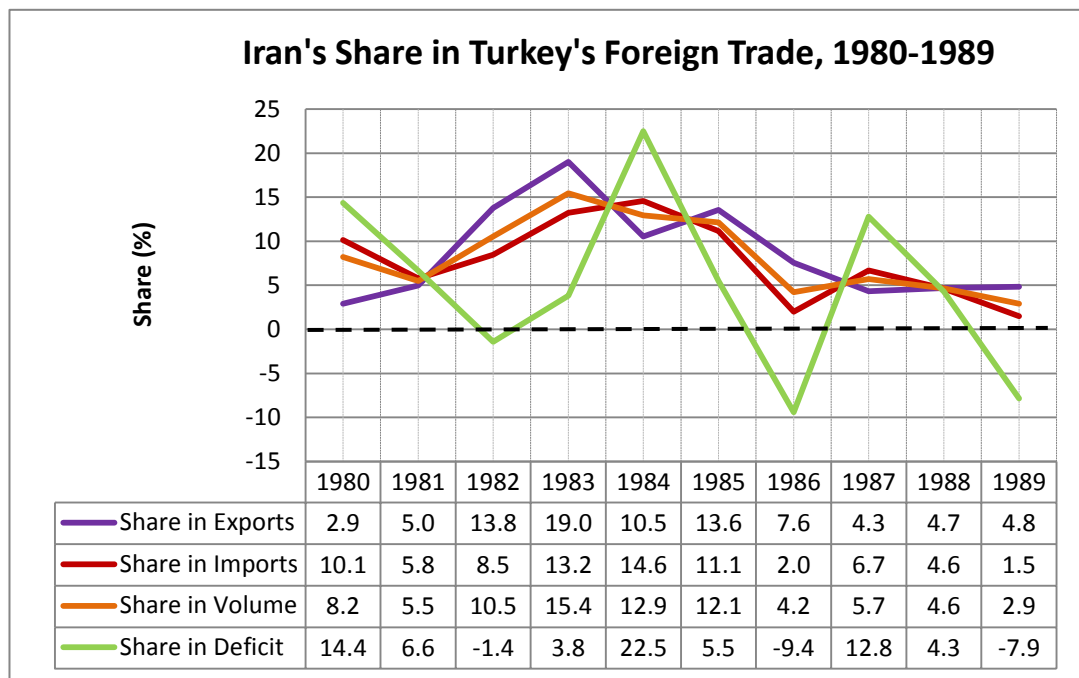
Source: TurkStat, 1980-1989, Million US \$.

Figure 3 Turkey's Foreign Trade with Iran, 1980-1989

In addition, instability in the balance of trade can be seen during the period. Although the balance was developed in favor of Iran during ten years generally, it turned to Turkey's favor in 1982, 1986 and 1989. 1984 was the most imbalanced year in bilateral trade during the 1980s with \$815 million foreign trade deficit. This deficit mainly stemmed from the peak of mineral fuels and oils imports worth \$1.6 billion. In fact, the foreign deficits of the 1980s did not stem from a huge difference

between imports and exports like in the 1970s. The reason behind the deficits was not the huge disproportion between imports and exports, actually the reason was the rise in quantities.

What is more impressive that the changes in the share of Iran Turkey's total foreign trade. Throughout the 1980s, Iran's share in Turkey's foreign trade showed an impressive development. Iran's share in Turkey's total exports increased from 3% in 1980 to its highest 19% in 1983 and decreased to 5% in 1989 as a result of the end of Iran-Iraq War. Iran's average share in Turkey's total exports increased from 1% in the 1970s to 9% in the 1980s. On the imports side, Iran's share in Turkey's total imports showed a relatively instable trend. Iran's share in total imports increased from 10% in 1980 to its highest 16% in 1984 and decreased to 1% in 1989. During the period, Iran's average share in imports increased from 2% in the 1970s to 8% in the 1980s.



Source: TurkStat, 1980-1989, Share (%).

Figure 4 Iran's Share in Turkey's Foreign Trade, 1980-1989

On the other hand, it can be useful to have a look at the rank of Iran among other export and import markets of Turkey to understand the rise and fall of Iran. In 1980, Iran was the 11th biggest export market of Turkey with a share of 3%. However only two years later, it became the biggest export market by replacing Germany, the traditional export market of Turkey. In 1983, Iran not only preserved its number one position in exports by increasing its share, but also became the first supplying market of Turkey. After 1983 Iran could not become biggest export market for Turkey again and started to degrade from 1st rank to 7th in 1989. A different situation prevailed on the imports side. In 1980, Iran was already among the first three markets and in 1983 and 1984 it climbed to the 1st rank by surpassing Iraq, the main energy supplier of Turkey and Germany, the main industrial goods supplier of Turkey. But after 1984, as the political and commercial problems came to the surface, Iran lost its position and only two years later, Iran drew back to 22nd with the share of 2% in 1986 and 18th with the share of 1% in 1989. Especially the global oil price declines and the disagreement about the oil price between Turkey and Iran were negatively affected the imports from Iran.

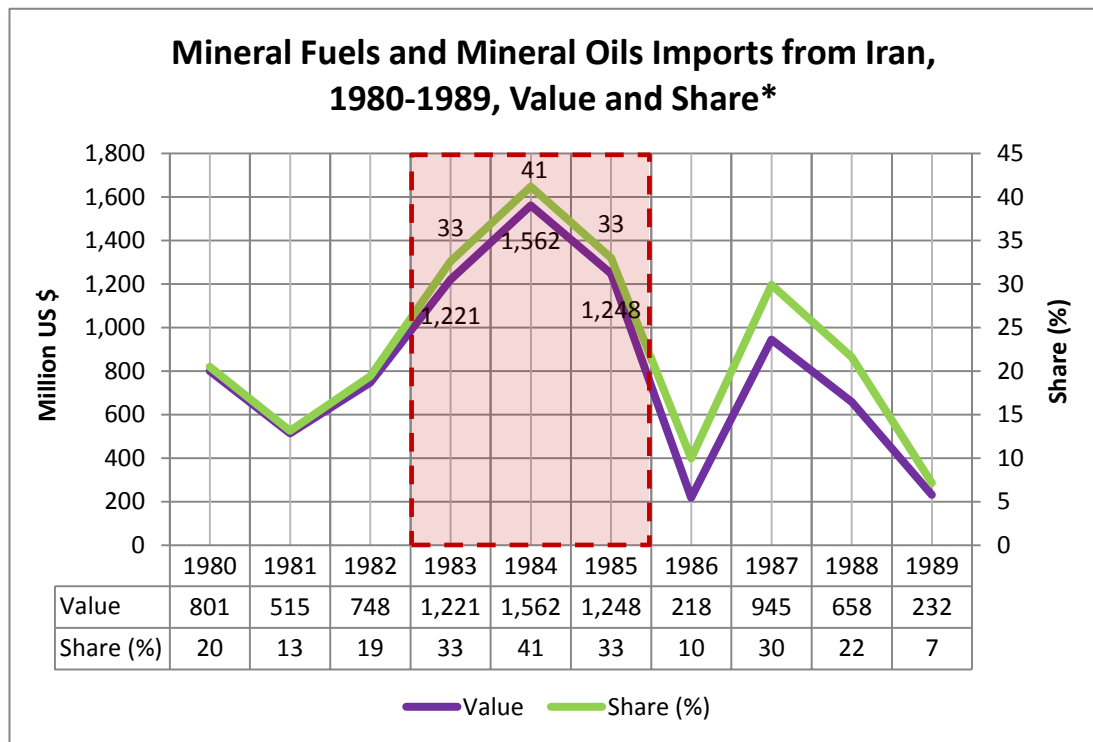
During the 1980s, the structure of foreign trade with Iran changed a little. Exports started to change and items that were subjected to exports already started to diversify after mid-1970s. However, major items in Turkey's exports to Iran also preserved their positions. Especially as a result of the outbreak of Iran-Iraq War, first of all, exportation of items which were fundamental to maintain the lives of society like live animals, meat, vegetables, cereals, sugar, dairy produce, flour, starch, animal and vegetable oil sharply increased. After these fundamental needs, as a result of the decline in Iranian production, exports of manufactured goods and their share in total started to increase. In this framework, besides foodstuff, pharmaceutical products, organic and inorganic chemicals, fertilizers, plastics, rubber, cotton and yarn, textile fabrics, glass, cement, iron and steel, aluminum and machinery exports land vehicles and parts and accessories thereof started to increase substantially. Furthermore, in the 1980s according to international standard industrial classification of all economic activities (ISIC Rev.3), the share of agricultural and forestry products in Turkey's total exports to Iran gradually decreased from approximately

20% to 1%, while the share of manufacturing products increased from nearly 80% to 99%. The average share of manufacturing products in Turkey's total exports to Iran was 93.1%, while the share of agricultural and forestry products was 6.8% during ten years.

In other words, during the 1980s the number of goods subjected to exports sharply and substantially increased and diversified. However this export boom was not because of the quality and price of the Turkish products. This was because of Turkey's proximity to Iran and Iran had no alternative because of the war and embargo. Actually Iran increasingly complained about the low quality and expensiveness of Turkish products. As a result, towards the end of the war, Turkey's exports to Iran started to decrease.

In the same period, mineral fuels and mineral oils was almost the only and major import item from Iran. In the course of time, Iran's discontent about this heavy reliance on mineral fuels and oils increased. Iran increasingly asserted that this structure of imports damaged its economy and hindered its efforts towards diversification of production. In order to quell Iran, Turkey began to import products like raw hides and skins, cotton and yarn, copper, chemicals and machinery from Iran, but imports of these items remain minimal in compared with the mineral fuels and oils.

During the 1980s, according to ISIC Rev.3, the share of mining and quarrying products, which covered the products of crude petroleum and natural gas, in Turkey's total imports from Iran was hardly changed. The average share of mining and quarrying products was 97.7%, while the share of manufacturing products limited with 2.3% during ten years.



Source: TurkStat, 1980-1989, Value: Million US \$, Share: Percentage (%).

*Share: Iran's share in Turkey's total imports of mineral fuels and mineral oils.

**Figure 5 Mineral Fuels and Mineral Oils Imports from Iran, 1980-1989,
Value and Share**

As can be seen from the graph above, from 1983 to 1985, Iran became the number one energy supplier of Turkey, by replacing its enemy Iraq with the share of 33%, 41%, 33% respectively. But one year after climbing to number one position, mineral fuels and oils imports dropped dramatically by 83%, from \$1.2 billion in 1985 to \$218 million in 1986. This decrease stemmed from the declines in oil prices in the global markets together with the disagreement about the price of oil between parties. In the first half of 1986 crude oil prices fell to about \$12 a barrel, back to their level of 1974 and, when adjusted for changes in the general price level, close to the real oil price that prevailed in 1973 just before the first OPEC price increase.¹⁶² Actually, the first half of the 1980s was under the influence of higher oil prices,

¹⁶² Dermot Gately, M. A. Adelman and James M. Griffin, "Lessons from the 1986 Oil Price Collapse," *Brookings Papers on Economic Activity*, No. 2 (1986), p. 237, http://www.brookings.edu/~media/Files/Programs/ES/BPEA/1986_2_bpea_papers/1986b_bpea_gately_adelman_griffin.pdf, internet access: 30.10.2011.

second half of the 1980s on the contrary, was under the influence of lower oil prices. Because of this, Turkey's energy bill and hence imports reduced after 1986 substantially. On the other hand, the sharp declines in oil output since 1980, together with significant real price declines, have resulted in a dramatic drop in revenues of Iran, like other oil producers. Revenue decreases caused a decline in the number of investments, a slowdown in construction projects and a reduction in imports of Iran and this eventually paved the way for decreasing import bill of Turkey on the one hand, and declining exports to Iran on the other hand. Iran was among Turkey's most important exports markets which suffered from the contraction in prices and resultant oil revenues after 1985.¹⁶³ Similar cases were experienced by Turkey in bilateral trade relation with other Middle Eastern markets like Iraq and Libya. In conjunction with the global oil price decline, a disagreement about the price of oil between Turkey and Iran emerged and this was also negatively affected the oil imports from Iran. Hence, oil imports from Iran declined both in terms of price and volume. At the end of the day, not only imports from, but also exports to Iran declined, thus the volume of trade dropped substantially in 1986.

In conclusion, during the 1980s the main determinants of the trade relations between Turkey's and Iran were Turkey's new policy of becoming export-oriented economy, idiosyncratic characteristics of the Özal's leadership, increasing influence of business community and their organizations, the Iran-Iraq War as a golden opportunity, consequent primacy of foreign trade over foreign policy, perception of resolution of political problems via economic interdependence. As a result, bilateral trade between Turkey and Iran sharply increased during the 1980s, but these changes did not last long. Because, a real and profound interdependency between Turkey and Iran could not be created during the period. In order to increase exports, a short term perspective was adopted and the medium and long term perspectives and projects which had the potential of shifting traditional weak interdependence, was neglected. In addition, fundamental political and ideological differences between parties were underestimated. Even sometimes, on behalf of increasing exports, important political

¹⁶³ Aydın and Aras, *loc. cit.*, p. 24.

concessions were given or the important political problems were ignored at least and did not tried to be settled. However, this attitude proved to be unsustainable. As the political problems become serious and non-negligible together with the disappearance of favorable and compelling conditions which was created by the Iran-Iraq War, not only political but also commercial bilateral relations started to deteriorate. Thus by the 1990s, Turkey and Iran became distant neighbors both politically and economically.

CHAPTER 3

TURKEY'S POLITICAL ECONOMY AND TURKISH – IRANIAN RELATIONS IN THE 1990s

3.1. General Features of the Turkish Economy in the 1990s

As mentioned earlier, Turkey entered the 1990s with serious economic problems as a result of the side effects and macroeconomic imbalances of the late 1980s. Nevertheless, the economic policies of the 1980s generally prevailed during the 1990s. Moreover, as the banned old politicians came back domestic politics following the lifting of political restrictions in 1987, the political system became more competitive and the government started to increasingly pursue populist policies. Combined with the lack of budgetary discipline and loss of pace on the export front, this new populist element in the Turkish economy was responsible for creating institutional instability in the 1990s.¹⁶⁴

Besides, during the 1990s, the role of the state in the economy both decreased and increased at the very same time in different areas. On the one hand, the role of the state in the financial markets and price regulations decreased substantially and strengthened the market forces, but on the other hand, state's role in the economy was reorganized and restructured by continuing public sector investments in the 1990s.¹⁶⁵

Throughout the period, Turkish economy was taken by the turbulent growth, sudden fluctuation of capital movements and financial instabilities. In Yeldan's words, during the decade Turkish economy was trapped within the mini cycles of growth-crisis-stabilization and renewed (artificial) growth.¹⁶⁶ During the 1990s, the inflation rate floated around 65-70% in the first half and 80-90% in the second half;

¹⁶⁴ Öniş and Bayram, *op. cit.*, p. 54.

¹⁶⁵ Altunışık and Tür, *op. cit.*, p. 83.

¹⁶⁶ Erineç Yeldan, "On the IMF-Directed Disinflation Program in Turkey: A Program for Stabilization and Austerity or a Recipe for Impoverishment and Financial Chaos?," 2001, p. 1, <http://www.econturk.org/Turkisheconomy/TurkCris2001.pdf>, internet access: 21.11.2011.

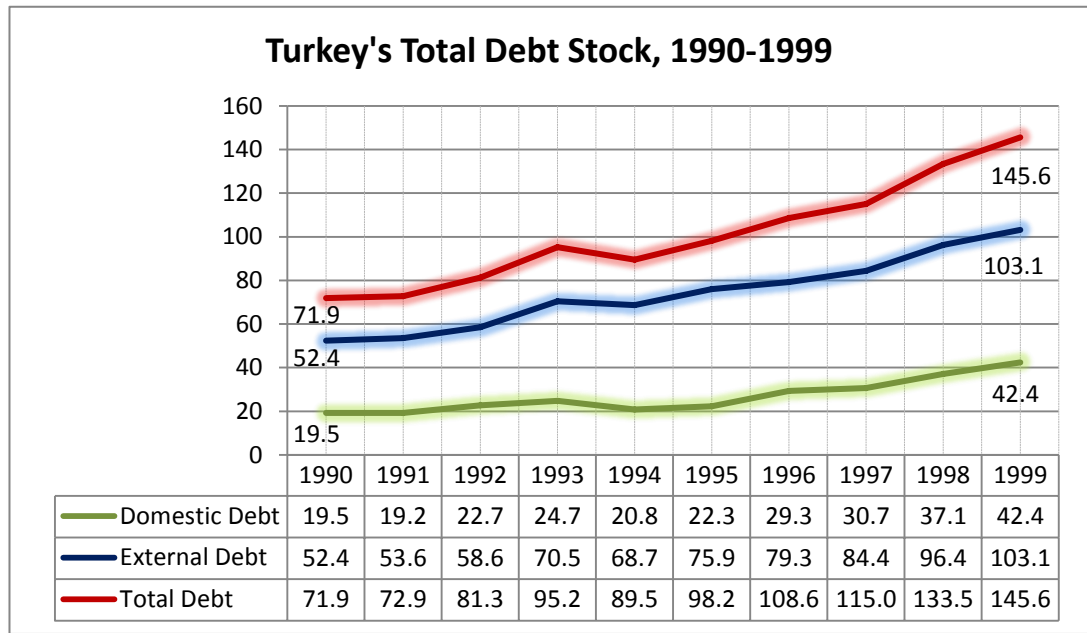
the nominal interest rates stayed above 100% during most of the decade and as a result of the rapid escalation of the domestic debt to unprecedented levels, the borrowing requirement as a ratio to GNP more than doubled and reached 9.5%.¹⁶⁷ The main feature of the domestic debt management was the extreme short-termism like in the 1970s. Net new domestic borrowings, as a ratio of the stock of the existing debt, rose to almost 50% over the 1990s. As a result, the public sector was trapped in a short term rolling of debt, a phenomenon characterized as Ponzi-financing in the fiscal economics literature.¹⁶⁸ As a result of the deficiencies in reforms towards establishing strong banking system, the number of banks increased and the concentration of assets in the larger banks declined through the period.¹⁶⁹ Furthermore, as a result of the liberalization of capital accounts, economy remained under the threat of hot money and speculative financial capital movements without any protection mechanism. Such an injection of hot money to the domestic economy enabled the financing of rising public sector expenditures on the one hand and provided relief on inflationary pressures by cheapening import costs via overvalued Turkish Lira on the other. Eventually, this ailing structure led to an uncontrolled increase in debts and vicious cycle of short term borrowing.¹⁷⁰

¹⁶⁷ Erinç Yeldan and Ebru Voyvoda, "Beyond Crisis Adjustment: Investigation of Fiscal Policy Alternatives in an OLG Model of Endogenous Growth for Turkey," 2002, pp. 1-2, <http://www.econ.utah.edu/~ehrbare/erc2002/pdf/P246.pdf>, internet access: 14.10.2011.

¹⁶⁸ Boratav and Yeldan, *op. cit.*, p. 23.

¹⁶⁹ Altunışık and Tür, *op. cit.*, p. 83.

¹⁷⁰ Korkut Boratav, Erinç Yeldan and Haşim Köse, "Globalization, Distribution and Social Policy: Turkey, 1980-1998," *CEPA Working Paper Series*, No. 20 (1999), p. 6, <http://www.newschool.edu/scepa/papers/archive/cepa0120.pdf>, internet access: 14.10.2011.



Source: UT, CBRT and TurkStat, 1990-1999, Billion US \$.

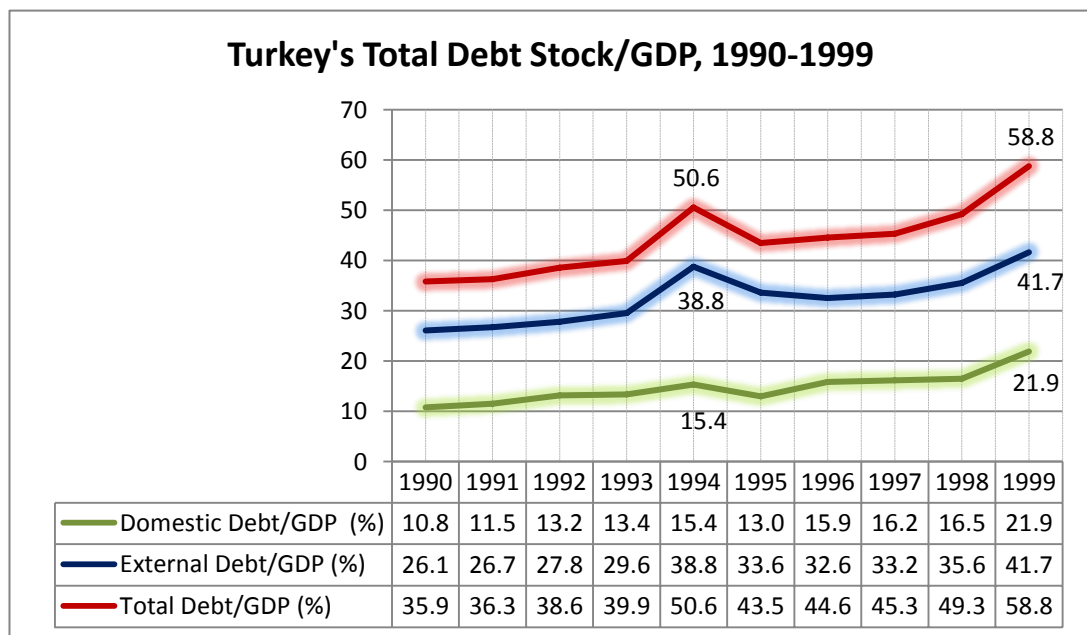
Figure 6 Turkey's Total Debt Stock, 1990-1999

Besides these internal problems and instabilities, the outbreak of the Gulf War put an additional burden on the economy. Different aspects of the economy were adversely affected from the heavy sanctions implemented on Iraq. First and foremost, Turkey lost one of its biggest energy supplier and export market, Iraq. Thus, foreign trade declined substantially. Secondly, not only trade in goods but also trade in services was negatively affected through the downturn in tourism and construction. Furthermore, the effects of the UN embargo on Iraq were heavily felt in the south eastern part of the Turkey where the economy mostly dependent on the border trade with Iraq and where the PKK was active and effective.¹⁷¹ In addition, Turkey also lost the revenues coming from the “Kerkük-Yumurtalık” oil pipeline. Actually, the prolonged armed struggle against the PKK also constituted a significant drain on the country’s resources.¹⁷² Moreover, the influx of Iraqi refugees further complicated the situation.

¹⁷¹ Aydın and Aras, *loc. cit.*, p. 27.

¹⁷² Ziya Öniş, “Turgut Özal and his Economic Legacy: Turkish Neo-Liberalism in Critical Perspective,” *Middle Eastern Studies*, Vol. 40, No. 4 (July 2004), p. 132.

High interest rates, overvalued currency and borrowing based on short term capital flows, which were proven to be unsustainable in other developing countries, made the Turkish economy more vulnerable and would create a crisis in 1994.¹⁷³ A massive devaluation of the Turkish lira, an astronomic inflation, flying interest rates and net reversal of both non-resident and resident capital flows led a sharp decline in industrial production and pushed the economy into a severe recession. With calls from the IMF and the WB, the coalition government under Tansu Çiller implemented an austerity program. With this program a transient recovery was provided but the very cause of the 1994 financial and economic crisis was not eliminated. As a result high inflation, higher interest rates and huge public deficits came back more strongly at the end of the decade.¹⁷⁴ Furthermore, the reliance on the IMF and WB left Turkey little room for to maneuver not only in economics but also in politics.



Source: UT, CBRT and TurkStat, 1990-1999, Percentage (%).

Figure 7 Turkey's Total Debt Stock/GDP, 1990-1999

¹⁷³ Ümit Sönmez, "Market and Regulatory Reforms in the Turkish Case of Neoliberalism: Maladies of a Temporal Disjunction," 2008, p. 9, <http://regulation.upf.edu/utrecht-08-papers/usonmez.pdf>, internet access: 15.10.2011.

¹⁷⁴ Altunışık and Tür, *op. cit.*, p. 84.

After the 1980s, in terms of foreign trade 1995 constituted a turning point. In this year, Turkey, as a member of the GATT (General Agreement on Tariffs and Trade) since 1951, became a member of WTO (World Trade Organization) as a developing country after signing the Uruguay Round Agreements in 1994. As being a member of the WTO, Turkey was bounded by the obligations of the agreements which were signed during the Uruguay Round. These agreements covered many crucial issues such as trade in goods and services, intellectual property, dispute settlement and the schedules of commitments. These obligations or liabilities concerning the WTO started to influence Turkey's foreign trade profoundly. The other important development of the 1995 was the establishment of Customs Union between Turkey and European Community with the adoption of the Decision 1/95 of the Association Council. With the Decision 1/95, Turkey committed to provide free movement of goods by elimination of tariff and non-tariff barriers to trade such as customs duties and quantitative restrictions; to align to the common customs tariff, including preferential arrangements, and harmonization of commercial policy measures and to approximate customs law and other laws regarding intellectual property, competition, taxation, etc. It is important to note that, while the industrial goods and processed agricultural products were covered by the Customs Union, the basic (unprocessed) agricultural products were excluded. On January 1st 1996 the Customs Union came into effect and from then on, Turkey's commitments towards the Customs Union started to influence its foreign trade, national foreign trade policy decisions and WTO policies as well. In this context, it is important to bear in mind that, although the then Prime Minister Tansu Çiller welcomed the Customs Union with great enthusiasm, Turkey was the only country that entered the Customs Union without a full membership. After the entry into force of the Customs Union, the import protection rate imposed on third countries' products decreased from 10.8% to 6%. Besides, import duties on some specific goods (car, truck, leather, shoes, ceramics, etc.) were decreased gradually. Turkey lowered import duties on these goods in 1997 by 10%, in 1998 by 10%, in 1999 and 2000 by 15% and in 2001 by 50%. After January 1st, 2001, import duties on these goods for the third countries decreased to the common customs duties level imposed by the EU. Moreover,

although basic agricultural products have been excluded from the initial package, a preferential trade regime has also been adopted in 1998 for these products. The expected positive effects of the Customs Union, such as the rapid increase in exports to and arrival of huge foreign direct investments from the Community failed to materialize in the 1990s.¹⁷⁵ Imports from the Community increased more rapidly than exports to the Community and the gap between imports and exports widened. In fact, during the period, foreign trade deficit was widened not only in favor of the EC but also in favor of the third countries such as Japan, Russian Federation, South Korea and China. Actually, even in this conditions, the adverse effects of the Customs Union with EC on the trade balance was delayed because of the substantial 1994 devaluation whose protective impacts continued to prevail during the following five years of mild appreciation.¹⁷⁶ Besides its effects on foreign trade, the formation of a Customs Union would also come to play an important role in creating an environment conducive to the eventual emergence of a “trading state”.¹⁷⁷

By the end of 1997, the anathema of the 1994 crisis, three digit inflation, high interest rates and unsustainable domestic and foreign debt, was back in stage in a stronger way. In order to overcome these problems, the coalition government implemented a rate-based disinflation and stabilization program which was designed, engineered, and monitored by the IMF.¹⁷⁸ However, government’s IMF program was far from success. In addition, 1997 Asian and 1998 Russian financial crises, public corruption, political uncertainties and weak coalition governments, 1999 Marmara earthquake, fight against the PKK and strained relations with neighboring countries added fuel to the fire. Then the same scenario played again in late 1999 and 2000. Turkey entered the new millennium in such an environment: The high level of public sector borrowing requirements and the deficit spending policies of the government

¹⁷⁵ *Ibid.*, p. 84.

¹⁷⁶ Boratav and Yeldan, *op. cit.*, p. 12.

¹⁷⁷ Kirişci, *op. cit.*, p. 33.

¹⁷⁸ Boratav and Yeldan, *op. cit.*, p. 11.

compelled the Treasury to issue high-interest bills and government bonds.¹⁷⁹ Small and medium-sized private commercial banks bought these bonds and financed these activities by borrowing short-term capital on international markets and by fiercely competing for the savings of the Turkish population in expense of investments, thereby contributing to the appreciation of the Turkish lira.¹⁸⁰ This appreciation secured access to foreign short-term funds on the one hand and deteriorated the macroeconomic imbalances on the other. The appreciated lira fuelled the imports and weakened the competitiveness of Turkish exports (at a time when the export incentive regime of the Özal period had come to an end due to the WTO obligations and the Customs Union with the EC) and eventually deteriorated the balance of trade. As credit ratings of Turkey were lowered and banks were refused to access foreign credits, liquidity crisis deepened.¹⁸¹ In addition massive outflow of resident and non-resident capital exacerbated the situation. Finally the crisis hit the country.

As stated before, the significance and magnitude of foreign trade in determining domestic and foreign policies substantially and rapidly increased during the 1980s, especially in the second half. However, in the 1990s, this trend could not be sustained in a similar pace. In fact, during the period the significance and magnitude of politics increased at the expense of foreign trade. In other words, throughout the 1990s, the significance and magnitude of military-political considerations increased in shaping the domestic and foreign policies while the preponderance of economic considerations diminished.

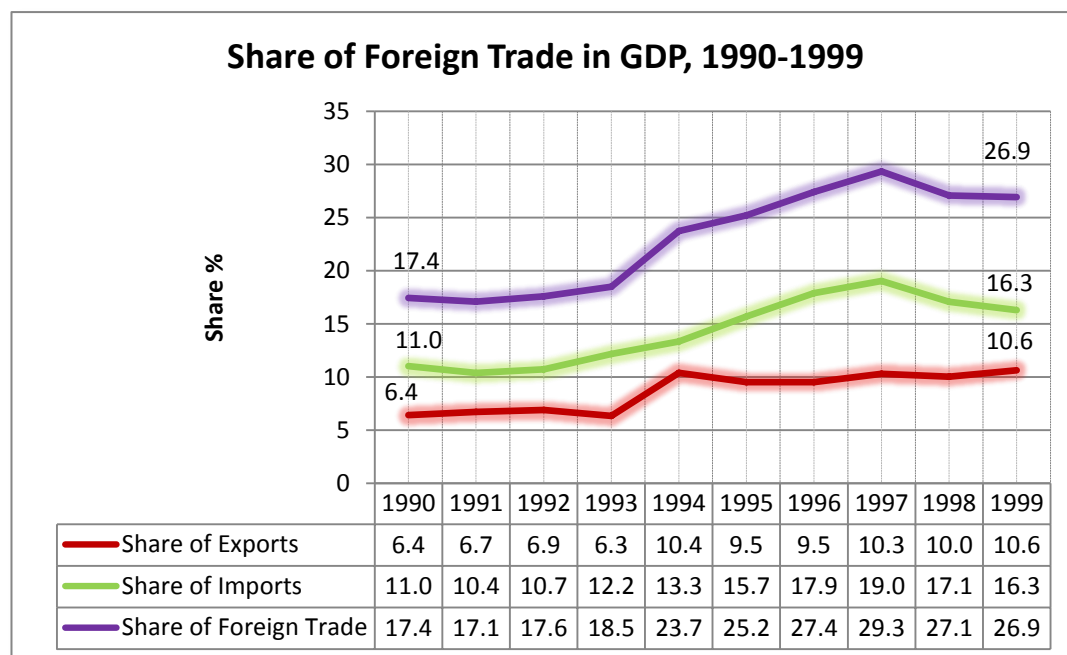
The average share of exports in GDP in the 1990s increased slightly when compared with the 1980s. In fact, during the first half of the 1990s, the share of exports in GDP decreased to the levels of ten years ago, however in the second half of the period the share increased. But the main reason behind this increase was the ups and downs in the GDP rather than the strong rise in exports. Since the rise in imports was more than exports, the share of imports in GDP increased more than

¹⁷⁹ Ümit Cizre Sakallıoğlu and Erinc Yeldan, "Politics, Society and Financial Liberalization: Turkey in the 1990s," *Development and Change*, Vol. 31, 2000, p. 486.

¹⁸⁰ Roy Karadag, "Neoliberal Restructuring in Turkey: From State to Oligarchic Capitalism," *MPIfG Discussion Paper 10/7*, July 2010, p. 18.

¹⁸¹ Altunışık and Tür, *op. cit.*, p. 85.

exports except the 1994 and 1998-99 crises. Therefore, in parallel with these developments the average share of foreign trade in GDP rose from 18% in the 1980s to %23 in the 1990s. Especially as a result of the poor performance of foreign trade in the first half of the 1990s, the share of foreign trade fell behind the levels of late 1980s, but then recovered in the late 1990s.



Source: TurkStat and IMF-World Economic Outlook Database-September 2011, Share (%).

Figure 8 Share of Foreign Trade in GDP, 1990-1999

As can be seen from the table below, during the 1990s, exports followed a slightly upward trend and doubled from \$13 billion 1990 to \$26.6 billion in 1999. The devaluation of Turkish lira in 1994 gave competitiveness to Turkish exporters and this resulted in the increase of exports from then on. However, imports followed a fluctuating course, not only increased but also decreased rapidly during the years of crises. An overvalued Turkish Lira, Turkey's membership to the World Trade Organization in 1995 and the entrance to the final stage of Customs Union with the European Community in 1996 were among the reasons of rapid growth rate of Turkey's imports. Thus imports rose by 85% from \$22.3 billion 1990 to \$40.7 billion in 1999.

Table 3 Turkey's Foreign Trade, 1990-1999

Turkey's Foreign Trade, 1990-1999									
Years	Exports		Imports		Volume		Balance		Proportion of Imports covered by Exports (%)
	Value	Change (%)	Value	Change (%)	Value	Change (%)	Value	Change (%)	
1990	13.0	11.5	22.3	41.2	35.3	28.6	-9.3	124.2	58.1
1991	13.6	4.9	21.0	-5.6	34.6	-1.8	-7.5	-20.2	64.6
1992	14.7	8.3	22.9	8.7	37.6	8.5	-8.2	9.4	64.4
1993	15.3	4.3	29.4	28.7	44.8	19.1	-14.1	72.7	52.2
1994	18.1	18.0	23.3	-20.9	41.4	-7.6	-5.2	-63.3	77.8
1995	21.6	19.5	35.7	53.4	57.3	38.6	-14.1	172.4	60.6
1996	23.2	7.3	43.6	22.2	66.9	16.6	-20.4	45.0	53.2
1997	26.3	13.1	48.6	11.3	74.8	11.9	-22.3	9.3	54.1
1998	27.0	2.7	45.9	-5.4	72.9	-2.6	-18.9	-15.0	58.7
1999	26.6	-1.4	40.7	-11.4	67.3	-7.7	-14.1	-25.7	65.4
1990-99		105.2		82.4		90.7		50.7	

Source: Republic of Turkey Ministry of Economy, 1990-1999, Billion US \$, Annual Change (%).

During the period, average growth rate of exports and imports was 8.8% and 12.2% respectively and despite following a fluctuating course, the trend was upside. Contrary to the 1980s, during the period, foreign trade deficit increased by 51% from \$9.3 billion in 1990 to \$14.1 billion in 1999, while volume of foreign trade increased by 91% from \$35.3 billion to \$67.3 billion. More important, as a result of the growing imbalances in foreign trade, exports financed on average 61% of the imports. This ratio declined rapidly from 81% in 1988 to 59% in 1998.

During the entire 1990s, the significance of the European markets in Turkey's foreign trade grew while Germany became the number one trade partner of Turkey in both exports and imports. In other words, the diversity of markets in the 1980s, gave its place to dependency on mostly European markets in the 1990s, especially after the Customs Union. Actually, after the end of the bipolar world system and the dissolution of the Soviet Union and Eastern Block, new trade markets for Turkey emerged in Central Asia and Caucasus, East Europe and Balkans. Turkey's proximity to the region gave an opportunity to Turkey to enhance its exports to these

countries. However, the impacts of this change started to be seen in the late 1990s and especially in the 2000s. On the other hand, as a result of the political turmoil in the Middle East and political tensions with some of these countries result in the decline of the region in Turkey's foreign trade, therefore the exports to Middle East couldn't have shown a desirable progress in 1990s. Besides Germany, the US and other leading European countries, Russian Federation and Saudi Arabia came to the fore as the biggest crude oil and natural gas suppliers. The number of export and import markets surged from around 130 in 1990 to 200 and 180 in 1999 respectively. However, despite this increase in the number of these markets, almost 60% of the exports and imports were made with the first ten markets.

The composition of the exported goods in the 1990s, changed in the direction of industrial products. From 1990 to 1999, according to International Standard Industrial Classification of All Economic Activities (ISIC Rev.3), the share of industrial products in total exports increased from 80% to 90%, while the shares of agricultural and mining products decreased from 17% to 9% and from 3% to 9% respectively. Within the same period, a parallel trend to exports observed in the composition of imports. The share of industrial products in total imports increased from 76% to 83%, while the shares of mining and agricultural products decreased from 19% to 10% and from 5% to 4% respectively.

In addition, according to System of National Accounts (SNA) classification, despite the decline in its share, intermediate goods still constituted the largest part of Turkey's imports and it was followed by capital and consumption goods. Conventionally, the import of intermediate goods constitutes an important part of total imports and follows a parallel trend with Turkey's economic growth. When this correlation is kept in mind, as a result of the growth-crisis-stabilization cycle, imports of intermediate goods showed a downtrend, while the consumption and capital goods showed an opposite trend. Especially, after 1996, the policy implementation of international liabilities arising from the WTO membership and Customs Union, paved the way for a rapid growth in the imports of consumption goods. Therefore, in ten years the share of intermediate goods dropped from 72% to 67%, while the shares of capital and consumption goods increased from 18% to 22%

and from 10% to 11%. On the exports side, the structure changed in the direction of investment goods. While the share of investment goods jumped from 2% to 7%, the share of intermediate goods fell from 47% to 41% and the share consumption goods rose slightly from 51% to 52% in ten years.

During the 1990s, crude oil and natural gas, motor cars and other motor vehicles, ferrous waste and scrap, coal, electrical machinery and equipment and parts thereof, helicopters and aeroplanes and cotton were among the most imported products. Moreover, through the late 1990s, imports of mobile phones jumped substantially. On the exports side, articles of apparel and clothing accessories, iron and steel, fruit and nuts, cotton and unmanufactured tobacco were the most exported products. In addition by the late 1990s, with the positive impact of Customs Union, exports of motor cars and other motor vehicles increased gradually. In fact, as in the 1980s, the process was accompanied by a diversification of exports, involving a striking increase in the exports of manufactured goods. In fact, Customs Union positively affected the quality of the industrial production. In order to survive the harsh competition of high quality products of Europe, Turkish companies were compelled both to improve the quality and to mark down the price of their products. The expansion of exports during the decade was accompanied by the rise of new industrial centers across Anatolia, this new business elite, namely the Anatolian Tigers, increased their export oriented productions during the period.

As mentioned before, another striking phenomenon of the 1990s was the simultaneous rise of the political Islam in domestic politics and the Islamic capital in domestic economics. In this context, the Welfare Party (WP) came to power and its leader Necmettin Erbakan became the Prime Minister in 1996. This Islamic party was enthusiastically supported by the MÜSİAD (the representative of the Anatolian capital which was established through the cheap credits provided in the period of Özal) and Islamic financial institutions.¹⁸² And the WP was indeed voicing the position and the interests of this newly emerging, but still peripheral, industrialist

¹⁸² Baskın Oran, "Dönemin Bilançosu: 1990-2001", in Baskın Oran, (Ed.), *Türk Dış Politikası: Kurtuluş Savaşından Bugüne Olgular, Belgeler, Yorumlar (1980-2001)*, Vol. II, 6th ed., İstanbul, İletişim Yayınları, 2003, p. 219.

class.¹⁸³ In other words, the transformation of the WP from a marginal power to a significant political movement was a parallel phenomenon to and a reflection of the growing power of Islamic business in the Turkish economy and society in the course of the 1990s.¹⁸⁴

The industrialists and businessmen who were unable to find any representation in the chambers and existent organizations of the business class established the MÜSİAD in 1990 in order to unite and represent the interests of the pro-Islamist SMEs that proliferated rapidly in the 1980s and 1990s.¹⁸⁵ Put it another way, MÜSİAD represents the new and the peripheral segments of the business class that supported political Islam and the emergence of MÜSİAD during the 1990s was closely associated with the economic and political challenge of the rising Islamic capital from inner Anatolia. In a few years after the foundation, members of the organization have grown rapidly to around 3000 individual companies.¹⁸⁶ With the exception of some large companies, most of the MÜSİAD's member companies were the SMEs which were established after 1980 and these SMEs started to scale up in the 1990s. In addition, contrary to TÜSİAD, the members of the MÜSİAD swept all over the country, both the major metropolitan centers such as Istanbul, Kocaeli, Bursa, Izmir and the key traditional inner Anatolian cities such as Konya, Kayseri and Gaziantep as well.

Since its formation, the WP has announced its policies against the European Union and NATO. Erbakan advocated what he called an Islamic Common Market and even an Islamic NATO.¹⁸⁷ Very much in line with the basic stance of the WP, at the peak of its influence, MÜSİAD desired a reorientation of Turkey's economic and also political relations towards the Middle East and Islamic world in general.¹⁸⁸ As

¹⁸³ Haldun Gülalp, "Globalization and Political Islam: The Social Bases of Turkey's Welfare Party," *International Journal of Middle East Studies*, Vol. 33, No. 3 (August 2001), p. 438.

¹⁸⁴ Ziya Öniş, "The Political Economy of Islamic Resurgence in Turkey: The Rise of the Welfare Party in Perspective," *Third World Quarterly*, Vol. 18, No 4 (1997), p. 760.

¹⁸⁵ Gülalp, *op. cit.*, p. 439.

¹⁸⁶ Cizre Sakallıoğlu and Yeldan, *op. cit.*, p. 500.

¹⁸⁷ Kemal Kirişçi, "Turkey's Foreign Policy in Turbulent Times," *Chaillot Paper*, No.92 September 2006, p. 88.

¹⁸⁸ Öniş and Türem, *op. cit.*, p. 449.

Öniş emphasized, in harmony with the stance of the WP, what is unique to MÜSİAD was a strong rejection of the Customs Union with Europe and a corresponding emphasis on the need to reorient the country's economic relationship and foreign policy stance away from the West towards a closer union with the Islamic world.¹⁸⁹ Moreover, in MÜSİAD's obviously Eastern-oriented strategy, the idea of the Islamic solidarity and the economic integration among Muslim countries could be used with a view to secure markets in Muslim regions and strengthen the links with the real tigers of East Asia.¹⁹⁰

However, the winds have changed for MÜSİAD following the collapse of the coalition government in 1997 and the prohibition of the WP in 1998. Following the February 28 process, the activities of business establishments with close links to MÜSİAD came under increasing scrutiny of state agencies, resulting in a relative decline in membership towards the end of the 1990s.¹⁹¹ Despite gaining considerable power, the overall weight of the MÜSİAD's membership in the Turkish economy was still marginal compared to the TÜSİAD, the rival business association with a secular, Western orientation representing the big business and large conglomerates located in the Marmara region of Turkey.

By defending the collective interests of big business, TÜSİAD continued to play an important role in the 1990s. The influence of the economic, political and social characteristics of the European model that can be said to define TÜSİAD's general outlook, could also be perceived in the association's choices of foreign trade policies. The strategic vision of the association thus included a pro-European policy orientation advocated on both economic and political grounds.¹⁹² Nevertheless, the evolution of the association and its explicit agenda for democratization did not mean that TÜSİAD's interest in economic issues retreat into the background. It continued

¹⁸⁹ Öniş, "The Political Economy of Islamic Resurgence in Turkey: The Rise of the Welfare Party in Perspective," p. 759.

¹⁹⁰ Ayşe Buğra, "Class, Culture, and State: An Analysis of Interest Representation by Two Turkish Business Associations," *International Journal of Middle East Studies*, Vol. 30, No. 4 (November 1998), pp. 531-532.

¹⁹¹ Öniş and Türem, *op. cit.*, pp. 447-448.

¹⁹² Buğra, *op. cit.*, pp. 526-527.

to display considerable interest in issues concerning to the implementation of the Customs Union, the reform of state finances, and other major economic issues of the day. In fact, since the democracy is conceived as a mechanism to reach the ultimate goal and receive the benefits of full EU membership and economic globalization, an explicit democratization issue was on the top of the TÜSİAD's agenda during the 1990s and this agenda sharply contrasted with the association's single-minded interest in economic issues in the 1970s and 1980s.¹⁹³

3.2. Turkey's Political Relations with Iran in the 1990s

Unlike the 1980s, the main parameters that have been decisive on the relations between Turkey and Iran have been political in nature rather than economical. Correspondingly in the 1990s, with the fading away of the pragmatism and optimism, Turkey and Iran had difficulties in finding common grounds to cooperate. The developments throughout the 1990s have tightened relations between the two than soften. As Aydın and Aras emphasized, during the period the main determinants of the fate of bilateral trade relations in the Middle East are mainly politics rather than economics¹⁹⁴ and Turkish-Iranian trade relations throughout the 1990s did not constitute an exception in that sense and political issues have been decisive on trade relations of aforementioned parties.

In this new chaotic era, it is possible to classify political shifts which have reflections on trade relations between Turkey and Iran in three levels; namely international, regional and bilateral. The main shift in the international system was the demise of bipolar world order. By the collapse of Soviet Union, the breakup of the Eastern Bloc and the emergence of new states in Central Asia and Caucasus, new variables and unknowns were added to the equation of Turkish-Iranian relations. Aforementioned uncertainties firstly drove Turkey and Iran into a competition and thereafter into a so-called cooperation. When regional level is considered, Middle

¹⁹³ Öniş and Türem, *op. cit.*, pp. 442-447.

¹⁹⁴ Aydın and Aras, "Ortadoğu'da Ekonomik İlişkilerin Siyasi Çerçevesi; Türkiye'nin İran, Irak ve Suriye ile Bağlantıları," pp. 103-106.

Eastern sub-system was as chaotic as the international system itself. The outbreak of Gulf War after the Iraqi invasion of Kuwait wrecked the balance of power in the region. Especially, the influence of the hegemon, the US, in the region has considerably increased. With the Gulf War the presence of the US has gone beyond political and economic influence; now it has been physically prevalent in the region. The Kurdish question, which located in the triangle of Turkey-Iran-Iraq and intensification of PKK terrorism, was unsettling all the relations among these countries. Within this environment, new alliances were established or already existed alliances were strengthened. While the Arab-Israeli conflict was escalating, Turkey was aligning to Israel whereas Iran was strengthening its alliance with Syria. Turkey's alliance with Israel was welcomed by the US, whereas it was receiving negative reaction from the Arab world. In bilateral relations, together with these changing parameters, ideological frictions which were accustomed to be ignored throughout the 1980s were coming into sight. Now the secular Turkey and the theocratic Iran came across and challenged each other. Moreover, the 1990s was a period that the political Islam and Islamic capital were gaining ground and threatening the status quo, counter-statements, fierce criticisms, assassination of some prominent Turkish intellectuals, support for the opposition groups and the use of PKK as a trump card were all putting strain not only on political but also on commercial relations between Turkey and Iran.

In conclusion, this new geopolitics of Turkey and Iran, and the internal developments in these countries established a sense of competition and an atmosphere of conflict between the two countries. In addition, the tensions, ideological frictions and mutual distrust between the two further exacerbated the already conflictual process.¹⁹⁵ However, developing joint projects towards the areas where the two states competed would have a potential to increase cooperation and to encourage better relations between Turkey and Iran.

Throughout the 1990s, aforementioned political developments posed a huge obstacle for the expansion of bilateral trade relations. Mutual economic

¹⁹⁵ Bayram Sinkaya, "Turkey-Iran Relations in the 1990s and the Role of Ideology," *Perceptions Journal of International Affairs*, Vol. 10, No. 1 (Spring 2005), p. 15.

interdependence created by the economic transformation of Turkey and the Iran-Iraq War have faded away towards the end of the 1980s. Nonetheless, it was impossible for a rupture of trade relations altogether because, although the parties were politically independent, they were economically interdependent. Turkey was dependent on Iran as it was in dire need of new markets to offer its products to supply and energy supplies, crude oil and natural gas, which were vital for its economy. On the other hand, Iran was dependent on Turkey with a view to reach both Turkish and more important, European markets to sell its hydro-carbon resources in return for required capital, intermediary and consumer goods.

Hence in the 1990s, although Turkey was earning a reputation for being a coercive regional power with respect to a number of bilateral conflicts and “high politics” issues, there was also a dimension of Turkish foreign policy that was composed of cooperation and dialogue especially on “low politics” issues.¹⁹⁶ This approach was also critical because it reflects the efforts of raising the influence of commercial and economic interests in the process of foreign policy-making by the emerging actors both inside and outside the state in addition to the traditional actors such as the Ministry of Foreign Affairs and military. As Kirişci clearly explained, according to the nature of a trading state, a wider range of actors come to participate in foreign policy-making or diplomatic games and the interests and priorities of these actors are quite different from those of traditional foreign policy-makers.¹⁹⁷ In reality, the rising pro-Islamist business circles and traditional big business circles of the Marmara region to some degree were in favor of conducting trade with Iran. However, it was not easy to verbalize such demands when the conditions and tensions of the era were considered. In this context, during the 1990s, issues of crude oil and natural gas trade and pipelines, border trade, ECO and D-8 were on the top of the bilateral trade agenda on which Turkey and Iran were aiming to maximize their gains.

¹⁹⁶ Kirişci, “Turkey’s Foreign Policy in Turbulent Times,” p. 32.

¹⁹⁷ Kirişci, “The Transformation of Turkish Foreign Policy: The Rise of the Trading State,” pp. 33-34.

Within this perspective, the political conditions of bilateral trade relations between Turkey and Iran, issues on the bilateral trade agenda and data of bilateral trade will be analyzed respectively.

During the most part of the 1990s, Turkey tackled with serious internal problems and perceived its neighborhood, as well as Iran, through the lens of national security. By the mid-1990s the legacy of Özal with regard to foreign policy making and the substance of foreign policy gradually changed.¹⁹⁸ Turkish foreign policy-making at the time was mainly dominated by the military establishment and the Ministry of Foreign Affairs.¹⁹⁹ As mentioned before, in the 1980s the authority and the efficacy of the Ministry of Foreign Affairs was eroded. Both the Ministry of Foreign Affairs and the military institutions perceived threats to Turkey's unity and territorial integrity emanating from foreign powers (dış mihraklar) around Turkey. Throughout the period, this perception paved the way for a state of escalated tensions with immediate neighbors including Iran. In his prominent article "2½ War Strategy", Şükrü Elekdağ, a retired ambassador and former Deputy Undersecretary of the Ministry of Foreign Affairs, put forward the idea that Turkey was under the threat of a simultaneous war coming from Greece, Syria and PKK and adopted the adage of "those who want peace, must be prepared for war" in return.²⁰⁰ This thesis was also strengthened by a conviction that Turkey was being encircled by an 'alliance' composed of Greece, Russia, Armenia, Iran and Syria.²⁰¹ This perception is a key to understand the mood of the 1990s and to reflect the mentality of the period clearly. As a result, during the 1990s Özal's relatively liberal approach towards the Kurdish problem, Islam and international relations faded away and an approach that emphasized the threat to Turkey's national security, territorial integrity and secular quiddity of state came to the fore.²⁰² During the period, Turkey was swamped with

¹⁹⁸ Kirişçi, "Turkey's Foreign Policy in Turbulent Times," p. 12.

¹⁹⁹ Kirişçi, "The Transformation of Turkish Foreign Policy: The Rise of the Trading State," p. 31.

²⁰⁰ Şükrü Elekdağ, "2½ War Strategy," *Perceptions*, No. 1 (1996).

²⁰¹ Kirişçi, "Turkey's Foreign Policy in Turbulent Times," p. 15.

²⁰² *Ibid.*, p. 12.

economic and political instabilities and successive coalition governments failed to deal with the country's economic and political structural problems.

3.2.1. The End of Cold War and the Dissolution of USSR

The 1990s signalled the coming up of a new and chaotic period. After the sudden end of the Cold War, Turkey found itself in the very midst of a turbulent region with serious conflicts erupting in the Balkans, the Caucasus and the Middle East.²⁰³ The new geopolitics of Iran and Turkey which emerged in the wake of the dissolution of the USSR generated a short-lived but severe competition between the two countries over the Caucasus and the Central Asia and produced a conflictual atmosphere in bilateral relations.²⁰⁴ Furthermore, disappearance of the earlier concerns expressed by Turkey about a possible entrance of Iran into the Soviet sphere of influence, probably made Turkey more comfort about defend its interests and challenge Iran if necessary.

3.2.2. Newly Independent States of Central Asia and Caucasus

Actually, both Turkey and Iran were surprised by the collapse of the USSR, because they did not anticipate such a development and until that time, both of them had adopted Moscow-centered policies in their relations with the newly independent states.²⁰⁵ However, the surprise quickly ended and was followed by “euphoria period” both in Turkey and Iran until mid-1990s. Both countries tried to derive a great deal of benefit from and to project their influence in these newly emerging states and land-locked markets as well, by using their historical, cultural, religious, linguistic ethnic and geographic affinities. Turkey, which expected to increase its diminishing strategic role in the eyes of the West and strived to guarantee the access to vital energy resources and rich export markets, lucrative oil and natural gas, turn into a transit hub that connects the suppliers in the Middle East and Central Asia to

²⁰³ *Ibid.*, p. 12.

²⁰⁴ Sinkaya, *op. cit.*, pp. 1-8.

²⁰⁵ *Ibid.*, pp. 11-12.

the big consumers in Europe and thus surge transport revenues, as well as improve its diplomatic dominance against others. Moreover, Western encouragement of Turkey to serve as “a model” for these newly emerging states perpetuated Turkish euphoria.²⁰⁶ Iran for its part, anticipated to fill the vacuum in these newly independent “Muslim” states, to break the political and economic isolation and sponsored the “Iranian model” for structuring and development of these economies.

As a result, both Turkey and Iran started to implement ambitious economic and political policies towards these regions and entered into a rivalry. Nevertheless, in the course of time, both countries realized the individual limits and inadequacies of their financial and political capabilities for undertaking ambitious projects and filling the vacuum in the region. As Gökhan Çetinsaya indicated, since Iran served as a land corridor to the Caucasus and Central Asia for Turkey and Turkey served as a gateway to the West for Iran, the two states refrained from alienating each other and escalating the conflicts and having awakened to this fact, they managed to cooperate on economic and security issues, and improved their bilateral relations.²⁰⁷ Previously only Turkey hold the status of transit country for Iran, but now with the emergence of newly independent states of Central Asia and Caucasus Iran also became a transit country for Turkey and increased its importance. Both countries used the trump card of being a transit country against other as the competition between them escalated. Furthermore, after recovered its power, Russian Federation came back to its backyard. Thus, it became obvious that Russian Federation would not tolerate their regional influence, hence limiting the two countries competition and engagement over the Central Asia and Caucasus.²⁰⁸ As a result, the US exerted its influence in order to counterbalance Russia. That’s why Turkey and Iran put an end the competition and took steps towards cooperation concerning the Caucasus and Central Asia.

²⁰⁶ Bulent Aras and George K. Foster, “Turkey and the Azerbaijani oil controversies: looking for a light at the end of the pipeline,” *Research Institute for European and International Studies*, Special Report, Athens, 1998, p. 1.

²⁰⁷ Gökhan Çetinsaya, “Rafsanjani’den Hatemi’ye İran Dış Politikasına Bakışlar,” in Mustafa Türkeş and İlhan Uzel, (Eds.), *Türkiye’nin Komşuları*, Ankara, İmge Kitabevi, 2002, pp. 293-329.

²⁰⁸ Nilüfer Karacasulu and İrem Aşkar Karakır, “Iran-Turkey relations in the 2000s: Pragmatic Rapproachment,” *Ege Academic Review*, Vol.11, No.1 (January 2011), p. 112.

As a first step, in 1992, the ECO was eventually reinvigorated with the participation of seven new members, six of them were the newly independent states of Central Asia, namely Azerbaijan, Kazakhstan, Turkmenistan, Uzbekistan, Tajikistan, Kyrgyzstan and Afghanistan. The participation of these new members in the activities of the Organization commenced after their formal accession to the Treaty of Izmir at an extraordinary meeting of ECO Council of Ministers held in Islamabad on May 1992. While expanding the ECO, Turkey and Iran expected to find new markets for their manufactured goods and maintain access to the energy and non-energy raw materials of these new members and facilitate the sustainable supply of raw materials that were essential for the national industrial production, in best possible prices. However, despite the expansion of the organization, ineffectiveness of the ECO continued in the 1990s as in the 1980s. One of the reasons behind this inefficiency was the Turkish-Iranian rivalry, which did not allow the organization to flourish further.²⁰⁹ However, the main reason was indeed structural. Since most of the members were underdeveloped countries that produce and export raw materials and intermediary goods, members could not meet the needs of each other and intra-ECO trade remained limited. In fact Turkey and Iran differentiate from other countries with regard to industrial production but the quality, quantity and diversity of the products still fell behind the demand.²¹⁰ Nonetheless, despite its ups and downs, ECO has continued to be important in terms of promoting regional cooperation.²¹¹

However, the efforts of cooperation did not mean that the competition is over. In fact, competition was and is continuing in different areas and in different shapes. For instance, throughout the 1990s, Turkey worked hard for the adoption of the Baku-Tbilisi-Ceyhan (BTC) pipeline project that envisaged transporting Caspian oil

²⁰⁹ Aydın and Aras, "Political Conditionality of Economic Relations between Patrimonial States: Turkey's Interaction with Iraq, Iran and Syria", p. 26.

²¹⁰ Atay Akdevelioğlu and Ömer Kürkçüoğlu, "İran'la İlişkiler: 1990-2001", in Baskın Oran, (Ed.), *Türk Dış Politikası: Kurtuluş Savaşından Bugüne Olgular, Belgeler, Yorumlar (1980-2001)*, Vol. II, 6th ed., İstanbul, İletişim Yayınları, 2003, pp. 583-586.

²¹¹ Bülent Aras, "Turkish Foreign Policy towards Iran: Ideology and Foreign Policy in Flux," *Journal of Third World Studies*, No. 18 (1), 2001, p. 116.

via Turkey. Since the BTC meant bypassing of Iran, it persistently opposed the project but did not prevent the adoption of it.²¹²

3.2.3. Middle East, Gulf War and the PKK

A similar competition between Turkey and Iran was also evident in the Middle East. In the post-Cold War and post-Gulf War period, the Middle East has remained in flux geopolitically as well as geoeconomically.²¹³ As a result of the aforesaid endogenous and exogenous developments, Turkish foreign policy towards the Middle East started to transform since the late 1980s. The reconsideration of Turkish foreign policy towards the Middle East culminated in a more active involvement in the region throughout the 1990s. Except the terms of Özal's presidency and Erbakan's prime ministry, Turkey followed cautious and conservative foreign policies and avoided to be drawn into regional conflicts traditionally.²¹⁴ Iraqi invasion and annexation of Kuwait in 1990 eventuated in US-led war against Iraq in 1991 and the war came to an end with political, economic and humanitarian devastation of Iraq by the armed forces of coalition. By supporting Washington's Iraq policy, Turkey expected to reiterate its strategic importance, at a time when Turkey was uncertain about its role in the new world order.²¹⁵ In addition, Turkey also made possible the creation of a safe haven for Kurds in northern Iraq, while deploying a military presence in the area to combat the PKK.²¹⁶

Subsequent power vacuum of the Gulf War led to another rivalry for Turkey and Iran. Despite the consensus about developing similar attitudes towards the establishment of an independent Kurdish State and sustaining the territorial integrity

²¹² Bayram Sinkaya, "Turkey-Iran Geopolitical Competition Over Central Asia and the Caucasus: 1989-2001," *Avrasya Etüdleri*, Vol. 12, No. 27-28 (2005), pp. 93-94.

²¹³ Calabrese, *op. cit.*, pp. 75-94.

²¹⁴ Hüseyin Bağcı, "Changing Geopolitics and Turkish Foreign Policy," *Sozialwissenschaftliche Schriftenreihe Reihe Studien*, Juni 2009, p. 9.

²¹⁵ Meliha Benli Altunışık, "Turkey's Changing Middle East Policy," *UNISCI Discussion Papers*, No. 23 (May 2010), p. 150.

²¹⁶ Kemal Kirişçi, "Between Europe and the Middle East: The Transformation of Turkish Policy," *Middle East Review of International Affairs*, Vol. 8, No. 1 (March, 2004), p. 40.

of Iraq, they occasionally differed seriously about Iraq. For instance, Turkey wanted Saddam Hussein to cooperate with the international community to end economic sanctions and wanted Baghdad to reestablish control over all Iraqi territory while Iran wanted the Baghdad regime weakened and thwarted by stringent UN sanctions. Moreover, since the balance of power considerations have been an important aspect of bilateral relations, any attempt by one of the countries to modify the balance to its own favor disturbed the other.²¹⁷ As regional powers, Turkey and Iran were always crucial in the struggle for regional stability and prosperity. Therefore, stable Turkish-Iranian relations are essential to the stability of the region.²¹⁸ Thus, how Turkey and Iran display their power, with whom they align, and whether they can manage or overcome their differences is vitally important not only for bilateral relations, but also for regional balances.

During the 1990s, Turkey became steadily more involved in the region, because of the power vacuum left by the Gulf War in northern Iraq from where the PKK was able to mount operations into Turkey. As mentioned before, since the economic sanctions against Iraq paved the way for aggravation of already dire economic conditions, contraction of trade levels and decline in income especially in the southeastern part of Turkey which was heavily populated by Kurds, the situation was further deteriorated. This economic disruption induced the violence that characterized the region during the 1990s. Additionally, this power vacuum in the northern Iraq stirred up the Turkish-Iranian rivalry. Despite their agreement on the territorial integrity of Iraq, Turkey and Iran did not trust each other with regard to northern Iraq and they remained suspicious of the other, which made competition between the two countries inevitable.²¹⁹ The situation was further complicated by the covert or overt assistance that neighboring countries, namely Iran and Syria, provided to the PKK.²²⁰ During the whole period, PKK operations originating from Iran also adversely affected Iran-Turkish relations. Turkish authorities constantly

²¹⁷ Altunışık, *op. cit.*, p. 154.

²¹⁸ Calabrese, *op. cit.*, pp. 75-94.

²¹⁹ Sinkaya, "Turkey-Iran Relations in the 1990s and the Role of Ideology," pp. 8-9.

²²⁰ Kirişçi, *loc. cit.*, p. 46.

accused Iran of giving the PKK training, health and logistic support, sheltering the PKK militants and encouraging its attacks inside Turkey. However, Iran always denied these accusations, but continued PKK attacks in areas adjacent to the border have frequently brought tensions between the two countries.²²¹ Furthermore Iran, responded to the Turkish complaints about PKK activities by arguing that Turkey should make more effort to stop the activities of Iranian opposition groups, especially the Mujahedeen-e Khalq Organization, on its territory.²²² These mutual allegations and criticisms created many tensions, including commercial ones, between Turkey and Iran throughout the 1990s. For instance, Turkey detained an Iranian flagged vessel, the Cap Maleas, in transit from Bulgaria, on suspicion that it was carrying arms for the PKK, in 1991. Moreover, some Turkish contingents went into Iranian territory in pursuit of PKK militants in August 1992 despite the absence of a hot-pursuit agreement between Turkey and Iran.²²³ Furthermore, after the capture of Abdullah Öcalan in February 1999, Turkey-Iran relations entered a more difficult phase. Turkish Prime Minister Bülent Ecevit said in July 1999, “We have some complaints against Iran. The PKK’s existence in Syria became nearly extinct, but Iran seems to take the place of Syria”.²²⁴ During the period, similar tensions were repeated in several times as a result of the friction between Turkey and Iran relating to the PKK. These incidents harmed bilateral relations and hindered cooperation efforts.

3.2.4. Alliances and Animositities with Third Parties

Besides the impact of ideology and internal developments in Turkey and Iran, their alliances and animositities with third parties also adversely affected the Turkish-

²²¹ Kemal Kirişçi, “Post Cold-War Turkish Security and the Middle East,” *Middle East Review of International Affairs*, Volume 1, No. 2 (July 1997), <http://meria.idc.ac.il/journal/1997/issue2/jv1n2a6.html>, internet access: 16.11.2011.

²²² Sinkaya, *loc. cit.*, p. 9.

²²³ Atila Eralp and Özlem Tür, “İran’la Devrim Sonrası İlişkiler”, in Meliha Benli Altunışık, (Ed.), *Türkiye ve Ortadoğu, Tarih, Kimlik, Güvenlik*, İstanbul, Boyut, 1999, pp.94-95.

²²⁴ Ayşegül Sever, “Turkey’s Stance on Dual Containment”, *Journal of South Asia and Middle Eastern Studies*, Vol. 24, No. 2 (Winter 2000), p.66.

Iranian relations in the 1990s. To begin with, Iran's stressed relations with the US, and the dual containment policy directed against Iran hindered the improvement of bilateral relations between Turkey and Iran. While the US opposed Turkey's any initiative to cooperate with Iran, Iranian leaders denounced Turkey's close relations with the United States.²²⁵

Furthermore, Turkey's alignment with Israel put an additional strain on relations between Ankara and Tehran.²²⁶ When Iran's hostile attitude towards Israel and its alliance with Syria were taken into consideration, it is natural for Iran to perceive this rapprochement as a new US strategy to contain Iran. Arab world also bitterly criticized Turkey for its close relations, which were dominated by the military sector, with Israel.²²⁷ However, this discontent did not prevent Turkey to sign a free trade agreement (FTA) with Israel in 1996. As being one of the most prominent and effective FTA of Turkey which was signed during the 1990s, Turkish-Israeli FTA had significant repercussions for the strategic balance in the Middle East.²²⁸ As an indication of this aversion, Iran and some of the Arab countries which led by Syria, tried to get the Organization of the Islamic Conference to adopt a decision critical of Turkey's relations with Israel in Tehran Summit in 1997.²²⁹ As a result the then President Süleyman Demirel left the summit untimely and returned to Turkey hastily.²³⁰ In a nutshell, the Turkish-Israeli and Iranian-Syrian alignment mutually triggered and reinforced the strategic partnership and coordination of regional policies between parties; exacerbated the threat perceptions of Turkey and Iran from each other and put another obstacle to the trade relations that had to be over jumped by the business class.

²²⁵ Sinkaya, *loc. cit.*, p. 8.

²²⁶ Bülent Aras, "Turkish-Israeli-Iranian Relations in the 1990s and Their Impact on the Middle East," *Middle East Policy*, Vol. 7, No.3 (2000), pp. 153-154.

²²⁷ Kirişçi, "Turkey's Foreign Policy in Turbulent Times," pp. 62-63.

²²⁸ Mine Eder, "The Challenge of Globalization and Turkey's Changing Political Economy," in Barry Rubin and Kemal Kirişçi, (Eds.), *Turkey in World Politics: An Emerging Multiregional Power*, Colorado & London, Lynne Rienner Publishers, 2001, p. 194.

²²⁹ Kirişçi, "Between Europe and the Middle East: The Transformation of Turkish Policy," p. 40.

²³⁰ Demirel, İKÖ Zirvesini terk edip döndü, *Milliyet*, 11.12.1997, <http://gazetearsivi.milliyet.com.tr>, internet access: 06.11.2011.

3.2.5. Ideological Frictions and the Rise of Political Islam

Moreover, internal developments in these two countries further deteriorated the situation. Ideological differences between Turkey and Iran reached its peak in the 1990s and twice resulted in reciprocal withdrawals of ambassadors. During the period, Iran frequently exploited political Islam or the Kurdish problem in Turkey at a time when both were perceived as serious threats to the Turkish regime. Indeed, there was ample evidence of Iranian involvement in support of the PKK as well as the Turkish Hizbullah. Turkey felt itself to be very vulnerable to Iranian interference and these would lead to serious mistrust and conflicts between Iran and Turkey.²³¹ As a result, not only state officials, but also journalists, intellectuals, writers, businessmen and exiled opponents came across with Iran and its appendages. Throughout the period, Turkey witnessed increasing acts of violence including assassinations and attacks of radical Islamist movements which were targeted the secular intellectuals such as Muammer Aksoy, Bahriye Üçok, Çetin Emeç and Uğur Mumcu and the Turkish businessman of Jewish origin, Jak Kamhi. These terrorist attacks provoked a sharp reaction from Turkish public opinion: huge street demonstrations in favor of the secular regime, a strong press campaign, and swift action by security authorities against the perpetrators and their sponsors. For the first time the Islamic Movement and Iran were directly accused of and implicated in acts of terror against the Turkish state.²³²

As a result of these incidents, the tensions between Turkey and Iran rapidly escalated. In this stressed period, as reflections of negative effects of deepening frictions and mutual accusations on commercial relations, Turkish Eximbank declared that it will not provide export credits to the directed to Iran. Furthermore, a few months later Turkey stopped the entrance of Iranian vessels into Turkey. In response, Iran also raised difficulties to Turkish transporters who were on the way of

²³¹ Kirişçi, Turkey's Foreign Policy in Turbulent Times," p. 71.

²³² Ely Karmon, Radical Islamic Political Groups in Turkey, *Middle East Review of International Affairs*, Vol. 1, No. 4 (December 1997), <http://meria.idc.ac.il/journal/1997/issue4/jv1n4a2.html>, internet access: 16.11.2011.

Turkmenistan via Iran.²³³ Neither the political disagreements nor the economic competition between these two countries by itself engendered these steps; *a fortiori* the actual reason was a kind of mixture of politic and economic competition.

However, this stressed period with Iran ruptured with the coming to the power of Erbakan, the leader of the Islamic Welfare Party. Erbakan at that time, tried to change the traditional attachments of the Turkish foreign policy. In this respect, Erbakan advocated to emphasize the Islamic character of Turkey, to keep the West in arm's length while developing and strengthening the relations with the Muslim world. During his tenure, Erbakan was highly critical about the close relations with the US, Israel and EC on the one hand and distant relations with the Muslim world, especially, with Iran and Libya. As a first step, after his one day visit to Turkish Republic of Northern Cyprus, Erbakan visited Iran as a first destination. In his meetings with Iranian counterparts, Erbakan strongly emphasized the Islamic solidarity and openly ignored some traditional sources of conflict frequently raised by Turkey concerning Iranian support for the PKK and Islamic fundamentalist groups in Turkey.²³⁴ However, Erbakan's efforts and enthusiasm to improve relations with Iran ran against bureaucratic, military and public objections and Erbakan was loudly criticized for visiting Iran. Similarly, in December 1996 during Iranian President Hashemi Rafsanjani's visit, Erbakan's desire to reach a defense cooperation agreement with Iran was preempted by the General Staff and Defense Minister from the True Path Party.²³⁵ In addition, during this visit, Iran's request for visiting the Turkish Aviation Industry (TAI) factory and offer for cooperation in defense industry were refused by the military authorities.²³⁶ In other words, although the WP took every opportunity to normalize relations with Iran and displayed much

²³³ Akdevelioğlu and Kürkcüoğlu, *loc.cit.*, pp. 581-583.

²³⁴ Kemal Kirişçi, "US-Turkish Relations: New Uncertainties in a Renewed Partnership," in Barry Rubin and Kemal Kirişçi, (Eds.), *Turkey in World Politics: An Emerging Multiregional Power*, Colorado & London, Lynne Rienner Publishers, 2001, p. 40.

²³⁵ Kirişçi, "Post Cold-War Turkish Security and the Middle East".

²³⁶ Gencer Özcan, "The Military Making of Foreign Policy in Turkey," in Barry Rubin and Kemal Kirişçi, (Eds.), *Turkey in World Politics: An Emerging Multiregional Power*, Colorado & London, Lynne Rienner Publishers, 2001, p. 23.

enthusiasm for promoting bilateral relations, its efforts were strictly contained by the military establishment and Ministry of Foreign Affairs to a degree.²³⁷

In this process, an important crisis erupted following the incident of “Night of Jerusalem” organized in Sincan. In that night, as an honorary guest, Iranian ambassador harshly critical about Turkey and said “youngsters will deliver punishment of God to those who every day sign agreements with America and Israel”. As a response, tanks and troops were sent to Sincan next day. Moreover, this incident induced a diplomatic crisis that resulted in recalling of ambassadors reciprocally and paved the way for the adoption of the February 28 Decisions that subsequently led to the toppling of WP-TPP coalition. Taken together, February 28 Decision amounted to severe limits on the WP’s power and it deliberately humiliated the WP by criticizing Iran for its efforts to “destabilize Turkey’s regime”.²³⁸ In February 1997, just after the Sincan events deputy Chief of the General staff gave a speech in Washington and calling Iran a “registered terrorist state and accusing it of exporting “Islamic revolution to Turkey”, “supporting the PKK” and “manufacturing weapons of mass destruction”.²³⁹ This speech further undermined the bilateral relations between Turkey and Iran.

3.2.6. Efforts of Cooperation

During the term of Erbakan, in conjunction with his new foreign policy priorities, in order to improve cooperation among Muslim countries, he initiated the process of creation the D-8 (Developing-8) organization for economic cooperation. The idea of cooperation among major Muslim developing countries was verbalized by Erbakan, during a seminar on “Cooperation in Development” which was held in Istanbul in October 1996 and actually, this conference was the first step towards the establishment of D-8. After a series of preparatory meetings, D-8 was set up officially and began its activities with the Istanbul Declaration issued at the end of

²³⁷ *Ibid.*, p. 23.

²³⁸ *Ibid.*, p. 19-23.

²³⁹ *Ibid.*, p. 22.

the summit of Heads of State and Government held in Istanbul in June 1997. Turkey, Iran, Pakistan, Bangladesh, Indonesia, Malaysia, Egypt and Nigeria came together under the umbrella of D-8 with the objectives of improving member states' position in the global economy, creating and diversifying new opportunities in trade relations, enhancing participation in decision-making at international level and improving the standards of living. These efforts of Erbakan and the establishment of D-8 called as "economic jihad" or Islamic alternative of the G-8. Despite these exaggerated epithets, Erbakan's ideas and expectations from D-8 widely criticized in the domestic politics. His initiative criticized for being unrealistic and wishful thinking.²⁴⁰ In fact, as a result of the internal political and economic problems of the members, D-8 failed to satisfy expectations, thus criticisms proved to be true during the period.

Probably the most important and long-lasting development of the Erbakan era concerning the economic relations between Turkey and Iran were the negotiations and subsequent signing of agreements on the supply of natural gas and the construction of a pipeline between Turkey and Iran. In this framework, Erbakan concluded a \$23 billion natural gas supply contract and gas pipeline construction scheme with Iran, which making Iran Turkey's second largest supplier after Russia, as well as a pledge to increase bilateral merchandise trade to an annual value of \$2.6 billion in July 1996²⁴¹ despite harsh criticisms and threats of embargo articulated by the US. Because, these steps perceived by the US as direct challenge to the 1995 executive orders of the President Clinton prohibiting American companies and their foreign subsidiaries from conducting business with Iran or Libya, as well as the 1996 Iran-Libya Sanctions Act, which punishes non-US companies investing more than \$20 million in either country's gas and oil sectors. But to sustain its economic growth Ankara has little choice, because the traditionally biggest supplier of Turkey, Russia, has been unreliable.²⁴² Although many believed that the deal was mainly driven by

²⁴⁰ Siyaset Dünyasında M-8 Tartışılıyor, *Milliyet*, 23.10.1996, <http://gazetearsivi.milliyet.com.tr>, internet access: 06.11.2011.

²⁴¹ Daphne McCurdy, "Turkish-Iranian Relations: When Opposites Attract," *Turkish Policy Quarterly*, Vol. 7, No. 2 (Summer 2008), p. 89.

²⁴² Brents Susley, "Turkey's Energy Politics," in Barry Rubin and Kemal Kirişçi, (Eds.), *Turkey in World Politics: An Emerging Multiregional Power*, Colorado & London, Lynne Rienner Publishers, 2001, p. 220.

Erbakan's ideological vision of strengthening relations with the Muslim world, negotiations had been proceeding for some years, and the previous Tansu Çiller government had signed an outline agreement in 1995. During the 1990s, in addition to the loss of Iraq as an important supplier, the instability and insecurity in the Middle East obstructed the access to energy resources and raised prices.²⁴³ Because of the financial problems and the US opposition, this Iranian-Turkish pipeline began operation in 2001 after many delays. As a developing country Turkey's energy crunch was growing during time, and in order to increase production and exports, Turkey had to sustainably supply energy in favorable prices. Probably, along with the positive perceptions of Erbakan and some parts of the ruling elite concerning Iran, these considerations mainly drove Turkey to such an important and transforming project with Iran. Moreover, to supplement this arrangement, in December 1997 Turkey completed an agreement with Iran and Turkmenistan to connect with the Turkish-Iranian pipeline.²⁴⁴ In sum, these two steps, reflected the pragmatist aspect of the Turkish foreign policy, had long lasting impacts not only on economic but also on political relations between Turkey and Iran. As mentioned before, these agreements and the economic cooperation efforts of some circles could not prevent the emergence of tensions and even as the relations became conflictual, Iran began to play its strong trump card of supplying natural gas against Turkey to gain leverage.

Nevertheless, starting especially from the late 1990s, initiatives of dialogue with Iran emerged slowly. This normalization process mainly stemmed from the administration of İsmail Cem and Mohammed Khatami. Although the political relations to most of the neighboring countries remained tense until the late 1990s, this trend slowly changed under the new Foreign Minister İsmail Cem, who tried to break away from some of the previous orthodoxies.²⁴⁵ For instance, during his visit to Egypt in March 1998, he expressed his determination to improve relations with the

²⁴³ Kemal Kirişçi, "Post Cold-War Turkish Security and the Middle East".

²⁴⁴ Susley, *op. cit.*, p. 220.

²⁴⁵ Ekrem Eddy Güzeldere, "Turkish Foreign Policy: From 'Surrounded by Enemies' to 'Zero Problems'," *C·A·P Policy Analysis*, No. 1 (2009), p. 14.

Middle Eastern Muslim countries and Turkey's desire to take a more active role in regional politics, raised Tehran's expectations.²⁴⁶ The idea of expanding economic relations was seen as a mechanism to build confidence and dialogue in Turkey's relations with the Middle Eastern countries, including Iran.²⁴⁷

In the same year, with the election of reformist Mohammad Khatami as the new President of Iran and the rising influence of the reformists in Iranian foreign policy also raised Turkey's expectations from Iran. As a result of this optimism, Turkey's perceived threats from Iran diminished and relations between the two countries improved significantly, because with Khatami's government, Iran's quest to export the Revolution and the support for the radical Islamist groups and PKK terrorism had gradually declined.²⁴⁸ The ascendancy of the pragmatist/reformist wing in Iranian politics and consequent relaxation of Iran contented Turkish leaders who expected from Iran to adopt moderate and constructive policies. As always be, in order to support the pragmatic-reformist wing, Turkey generally adopted a moderate and accommodative approach towards Iran.²⁴⁹

In sum, the 1990s witnessed a corrosion process of bilateral relations as result of the stubborn cycles of tension-détente-tension. During the period, "high politics" occupied the top of the agendas of Turkey and Iran, rather than "low politics". Thus economic and commercial interests were overlooked to some degree. Under these conditions, the strengthening and deepening of commercial relations could not be achieved and remained limited. Nevertheless, this did not mean that no effort was made with a view to develop commercial relations. But still, under such an environment that the mutual hostility became evident, it was not so easy to advocate the development of economic relations as if all the hitches had not been experienced. In addition the lack of clear and constant political will towards improving economic relations, negatively affected the progress of trade. Nonetheless, by the late 1990s the

²⁴⁶ Aras, "Turkish-Israeli-Iranian Relations in the 1990s and Their Impact on the Middle East," p. 155.

²⁴⁷ Kemal Kirişçi, The Future of Turkish Foreign Policy Toward the Middle East, in Barry Rubin and Kemal Kirişçi, (Eds.), *Turkey in World Politics: An Emerging Multiregional Power*, Colorado & London, Lynne Rienner Publishers, 2001, p. 106.

²⁴⁸ Karacasulu and Aşkar Karakır, *op. cit.*, p. 112.

²⁴⁹ Sinkaya, "Turkey-Iran Relations in the 1990s and the Role of Ideology," p. 7.

degree of tension declined even a little by the effects of İsmail Cem and Mohammed Khatami and economy and trade tried to be given prominence. Thusly, as of 2000 cursors slowly shifted again to the direction of economy and trade. This shift signalled that the political and especially economic relations will show a different trend from the 1990s in the new decade.

3.3. Turkey's Economic Relations with Iran in the 1990s

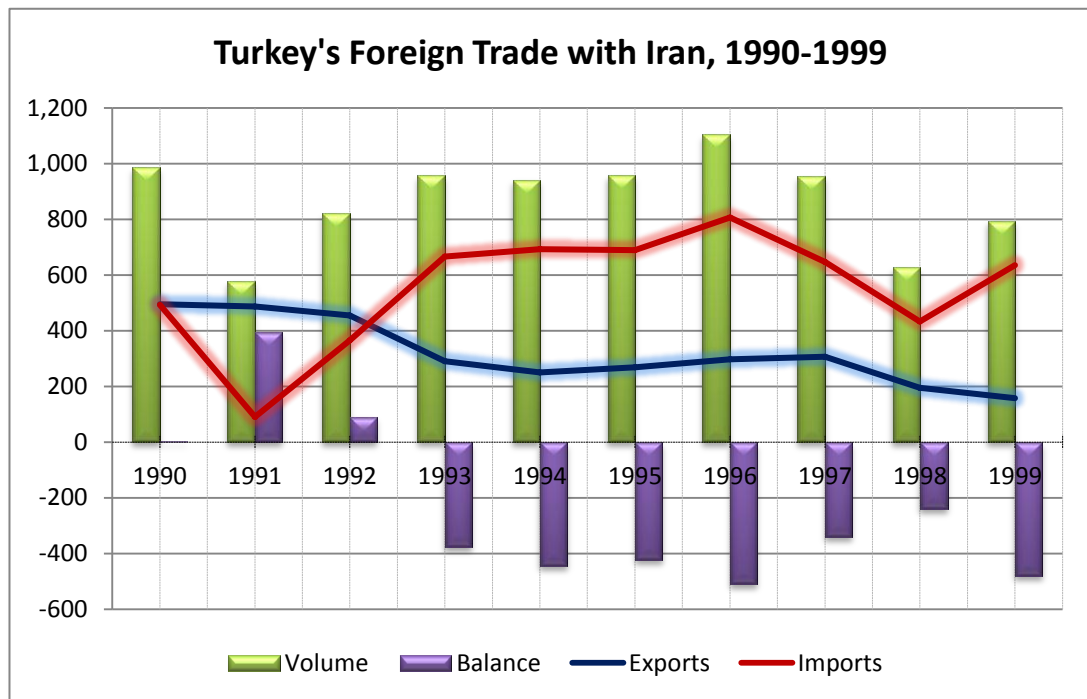
As a result of the abovementioned political problems and disagreements, during the 1990s, bilateral trade relations between Turkey and Iran and the performances shown by the two were far from impressive. Compared with the 1980s, Turkey's average exports to Iran decreased by 48%, average imports from Iran declined by 33% and hence average volume of trade shrunk by 39% in the 1990s. Furthermore, when the lowest levels of 1990s compared with the highest levels of 1980s, the deterioration in bilateral trade relations became more evident. Exports to Iran decreased by 85% from its \$1.1 billion peak in 1983 to \$158 million in 1999; while the imports from Iran decreased by 94% from its highest \$1.6 billion in 1984 to \$91 million in 1991. The volume of bilateral trade also dropped by 75% from its highest \$2.3 billion in 1985 to \$577 million in 1991.

Table 4 Turkey's Foreign Trade with Iran, 1990-1999

Turkey's Foreign Trade with Iran, 1990-1999									
Years	Exports		Imports		Volume		Balance		Proportion of Imports covered by Exports (%)
	Value	Change (%)	Value	Change (%)	Value	Change (%)	Value	Change (%)	
1990	495.5	-11.7	492.4	110.9	987.9	24.3	3.1	-99.1	100.6
1991	486.9	-1.7	90.5	-81.6	577.4	-41.5	396.4	12,758.3	537.8
1992	455.2	-6.5	364.9	303.0	820.1	42.0	90.3	-77.2	124.8
1993	290.1	-36.3	667.0	82.8	957.2	16.7	-376.9	-517.2	43.5
1994	249.8	-13.9	692.4	3.8	942.2	-1.6	-442.6	17.4	36.1
1995	268.4	7.5	689.5	-0.4	957.9	1.7	-421.0	-4.9	38.9
1996	297.5	10.8	806.3	16.9	1,103.9	15.2	-508.8	20.8	36.9
1997	307.0	3.2	646.4	-19.8	953.4	-13.6	-339.4	-33.3	47.5
1998	194.7	-36.6	433.0	-33.0	627.7	-34.2	-238.3	-29.8	45.0
1999	157.8	-18.9	635.9	46.9	793.7	26.4	-478.1	100.6	24.8
1990-99		-68.1		29.1		-19.7		-15,610.2	

Source: Republic of Turkey Ministry of Economy, 1990-1999, Million US \$, Annual Change (%).

As can be seen from the table above, Turkey's exports to Iran substantially decreased during the 1990s. Exports to Iran which were around \$495 million in 1990, dropped by 68% to \$158 million in 1999 and most severe drops were experienced in 1993 and 1998. On the other hand, imports fluctuated during the period and increased by 29% from \$492 million in 1990 to \$636 million in 1999. The most severe ups and downs occurred in 1991 and 1992. First imports dropped sharply by 82% and then jumped 303% in 1992. In conjunction with imports and exports, the volume foreign trade with Iran also fluctuated during ten years and declined by 20% from \$988 million in 1990 to \$794 million in 1999. The lowest and highest levels were recorded in 1991 (\$577 million) and 1996 (\$1.1 billion) respectively. As usual, during most of the 1990s, balance of trade developed to the detriment of Turkey. In addition, the proportion of imports covered by exports shrunk substantially from 538% in 1991 to 25% in 1999.



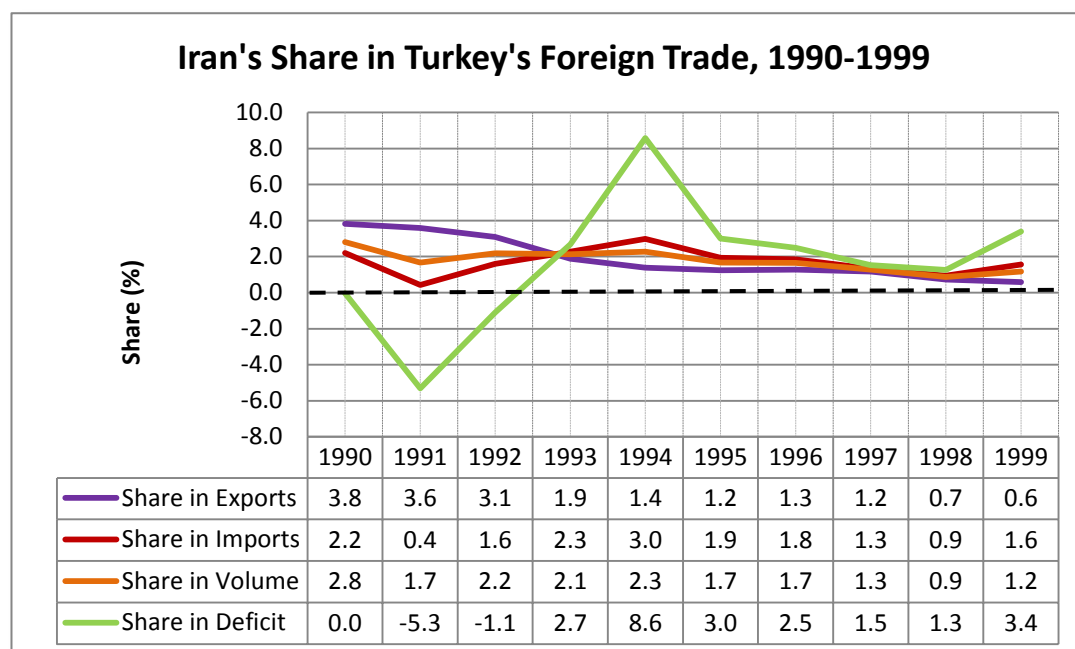
Source: Republic of Turkey Ministry of Economy, 1990-1999, Million US \$.

Figure 9 Turkey's Foreign Trade with Iran, 1990-1999

Actually, during the 1990s, Turkey's foreign trade with Iran differed from the overall foreign trade performance of Turkey. Moreover, when the rise in Turkey's total exports and imports in the 1990s bear in mind, the relative fall in exports to and imports from Iran became more evident. As a result, Iran's share in Turkey's total exports, and imports also fell substantially during the 1990s compared with the 1980s and even dropped below levels of the 1970s.

As can be seen from the graph above, during the period, Iran's share in Turkey's exports decreased from 3.8% in 1990 to 0.6% in 1999. In ten years, Iran's share sharply (ten times) fell from 19% in 1983 to 1.9% in 1993. Iran's average share in exports fell from 8.6% in 1980s to 1.9% in 1990s. A similar downtrend also prevailed on the imports. Iran's share in total imports dropped from 2.2% in 1990 to 1.6% in 1999. Compared with the 16% share in 1984, this 1.6% share in 1996, pointed another sharp fall in bilateral trade. During the period, Iran's average share in imports declined from 7.8% in 1980s to 1.7% in 1990s. As a result, Iran's average

share in Turkey's total volume of trade decreased from 8.2% in the 1980s to 1.8% in the 1990s while its average share in trade deficit fell from 5.1% to 1.6%.



Source: Republic of Turkey Ministry of Economy, 1990-1999, Share (%).

Figure 10 Iran's Share in Turkey's Foreign Trade, 1990-1999

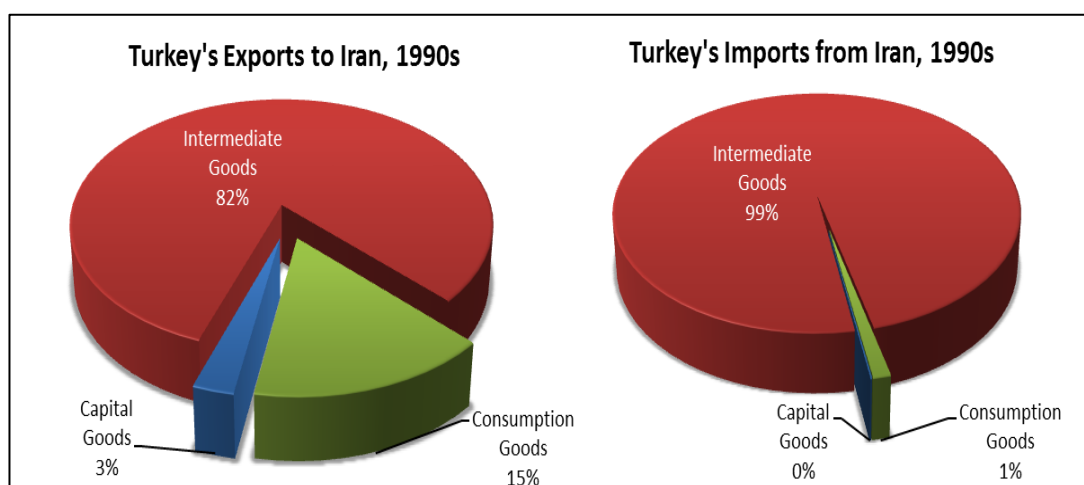
Moreover, it can be useful to have a look at the rank of Iran among other export and import markets of Turkey to understand the fall of Iran. In 1983, Iran was both the number one export and import partner of Turkey. However, since then its rank among other import and export markets of Turkey also degraded in parallel with the fall of its share in Turkey's foreign trade. During most part of the 1990s, Iran did not even enter for the top 10 and its rank among export and supply markets drew back to 34th and 17th in 1999 respectively. During the period traditional Western import and export markets namely Germany, the US and Italy replaced Iran. Germany toppled Iran from the throne and became the number one export and import partner of Turkey in the 1990s.

Furthermore, in parallel to its place in total exports, during the period, İstanbul was the biggest exporter city of Turkey to Iran. Throughout the 1990s, nearly 60% of the total exports were made in İstanbul and it was followed by İzmir, Kocaeli, and Ankara. These were the traditional suppliers of the Iran during the

period. However, there were also a number of emerging cities such as Gaziantep and Adana, where the Anatolian tigers arise from. On the other hand, in 1996 and 1997 as a result of the increased border trade, Ağrı and Iğdır, neighboring cities of Iran, took part among the first five exporter cities to Iran. On the imports side, as being the heart of the petrochemical industries and one of the biggest industrial cities, Kocaeli was the biggest importer of the Iranian products. During the 1990s, approximately 75% of the total imports from Iran were made by Kocaeli and it was followed by İstanbul, İzmir and Ankara. As in the case of exports these four cities were also the traditional markets of Iran. In addition to these cities, Kayseri, Sakarya and Bursa were the emerging cities of the 1990s in imports from Iran. Besides these cities, as a bordering city, Hakkari also increased its imports from Iran and it was followed by Ağrı and Van. In 1996, the scope of the border trade was expanded by the decree of the council of ministers and border trade was allowed in 13 cities in general and border trade with Iran was allowed in Ağrı, Van, Hakkari, Iğdır and Kars in particular.²⁵⁰ As a result the shares of these cities in exports and imports increased. However, in 1998 some changes were made in the border trade system in order to prevent borderless trade. In this context, the scope was narrowed and the Undersecretariat for Foreign Trade was given mandate instead of governorates and furthermore, cross border trade of agricultural products was restricted in 1999. As a result, in the last years of the 1990s, border trade with Iran decreased.

When we consider the structure of the foreign trade with Iran, according to SNA (System of National Accounts) classification, despite relative decrease in its share, intermediate goods still constituted the largest part of Turkey's exports to Iran and consumption and capital goods followed it. While intermediate good showed a downtrend, consumption and capital goods showed an uptrend in exports. On the imports side, the structure of imports from Iran hardly changed. The share of intermediate goods was over 97% throughout the period as it used to be. The average shares of capital, intermediate and consumption goods in exports to and imports from Iran during the 1990s has depicted on the graphic below.

²⁵⁰ Öztürk, *op. cit.*, pp. 110-112.



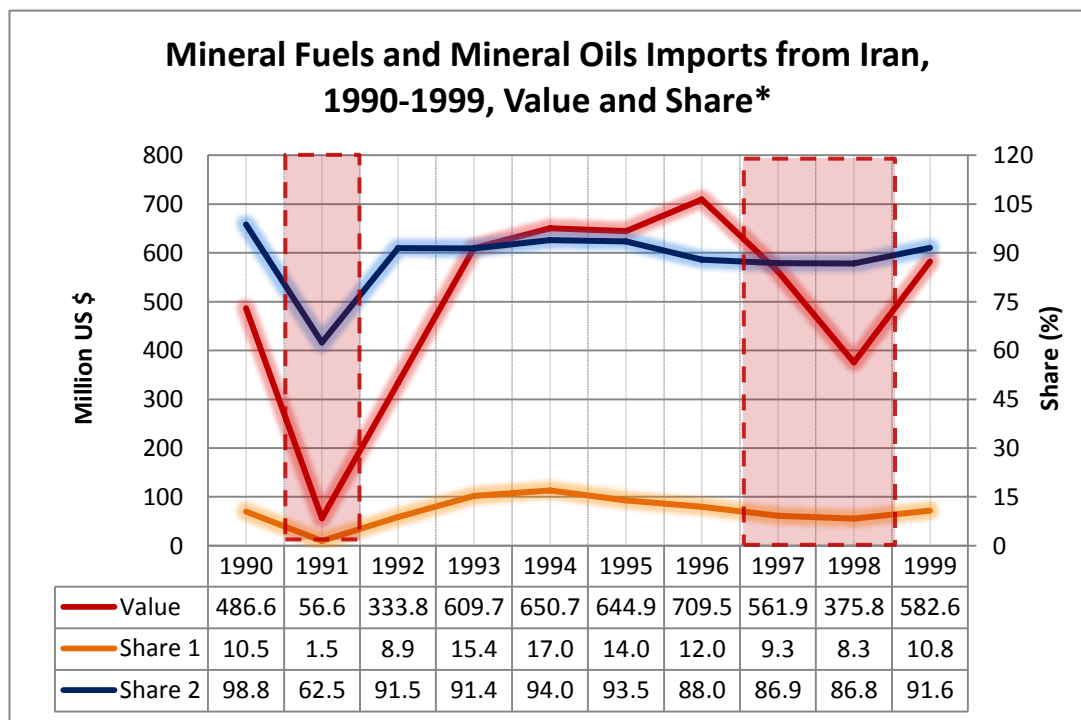
Source: Republic of Turkey Ministry of Economy, Average Share (%), SNA (System of National Accounts).

Figure 11 Structure of Turkey's Foreign Trade with Iran in the 1990s

During the 1990s, not only quantity but also diversity of export goods declined substantially. Although some of the major export items in the 1980s preserved their positions, some of them like live animals, meat, milk and dairy products lost their market shares. During the period, iron and steel, textile fabrics, fibres, cotton yarn, plastics, paper and paperboard, organic chemicals, rubber, glass and glassware, vehicles and their parts, animal or vegetable fats and oils were the leading export items. On the other hand, the structure of Turkey's imports from Iran changed a little. This change was not about quantity but diversity. In the same period, although the position of mineral fuels and oils as the most imported item from Iran did not change, it was not the only item any more. During the period the average share of mineral oils and fuels in Turkey's total imports from Iran was decreased to 89%. Besides mineral fuels and oils, copper and articles thereof, aluminum and articles thereof, ores, slag and ash, raw hides and skins, edible fruit and nuts, cotton and staple fibres were imported from Iran.

Furthermore, in the 1990s according to international standard industrial classification of all economic activities (ISIC Rev.3), the share of agricultural and forestry products in Turkey's total exports to Iran fluctuated between 0.1% and 6% and its share in 1990 dropped from 3% to 1% in 1999. Besides, the share of manufacturing products fluctuated between 93% and 100% and its share reached

98% in 1999. On the other hand, the share of mining and quarrying products, which was not exported in the 1980s, increased from 0.1% to 1.3%. To sum up, during the 1990s, the average share of manufacturing and mining products in Turkey's total exports to Iran increased to 97.8% and 0.3% respectively, while the share of agricultural and forestry products decreased to 1.9%. On the imports side, data indicated the diversification of imports. Throughout the period, according to ISIC (Rev.3), the share of mining and quarrying products that covered the crude petroleum and natural gas, in Turkey's total imports from Iran somewhat changed. The average share of mining and quarrying products dropped from 97.7% to 87.9% while the share of manufacturing and products jumped from 2.3% to 10.7% in ten years. And agricultural and forestry products started to import from Iran and its share reached to 0.7% on an average basis.



Source: Republic of Turkey Ministry of Economy, Value: Million US \$, Share: Percentage (%).

*Share1: Iran's share in Turkey's total imports of mineral fuels and mineral oils.

*Share2: Share of mineral fuels and mineral oils in Turkey's total imports from Iran.

**Figure 12 Mineral Fuels and Mineral Oils Imports from Iran, 1990-1999,
Value and Share***

As can be seen from the graph above, although the share of mineral fuels and oils decreased in Turkey's total imports from Iran during the 1990s, it still constituted the largest part of the imports. During the period, ups and downs were observed both in terms of value and share. However, Iran was able to preserve its position as one of the top five energy suppliers of Turkey except 1991 despite this fluctuation. It is important to emphasize that in 1991 both the value (88%) of crude oil and the share of Iran (9 points) decreased substantially and came to a standstill. However, this decline did not stem from the political crisis between the two. Despite the negative effects of political tensions in bilateral trade, the main reason behind this sharp fall in 1991 was the rise of crude oil imports from Saudi Arabia in the form of grant in order to make the losses of Turkey from the Gulf War. Furthermore, Turkey's oil imports from Iran also decreased in 1997 and 1998. The reason behind the decline of 1997 could be rather political, but it was because of the 1998 economic crisis and consequent slowdown in industrial production. In this year Turkey's total oil imports decreased by 36%, while the imports from Iran dropped by 33% in line with the general trend. Even so, during the period, imports of mineral fuels and oils from Iran increased by %20 from \$487 million to \$583 million, but Iran's share in total mineral fuels and oils imports did not change and were 11% in both 1990 and 1999. However its share swung between 1.5% and 17% in the 1990s. The average share of Iran dropped from 23% in the 1980s to %11 in the 1990s. During the 1990s, Saudi Arabia replaced Iran and became the biggest oil supplier of Turkey; Russian Federation advanced its position considerably against Iran while Iraq was ousted by the UN sanctions.

In conclusion, the overall outlook of the bilateral trade between Iran and Turkey during the 1990s indicated that political tensions negatively and profoundly affected the bilateral trade and paved the way for a substantial and mutual decline in both exports and imports by means of value, volume, diversity and share. Notwithstanding, the economic interdependency between these neighbors, notably the continued reliance of Turkey on Iranian crude oil, the deep-rooted commercial attachments and lobbying activities of traditional and emerging business circles in

Turkey prevented the bilateral trade from a further decline, ensured the continuity of minimal pragmatism in commercial relations which kept the foreign trade alive.

In this context, bilateral trade outlook of Turkey and Iran was in line with the general trend of the 1990s in such a way that the process of becoming a “trading state,” which was originally started during the tenure of Özal in the 1980s, was interrupted during the most part of the 1990s. In other words, Turkey’s foreign policy choices between the “military-political” and the “trading state” were constrained by the escalation of security concerns and threat perceptions. So to say, the 1990s witnessed the retreat of “trading state” and the rise of “military-political state” in relations with Iran. Thus, the emergence of the “trading state” could not be sustained in the 1990s and the process was interrupted. During this era of interruption, contrary to the pragmatism and economic considerations of the 1980s, ideology with military-political and territorial considerations dominated the 1990s. Özal’s thinking and priorities by the early 1990s succumbed to the traditional approach.²⁵¹ As might be expected, it would have been rather difficult to talk about the interests of the business class while the alarm bells were tolling for the national security. This interruption adversely affected Turkey’s relations with Iran and *vice versa*, thus further deteriorated the situation. Nevertheless this process again started to accelerate in the late 1990s as a result of the degradation of the levels of national security alert as a result of the relaxation of tensions in the issues of PKK, Syria, Greece, Iraq and Iran as well. Thus, by the late 1990s but especially by the 2000s the balance once more began to change, as policies much more closely associated with a trading state began to make a comeback and started to transform traditional foreign policy determinants and makers as well.²⁵²

²⁵¹ Kirişçi, “The Transformation of Turkish Foreign Policy: The Rise of the Trading State,” p. 45.

²⁵² Kirişçi, *loc. cit.*, p. 45.

CHAPTER 4

TURKEY'S POLITICAL ECONOMY AND TURKISH – IRANIAN RELATIONS IN THE 2000s

4.1. General Features of the Turkish Economy in the 2000s

After going through a series of short-term cycles of instability-crisis-(unsustained) growth-instability throughout the 1990s, Turkey entered the new millennium with severe economic and political crisis in November 2000 with a final blow of the financial bubble in February 2001.²⁵³ After unsuccessful reforms and deteriorated macroeconomic performance of the 1990s, Turkey entered the 2000s under an austerity program which was put into practice in December 1999. The program was sponsored and supervised by the IMF and aimed to decrease the inflation rate to a single digit by the end of 2002 and reducing the real interest rates. Nonetheless, one year after introducing the program, the country experienced a severe financial crisis in November 2000. More than \$6 billion of short-term capital fled the country, creating a severe liquidity shortage in the domestic commodity and asset markets and sky-rocketing interest rates.²⁵⁴ As a result, an additional support was provided by the IMF whereas the program was revised and continued to be implemented.

Since there were still serious problems in the fundamentals of the economy, the stability did not last long and subsequent to a political dispute between the President Ahmet Necdet Sezer and Prime Minister Bülent Ecevit, the already fragile market confidence eroded totally and a huge amount of capital fled the country again. Consequently, Turkey was hit by a stronger financial crisis for a second time in February 2001. Right after the crisis the Central Bank declared that it was going to

²⁵³ Ümit Cizre and Erinc Yeldan, "The Turkish Encounter with Neo-Liberalism: Economics and Politics in the 2000/2001 Crises", *Review of International Political Economy*, Vol. 12, No.3 (August 2005), p. 388.

²⁵⁴ Yeldan, "The IMF-Directed Disinflation Programme In Turkey: A Program For Stabilization and Austerity Or A Recipe For Impoverishment and Financial Chaos?," p. 2.

implement a floating exchange rate regime from that date onwards. With the breakdown of the program in February 2001, the newly appointed Minister of Economy Kemal Derviş, at the time serving as a vice president at the World Bank, initiated a new stabilization program on May 2001. This program relied mainly on three pillars: (1) fiscal austerity (2) contractionary monetary policy (through an independent Central Bank) that exclusively aims at price stability (via eventually inflation targeting); and (3) structural reforms consisting of many of the customary IMF demands: privatization, large scale layoffs in public enterprises, and abolition of any form of subsidies.²⁵⁵

Devastating socio-economic impacts of the crisis shook the whole country profoundly. In this respect, an important characteristic of this crisis was that contrary to the previous crises, where a disproportionate share of the burden had fallen on wage earners and other low income groups, almost all sections of society were negatively affected by the crisis this time. In the aftermath of the 2001 crisis, all of the macroeconomic indicators deteriorated rapidly. In this context, the economic growth rate fell substantially; the decline in the industrial production was accompanied by widespread bankruptcies particularly in the realm of small and medium scale firms; accordingly a great deal of the Anatolian Tigers also collapsed. The banking sector felt the negative impact of the crisis in a drastic manner as well. Even large conglomerates experienced a reduction in their profit margins. As a result not only unskilled, but also skilled workforce fell out of work. Consequently, unemployment rate increased swiftly.

The political impact of the 2001 crisis was also profound in the sense that domestic political actors and notably the parties that constituted the coalition government emerged as the main targets for widespread criticism.²⁵⁶ Ultimately, the members of the coalition government Democratic Left Party (DSP) from the center-

²⁵⁵ Teoman Pamukçu and Erineç Yeldan, "Country Profile: Turkey Macroeconomic Policy and Recent Economic Performance," p. 3, http://www.bilkent.edu.tr/~yeldane/FEMISE_Macro2005.pdf, internet access: 21. 11.2011.

²⁵⁶ Ziya Öniş, "Beyond The 2001 Financial Crisis: The Political Economy of The New Phase of Neo-Liberal Restructuring in Turkey," p. 8, http://cesran.org/Dosyalar/MAKALELER/ZIYA_ONIS_Beyond_the_2001_financial_crisis.pdf, internet access: 20. 11.2011.

left, Motherland Party (ANAP) from the center-right and the Nationalist Action Party (MHP) from the far-right wings were condemned and marginalized by the time of the early general elections of November 2002. As a consequence of the economic crisis, all the established political parties of the left and the right represented in the parliament were wiped out and the Justice and the Development Party (AKP), a new center-right political party with Islamic roots, came to power with absolute majority in the parliament.²⁵⁷ After a substantial time-lag, following the electoral victory of the AKP, the optimism that characterized the early Özal era revived to a large extent and indicated the outset of a new era of confidence about the future of the Turkish economy.²⁵⁸

Despite its otherwise pre-election rhetoric, the AKP embarked on and vigorously implemented a new and intensified adjustment program with the IMF staff.²⁵⁹ In this context, shortly after it has taken office, the AKP abandoned the discourse manipulating anti-IMF and anti-liberal reactions in the country and showed no hesitation in fully adopting neo-liberal policies.²⁶⁰ The distinguishing feature of the AKP government in this respect was that it has undertaken the mission of executing the neo-liberal project under the discourse of a “strong government” without confronting any strong popular opposition and has acted faster and more boldly than any preceding government in implementing the neoliberal agenda.²⁶¹

In this regard, the post-2001 period represents a clear rupture from the unstable macroeconomic environment of the 1990s in terms of relatively higher growth rates, lower inflation, fiscal discipline, attracting FDI and realizing privatization.²⁶² However, this success has still restrained with significant fundamental deficiencies. Although the post-2001 growth had indeed been high, it

²⁵⁷ *Ibid.*, p. 8.

²⁵⁸ Öniş, “Turgut Özal and His Economic Legacy: Turkish Neo-Liberalism in Critical Perspective,” p. 129.

²⁵⁹ Pamukcu and Yeldan, *op. cit.*, p. 3.

²⁶⁰ Erinç Yeldan, “Patterns of Adjustment under the Age of Finance: The Case of Turkey as a Peripheral Agent of Neoliberal Globalization,” *PERI*, Working Paper Series No.126 (February 2007), p. 3.

²⁶¹ *Ibid.*, p. 4.

²⁶² Öniş and Bayram, *op. cit.*, p. 10.

was not free from problems. In fact, recent upswing in economic activity was mostly fueled by capital inflows, hence was speculative-led; and it was accompanied by high rates of unemployment; and fit in with the jobless-growth type.²⁶³ Until 2007, higher and more stable growth was recorded in Turkey in parallel with the general tendency in the world economy, especially in developing countries. However, after 2007 economic growth started to decline noticeably. Furthermore, despite the positive achievements on the inflation, which has been brought under control and dropped significantly to single-digit levels by 2004 after decades, interest rates remained slow to adjust, and are still highest among the developing world. Furthermore, high interest rates generated relatively large capital inflows. Thus, the over-abundance of foreign exchange led significant pressures for the Turkish Lira to appreciate and finally paved the way for ever-expanding deficits on the foreign trade and current account balances.²⁶⁴ In the end, increasing current account deficits and appreciating currency has made growth unsustainable after 2007.

Despite appreciated Turkish Lira, in parallel with economic growth and initiation of export mobilization efforts, exports increased substantially in the 2000s. However, as a result of the dependency of production and exports to imports, the import bill outpaced exports, thus current account deficit widened during the same period. Therefore, as the integration process of Turkey's into world economy accelerated, the current account deficit problem worsened and increasingly constituted a serious stalemate in the 2000s.

However, in May 2008 things have changed for Turkish foreign trade by the reaching of global economic crisis to Turkey. Although otherwise said by the Prime Minister, given the degree of Turkey's integration into the global economy and the severity of the global recession, Turkish economy suffered a serious blow from the global crisis of 2008-09. In this respect, foreign trade flows have been an important channel through which the recent global crisis profoundly affected the Turkish

²⁶³ Pamukcu and Yeldan, *op. cit.*, p. 4.

²⁶⁴ Yeldan, *loc. cit.*, pp. 10-12.

economy.²⁶⁵ As a result of the crisis, both exports and imports dropped from their highest in 2008 by 22.6% and 30.2% respectively. Thus, volume of foreign trade declined by 27%, from \$334 billion in 2008 to \$243 billion in 2009. Since the decrease of imports exceeded exports' and falling import prices, especially in oil and natural gas, current account deficit narrowed by %45, in spite of the sharp declines in exports. Naturally, these sharp contractions in both exports and imports have had severe impacts on the real economy and economic growth. By the end of the 2010, despite the recovery, both exports and imports were still under the levels of 2008. The sharp decline in the value of exports resulted from not only falling volumes but also falling prices after the global economic crisis. The main factor behind the export contraction was the sharp contraction in EU demand, the largest export partner of Turkey. On the other hand, in a move to counterbalance the negative effects of declining EU demand, the share of Middle East and North Africa in total exports increased significantly. In this context, government efforts to boost exports, such as export financing and especially ever larger trade delegations under the leadership of the State Minister responsible for Foreign Trade, the Prime Minister or the President, prove to be effective. In fact, Turkey's new-style foreign (trade) relations and trade destinations have helped to alleviate the negative impacts of the global crisis at a certain level.

Throughout the 2000s, except the years of crisis, Turkey's foreign trade performance was relatively good when compared with the world trade performance. As can be seen from the table below, except 2000 and 2010, the growth rate of Turkey's exports exceeded the growth rate of world exports. On the other hand, Turkey's exports shrunk more than world exports in 2009 as a result of global financial crisis. Although Turkey's share in world total exports increased slightly from 0.4% in 2000 to 0.7% in 2010, it remained minimal. On the imports front, the growth rate of Turkey's imports surpassed the growth rate of world imports throughout the period. Nevertheless, in the years of crisis, Turkey's imports shrunk more than the world imports. Turkey's share in the world total imports augmented

²⁶⁵ Ercan Uygur, *The Global Crisis and the Turkish Economy*, Penang, Third World Network, 2010, p. 14.

from 0.8% in 2000 to 1.2% in 2010 and hence exceeded its share in world exports during the whole period. Thus, Turkey became the 33rd biggest exporter and 21st biggest importer of the world by the end of 2010.

Table 5 Turkey's Place in World Trade, 2000-2010

Turkey's Place in World Trade, 2000-2010											
	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
World Exports	6,456	6,191	6,492	7,586	9,218	10,489	12,113	14,003	16,120	12,516	15,237
Turkey's Exports	27.8	31.3	36.1	47.3	63.2	73.5	85.5	107.3	132.0	102.1	114.0
Annual Change of World Exports, %	13.0	-4.1	4.9	16.9	21.5	13.8	15.5	15.6	15.1	-22.4	21.7
Annual Change of Turkey's Exports, %	4.5	12.8	15.1	31.0	33.7	16.3	16.4	25.4	23.1	-22.6	11.6
Turkey's Share in World Exports, %	0.4	0.5	0.6	0.6	0.7	0.7	0.7	0.8	0.8	0.8	0.7
World Imports	6,724	6,483	6,742	7,867	9,568	10,855	12,437	14,304	16,524	12,720	15,402
Turkey's Imports	54.5	41.4	51.6	69.3	97.5	116.8	139.6	170.1	202.0	140.9	185.5
Annual Change of World Imports, %	13.6	-3.6	4.0	16.7	21.6	13.5	14.6	15.0	15.5	-23.0	21.1
Annual Change of Turkey's Imports, %	34.0	-24.0	24.5	34.5	40.7	19.7	19.5	21.8	18.8	-30.2	31.7
Turkey's Share in World Imports, %	0.8	0.6	0.8	0.9	1.0	1.1	1.1	1.2	1.2	1.1	1.2

Source: WTO, 2000-2010, Billion US \$, Annual Change (%), Share (%).

As seen from the table below, during the 2000s, both exports and imports increased substantially and reached their highest, \$132 billion and \$202 billion respectively, in 2008. This upward trend in foreign trade was reversed by the global economic crisis. During the 2000-2010 period, despite the appreciation of Turkish Lira, exports quadrupled and jumped from \$27.8 billion in 2000 to \$113.9 billion in 2010. During the same period, imports followed a similar trend except the crises years of 2001 and 2009. As a result of appreciated Turkish Lira, and the import dependent structure of exports and production rate of increase in imports exceeded exports. In addition to the rapid economic growth process after the 2001 economic

crisis, the Chinese accession to the WTO in December 2001 fueled the Turkish imports. Together with the appreciation of Turkish Lira, the tightening competitiveness conditions have forced the exporters to “buy from Asia and sell to European markets”.²⁶⁶ On the other hand, growing industrial production and household consumption aggravated the energy need of Turkey. Rising energy prices until the global crisis galvanized the imports. Thus imports more than tripled and rose from \$54.5 billion in 2000 to \$185.5 billion in 2010.

Table 6 Turkey's Foreign Trade, 2000-2010

Turkey's Foreign Trade, 2000-2010									
Years	Exports		Imports		Volume		Balance		Proportion of Imports covered by Exports (%)
	Value	Change (%)	Value	Change (%)	Value	Change (%)	Value	Change (%)	
2000	27.8	4.5	54.5	34.0	82.3	22.0	-26.7	90.0	51.0
2001	31.3	12.8	41.4	-24.0	72.7	-12.0	-10.1	-62.0	75.7
2002	36.1	15.1	51.6	24.5	87.6	20.0	-15.5	54.0	69.9
2003	47.3	31.0	69.3	34.5	116.6	33.0	-22.1	43.0	68.1
2004	63.2	33.7	97.5	40.7	160.7	38.0	-34.4	56.0	64.8
2005	73.5	16.3	116.8	19.7	190.3	18.0	-43.3	26.0	62.9
2006	85.5	16.4	139.6	19.5	225.1	18.0	-54.0	25.0	61.3
2007	107.3	25.4	170.1	21.8	277.3	23.0	-62.8	16.0	63.1
2008	132.0	23.1	202.0	18.8	334.0	20.0	-69.9	11.0	65.4
2009	102.1	-22.6	140.9	-30.2	243.1	-27.0	-38.8	-45.0	72.5
2010	113.9	11.5	185.5	31.7	299.4	23.0	-71.7	85.0	61.4
2000-10		310.0		240.4		263.9		168.1	

Source: Republic of Turkey Ministry of Economy, 2000-2010, Billion US \$, Annual Change (%).

Between 2000 and 2010, foreign trade deficit increased by 168% from \$26.7 billion to \$71.7 billion, while volume of foreign trade increased by 264% from \$82.3 billion to \$299.4 billion. Despite this huge gap, exports financed on average 65% of

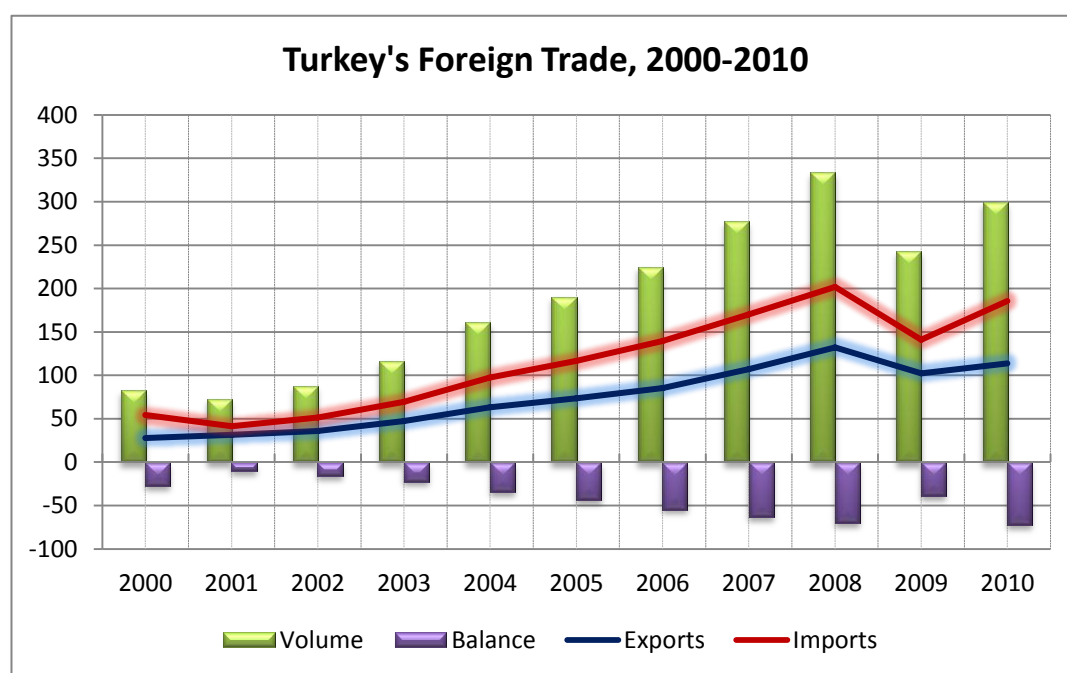
²⁶⁶ Ümit İzmen and Kamil Yılmaz, “Turkey’s Recent Trade and Foreign Direct Investment Performance,” *Tüsiad-Koç University Economic Research Forum*, Working Paper 0902, March 2009, p. 9, <https://www.econstor.eu/dspace/bitstream/10419/45435/1/599164409.pdf>, internet access: 21.11.2011

the imports during the 2000s and this ratio was 61% during the 1990s. In the first decade of the new millennium, average growth rates of exports, imports and volume of foreign trade were 15.2%, 17.4% and 16.0% respectively.

During the 2000s, despite preserving its number one position, the share of the EU in foreign trade decreased while the share of the “rest of the EU” increased. In other words, the 2000s has witnessed efforts of reducing the dependency on European markets and of increasing the diversity of both export and import markets. Actually, the crises of 2001 and 2008-09 and the consequent domestic and global demand contractions compelled Turkey to increase and diversify not only its exports but also its export markets. Especially after the mid-2000s the share of EU, traditionally the biggest export and import partner of Turkey, in exports started to decline below the level of 50%, while the shares of the Middle East, North Africa and “other Europe”²⁶⁷ started to increase. On the imports front, the decline in the share of EU was more evident while the shares of East Asia and “other Europe” increase substantially. As Babacan emphasized, the discussions about the so called “axis shift” might seem to be well fitting into Turkey’s changing foreign trade structure as the number of new export destinations and the significant rises in Turkey’s bilateral trade volume with Latin American, African and Middle Eastern countries as well as China could display such a case.²⁶⁸ It is important to bring in mind that although Turkey has successfully managed to increase its total trade volume as well as the diversity of its destinations, the main axes of its foreign trade partners remained unchanged in the 2000s.

²⁶⁷ The European countries other than EU members.

²⁶⁸ Babacan, *op. cit.*, p. 9.



Source: Republic of Turkey Ministry of Economy, 2000-2010, Billion US \$.

Figure 13 Turkey's Foreign Trade, 2000-2010

Actually, the changing structure of the Turkish foreign trade fits well into the new global trends since the 1990s, but especially in the 2000s. A careful analysis reveals the close correlation and overlap between the global patterns and Turkey's foreign trade in terms of trade partners, given the relative rise of the new and fall of the traditional centers. Indeed, world trade has undergone profound changes with tectonic shifts in global trading patterns throughout the 2000s. In this context, new power centers have emerged not only economically but also politically. As emerging markets' economic weight increases, their stake in that system is set to rise. In that sense, establishment of the G-20²⁶⁹ or coalescence of BRIC(S)²⁷⁰ countries indicated

²⁶⁹ G-20 (The Group of Twenty) was established in 1999 to bring together systemically important industrialized and developing economies to discuss key issues in the global economy. While the China, India, Russia, Republic of Korea, Brazil, South Africa, Turkey, Argentina, Mexico, Saudi Arabia and Indonesia constitutes the emerging wing; traditional powers like USA, Canada, Japan, Australia, United Kingdom, France, Italy, Germany, and European Union constitutes the developed wing.

²⁷⁰ BRIC is an acronym that refers to the countries of Brazil, Russia, India and China which are all regarded as the rapidly developing and emerging markets in the global economic system. By the end of 2010, after intense efforts, South Africa became the fifth member of the BRIC grouping and the group renamed as BRICS.

the growing importance of the emerging economies in world politics and also manifested the growing recognition that key emerging economies were not adequately included in the core of global economic discussion and governance. In order to emphasize the rise of trade and this axis shift in global economy, a prominent economist said that the three most important words in the past decade were not “war on terror” but “made in China”. On present trends, he adds, the three most important words of this decade will be “owned by China”.²⁷¹ Contrary to the past experiences, according to estimates, 90% of world growth will be generated outside the EU by 2015 and one third of it will be generated in the new locomotive of the global economic growth, China alone.²⁷² Since it is quite evident that a slow but gradual ‘axis shift’ towards East is in place at a global scale; it is natural for a state like Turkey to develop new ties or to strengthen the already existing weak ties with the emerging markets and its neighboring countries on the grounds of increasing economic power, dynamic young population, and common geographical, historical, religious and cultural ties.

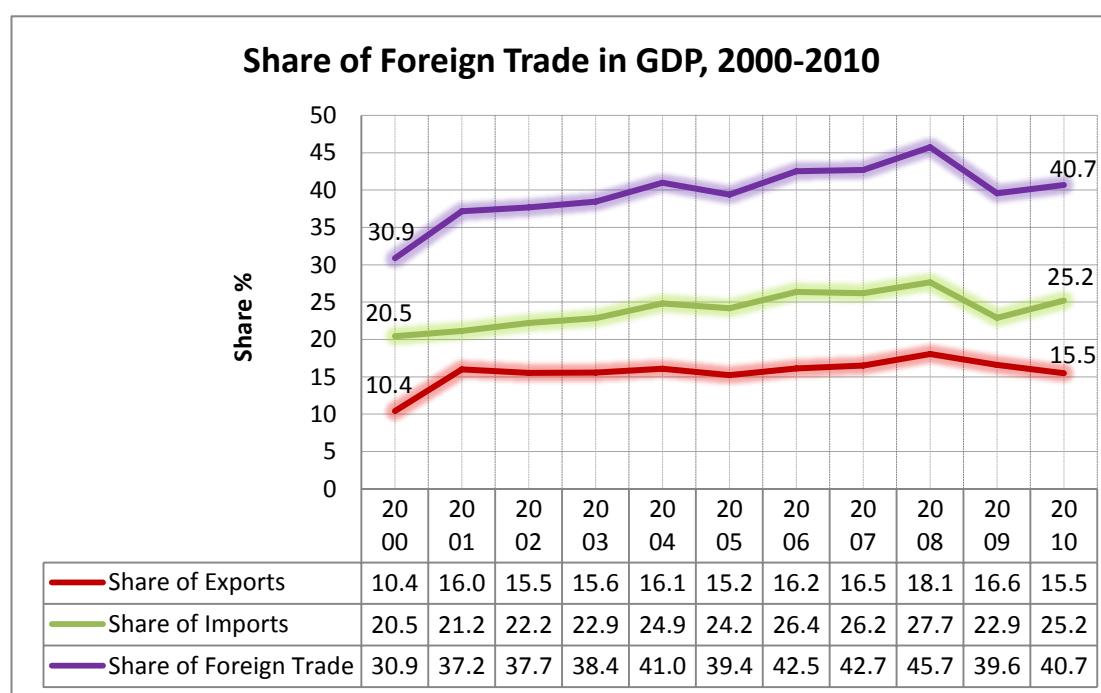
The transformation process of the export and import composition was almost complete in the 1990s. Thus in the 2000s, the composition of exports and imports barely changed and according to ISIC Rev.3, the average shares of industrial, agricultural and mining products in total exports were 93%, 5% and 1% respectively. On the imports side, the shares of industrial, mining and agricultural products in total imports were 80%, 14% and 3% respectively. Although the composition of exports hardly changed during the period, a transformation tried to be realized in terms of producing medium and high-tech products rather than low-tech products. In addition, according to System of National Accounts (SNA) classification, the shares of capital and intermediate goods in exports slightly increased whereas the share of consumption goods fell notably during the 2000s. As the industrial production

²⁷¹ Lionel Barber, “The End of US Hegemony: Legacy of 9/11,” *The Financial Times*, 05.09.2011, <http://www.ft.com>, internet acces: 06.09.2011.

²⁷² Karel De Gucht, European Commissioner for Trade, Speech at the annual seminar "EU Business in China: 2011/2012" organized by the European Union Chamber of Commerce in China, Brussels, 20 September 2011., <http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/11/587&type=HTML>, internet acces: 20.11.2011.

develops, imports of capital goods declined in favor of intermediate goods while the share of consumption goods did not change.

Another important indicator of rising importance of foreign trade, economy's openness or external orientation is the foreign trade as a percentage of GDP. Throughout the 2000s, the share of export, imports and hence foreign trade in GDP increased substantially.



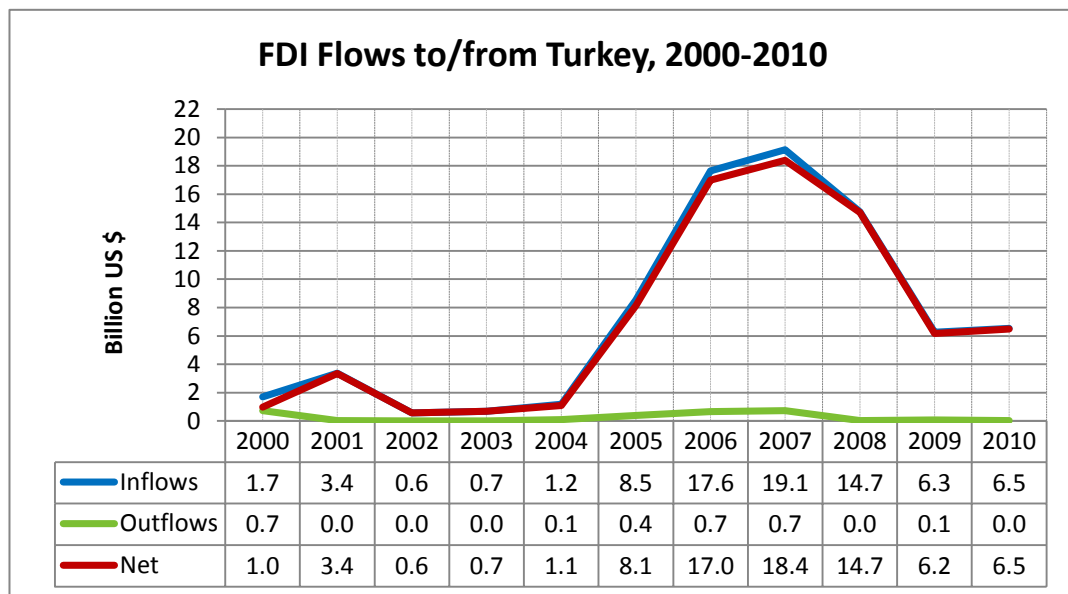
Source: TurkStat and IMF-World Economic Outlook Database-September 2011, Share (%).

Figure 14 Share of Foreign Trade in GDP, 2000-2010

As seen in the graph above, as a result of this strong performance during the period, the share of exports and imports in GDP increased from 10% to 15% and from 20% to 25% respectively. In this framework, between 2000 and 2010, the share of foreign trade in GDP increased 10 points and reached 41% in 2010. Therefore the average share of foreign trade in GDP sharply rose from 23% in the 1990s to 40% in the 2000s. Actually, these shares were the highest levels that were recorded up till now. In other words, in the 2000s foreign trade steadily grown and started to constitute a growing proportion of Turkish economy. Furthermore, these relatively

high levels have signalled the rising importance and magnitude of foreign trade in both domestic and foreign politics in the 2000s.

In order to show the economic integration and interdependence of Turkey it is also useful to have a look at the FDI flows during the 2000s. In parallel with the foreign trade tendency, FDI activities revived in the 2000s and mainly after the mid-2000s. In this context, FDI inflows to Turkey rapidly and sharply increased whereas the FDI outflows have remained minimal, below \$1 billion. In terms of FDI inflows, EU's December 17, 2004 decision to initiate membership negotiations with Turkey marked a turning point for Turkey. This decision of the EU facilitated to convince international investors and multinational corporations that the future of Turkey lies with the EU.²⁷³ In other words, EU's strong signal about the prospective EU accession of Turkey convinced the investors that the most problematic institutional, legal and judicial obstacles to FDI inflows would eventually be removed.²⁷⁴ As a result, the FDI inflows to Turkey bounced substantially after 2004.



Source: CBRT and UT, 2000-2010, Billion US \$.

Figure 15 FDI Flows to/from Turkey, 2000-2010

²⁷³ Selin Sayek, "FDI in Turkey: The Investment Climate and EU Effects," *The Journal of International Trade and Diplomacy*, Vol. 1, No. 2 (Fall 2007), p. 107.

²⁷⁴ İzmen and Yılmaz, *op. cit.*, p. 20.

As can be seen from the figure above, despite sharp fluctuations, FDI inflows increased during the 2000s. Especially in the subsequent years of crises, FDI inflows dropped substantially. In this context, FDI inflows dropped from \$3.4 billion in 2001 to \$600 million in 2002 and after the EU's decision jumped from \$1.2 billion to \$8.5 in 2005 and 19.1 billion in 2007. However, with the impact of global crisis FDI inflows started to drop after 2007 and dipped in 2009 and after a slight recovery, were reached \$6.5 billion in 2010.

In parallel with the developments in bilateral trade and political relations in the 2000s, although the European countries remain the biggest investors, the share of Gulf countries increased during the period. However, when the worldwide trends of FDI flows and the share of Turkey in the global FDI flows are taken into account, it is evident that Turkey has not been able to benefit from the increased extent of foreign direct investment activity worldwide and fell behind other emerging markets. In addition, most of the FDI inflows has come in the form of mergers and acquisitions rather than greenfield investments and was mainly directed towards banking and retail trade.

In a nutshell, despite deficiencies in some areas of the economy and trade, relatively good economic and trade performance shown in the post-2001 period strengthened the hand of the AKP. Since, all of these developments in economy and trade largely emerged as a consequence of the policies pursued by the AKP government, it is important to analyze the economic and resultant political orientation and mentality of the AKP. In this framework as Öniş puts it, a strong emphasis on liberal economy, properly regulating market economy, attracting foreign direct investments, realizing privatizations, booming exports via increasing production directed to exports constitute the main fundamentals of economic thinking of the AKP which presented itself as a progressive force that could bring benefits from the positive aspects of economic globalization, based on active participation and competition in the global market.²⁷⁵ In parallel with these economic objectives, a strong western orientation with full commitment to EU membership

²⁷⁵ Ziya Öniş, "Globalization and Party Transformation: Turkey's Justice and Development Party in Perspective," pp. 9-14, <http://www.setav.org/ups/dosya/15714.pdf>, internet acces: 21.11.2011.

while following entrepreneurial approach towards the rest of the world, especially towards the Middle East and North Africa, Latin America and South-East Asia constitutes the foreign policy orientation of the AKP.²⁷⁶ As a result of this significant foreign policy shift from a hard-line nationalistic stance towards a pragmatic approach, relations with all neighboring countries have also improved during the 2000s. Hence, the foreign policy paradigm adopted by the AKP government, which subsumed “constructive engagement in its neighborhood and beyond” and based on the improvement of bilateral economic and commercial relations as a tool of engagement, paved the way for an increasing role of business associations as foreign policy actors.²⁷⁷

Since the government has used greater volumes of trade, especially exports, and investment as an instrument of its foreign policy, exporters and industrialists emerged as the natural ally of the AKP government to reach its objectives. However, since the state cannot be expected to have the resources to maintain direct contact with businessmen, it cooperates with business associations, which voice the interests of businessmen and provide a platform for business-state interaction in an effective manner, for the purpose of attaining the common good.²⁷⁸ In harmony with its economic mentality and strategic partner choice, AKP has treated the private sector much more favorably and approached it pragmatically than any government to date and in return it was staunchly supported by large segments of the private sector. Business support, notably from small and medium-sized business units falling under the umbrella of major nation-wide business associations, TİM (Turkish Exporter's Assembly), TOBB (The Union of Chambers and Commodity Exchanges of Turkey), DEİK (Foreign Economic Relations Board), MÜSİAD (Independent Industrialists and Businessmen's Association), TUSKON (Confederation of Businessmen and Industrialists of Turkey) and ASKON (Anatolian Lions Businessman Association) have constituted a crucial element of the AKP's electoral support. AKP tried hard to develop good relations with these associations. In this picture, TUSİAD have a rather

²⁷⁶ *Ibid.*, p. 17.

²⁷⁷ Atlı, *op. cit.*, p. 116.

²⁷⁸ *Ibid.*, p. 124.

different position. Contrary to other associations, its stance and activities in the domestic politics sometimes strained the relations with the AKP. However, the AKP certainly tried not to conflict with more established industrial elites of the İstanbul region during its tenure.²⁷⁹ Since, the support of the numerous SMEs which spread across the country, counted much more at election time, the AKP has rather focused on this group. In this context, AKP's religious and socio-cultural roots along with its discourse facilitated the party to establish a consistent relationship with this group.

The government may not have helped these rising industrialists directly by providing them protection or large subsidies but it has certainly worked in a move to gain access to not only the new export markets to sell their products but also new supply markets to buy raw materials or inputs which have been in dire need to produce export products. In this respect, the largest trade missions until today were organized under the leadership of the high-level politicians of the AKP. During these visits, trade delegations which have been made up by tens or sometimes hundreds of businessmen, have gone abroad under the leadership of the AKP government and signed business deals worth millions and even billions of dollars. As Atlı emphasized, in contrast with their immediate predecessors, both President Abdullah Gül and Prime Minister Recep Tayyip Erdoğan and the consecutive State Ministers responsible for Foreign Trade Kürşad Tüzmen and Zafer Çağlayan adopted the Özal's model of active public-private partnership in foreign economic relations.²⁸⁰ In addition, the AKP government also organized events with a view to bring together the public and private sectors in order to build up national strategies and to find joint solutions to the economic and commercial problems. Highest representative bodies of businessmen have called for and welcomed to participate into these events.²⁸¹ In addition, businessmen have been actively represented at the Joint Economic Commission (JEC) meetings, which are held on a bilateral inter-governmental basis with foreign countries by DEİK. These meetings provide a platform for the

²⁷⁹ Pamuk, "Globalization, Industrialization and Changing Politics in Turkey," p. 271.

²⁸⁰ Atlı, *op. cit.*, p. 116.

²⁸¹ *Resmi Gazete*, Prime Ministerial Circular, Date. 12.05.2010, No. 27579, <http://www.resmigazete.gov.tr>, internet access: 20.11.2011.

respective parties to negotiate a road map about the future of their economic relations and formulate their policies.

Besides, it has to be noted that both national and international events organized by the business associations have been supported by the senior bureaucrats from the Undersecretariat of Foreign Trade, the Ministry of Foreign Affairs, Prime Ministry or Presidency. This high-level participation gives the business associations the opportunity to directly report to the “state” problems and policy recommendations experienced by the Turkish business circles not only in national but also in international levels. Hence this participation enables business communities of both sides to have direct contact with these statesmen. Furthermore, through international organizations, officials from different countries take the opportunity to exchange opinions and ideas with each other within a semi-formal and business-oriented setting. In addition to joint organizations, senior executives of these associations have regularly paid visits to the high-level state officials, in which they find the opportunity to directly express the opinions of the business circles they represent and rapidly find solutions to their problems, thus always have kept in touch with the state.

This rising business class produced its own business associations, which were established with the purpose of exploring new market opportunities and creating business partnership networks for their own clientele.²⁸² One of these business associations is the MÜSİAD. In its early years, as mentioned before in the previous chapter, MÜSİAD supported the Islamist parties led by Necmettin Erbakan, but the members were increasingly alienated by the inward-oriented, anti-Europe rhetoric of these parties. Ever since the group of politicians led by Recep Tayyip Erdoğan and Abdullah Gül broke off from Erbakan and moved to establish a new political party in 2001, the new industrialists and MÜSİAD offered critical support to AKP for its more moderate, outward looking, pro-Europe, pro-globalization positions.²⁸³ In this

²⁸² Atlı, *op. cit.*, p. 116.

²⁸³ Pamuk, *loc. cit.*, p.271.

context, numerous members of the association joined the AKP and provided not only financial but also human capital.²⁸⁴

Another one is the TUSKON which was founded in 2005 by 7 different regional business federations, in order to represent and enable Turkish businessmen to develop and penetrate into global markets in several industries ranging from iron-steel industry to textile industry.²⁸⁵ Today, approximately 33 thousand entrepreneurs, mainly from conservative new industrial centers, in 80 different provinces of Turkey are represented by TUSKON. Another business association is the ASKON which was founded in 1998, with an Erbakan-style, pro-Islamic discourse of economy and trade. In fact, similar concerns which have also felt by the MÜSİAD led the ASKON to build close relations with the AKP government. Regardless of its name, ASKON is representing approximately 560 companies from Marmara Region, mainly from İstanbul.²⁸⁶

Turkey asserts its new geo-strategic position via set of policies and instruments under the light of strategic engagement along with the practical and often tactical moves that would enhance regional and bilateral diplomatic and economic relations. MÜSİAD is in search for increased cooperation with the Gulf countries while the emerging business group, TUSKON has been actively engaging with the African and East Asian markets, and ASKON is focused primarily on the neighboring countries. Turkey's oldest business group TÜSİAD, in the meantime, actively lobbies for the eventual EU membership of the country.²⁸⁷ Beyond these, as being the top organization of the Turkish exporting firms around 50 thousand, Turkish Exporter's Assembly (TİM) has conducted several activities from lobbying in the country and abroad to taking part in the process of determining export policies and targets, from organizing trade missions and fairs to providing foreign trade consultancy services in order to defend the interests and rights of the exporters. In

²⁸⁴ Şebnem Gümüşçü and Deniz Sert, "The Power of the Devout Bourgeoisie: The Case of the Justice and Development Party in Turkey", *Middle Eastern Studies*, Vol.45, No. 6 (November 2009), p. 964.

²⁸⁵ <http://www.tuskon.org/hakkimizda/?id=history>, internet access: 20.11.2011.

²⁸⁶ <http://www.askon.org.tr/uyeler.asp?sirala=il>, internet access: 20.11.2011.

²⁸⁷ Babacan, *op. cit.*, p. 11.

this context, as a result of its wide-range exporter base, regardless of any specific region, TİM focused on all profitable regions from Brazil to China and India. In Kutlay's words, the interaction and mutual interdependence between Turkish businessmen and their counterparts have turned into one of the "practical hands" of Turkish diplomacy in the course of 2000s.²⁸⁸

At this point it is important to note that although the business associations started to function as foreign policy actors and their role in the foreign policy making substantially increased under the leadership of the AKP, their role has remained instrumental to a large extent. As Atlı stated, business associations do not have an autonomous role in shaping Turkey's foreign economic policies since they remain within the policy framework set by the state or government and refrain from challenging the policy objectives of state actors.²⁸⁹ Nevertheless, this does not mean that their role is insignificant. By establishing a platform of interaction between the state and the business community, business associations function as synapses which transmit the private sector's demands and opinions to the state. On the other hand, business-state interaction is also instrumental in facilitating the policies through providing greater legitimacy.

Besides all of these developments, during the period of AKP, a number of changes which was made in the state structure, indicates the rise of the "trading state" and transformation of the existing state structure in the direction of a powerful "trading state". In this context, the number of overseas commercial counselor cadres doubled to 250 and number of foreign missions increased to 100. State Minister responsible for Foreign Trade Zafer Çağlayan described the commercial counselors as the hand, arm and eye of the private sector in respective countries.²⁹⁰ This is also an indication of the changing perceptions about the relationship between bureaucrats and business circles. In addition, after the global economic crisis, in May 2009 Zafer Çağlayan, became the State Minister responsible for Foreign Trade. Like Özal, Zafer

²⁸⁸ Mustafa Kutlay, "Economy as the 'Practical Hand' of 'New Turkish Foreign Policy': A Political Economy Explanation," *Insight Turkey*, Vol. 13, No. 1 (2011), p.77. pp. 67-88

²⁸⁹ Atlı, *op. cit.*, p. 125.

²⁹⁰ Ticaret müşavirleri özel sektörün eli kolu olacak, *Dünya Gazetesi*, 25.04.2011, <http://www.dunya.com>, internet access: 22.11.2011.

Çağlayan, who had been an industrialist, President of the ASO (Ankara Chamber of Industry) and the Vice-President of the TOBB, has also been recognized and trusted by the businessmen before he was appointed. Furthermore, in the framework of changes which was made in the organization of the state in 2011, the name of the Undersecretariat for Foreign Trade converted into Ministry of Economy. This shift constitutes an interesting manifestation of the rising importance of foreign trade and the fact that foreign trade, especially exports, has been positioned at the heart of the economy policies of the AKP government. A similar change has made by the Özal government in 1983, at a time when the foreign trade and export were at the top of the economy agenda.

To sum up, all of the aforementioned changes and transformations in the domestic politics, in the role of the state and businessmen, in the way that the foreign policy conducted, in the foreign policy instruments, in the relations between public and private sectors and in the state apparatus itself all together signalize the rise of the “trading state” and this rise seems unlikely to change in the future.

4.2. Turkey’s Political Relations with Iran in the 2000s

As mentioned before, political and also commercial relations between Turkey and Iran seriously deteriorated throughout the 1990s. As a result, immediate neighbors of the 1980s became distant neighbors in the 1990s. Nevertheless, Turkish-Iranian relations have started to improve again in the 2000s. In this framework, Turkey has abandoned its remote policy towards Iran in favor of an unprecedented level of political, economic and cultural engagement. This thesis argued that this shift in bilateral political and commercial relations mainly stemmed from, *inter alia*, the transformation of the Turkish foreign policy and the rise of the “trading state”. In this context, Turkish-Iranian relations have considerably driven by economic considerations during the 2000s. Political and economic shifts in the global and regional system have significantly contributed to the improvement of Turkish-Iranian relations as well. As a consequence, further bilateral political relations

improved, the further economic relations gained momentum and *vice versa*, during the period.

Actually, Turkish-Iranian rapprochement in foreign policy and foreign trade in the 2000s have started during the then Minister of Foreign Affairs İsmail Cem. However it has substantially gained momentum during the tenure of the AKP, which started in November 2002. In other words, first small steps towards Iran have taken by İsmail Cem however, the AKP government has moved towards Iran at the double.

In the course of the 2000s, fundamental parameters of Turkish-Iranian relations were profoundly altered again. First of all, the shift in the global system from a unipolar to a multipolar world and the increasing pace of globalization facilitated bilateral relations. At the regional level, the strategic environment in which Turkey conducted its neighborhood relations transformed deeply. US invasion of Iraq upset all the balances and brought out serious consequences for Turkey and Iran. In the domestic level, since the AKP's rise to power Turkey's domestic politics has undergone a sea change. The new leadership set about altering the character of the Turkish state in a manner that diminished the role of the military-bureaucratic influence and the ideological differences in Turkish-Iranian relations. The number and substance of actors in domestic and foreign policy increased and changed substantially. In this new foreign policy Turkey envisaged and positioned as a central player which required greater regional activism and trade-driven foreign relations, thus a new economy-oriented foreign policy. In this context, cooperation between Turkey and Iran gained momentum in areas such as security, energy and nuclear issue. Furthermore, Turkey's deteriorating relations with the US and Israel, developing relations with the Middle Eastern countries and AKP's pro-Islamic discourse welcomed by Iran and generated a positive atmosphere in which Turkey and Iran come together.

4.2.1. AKP Government and the Policy of “Zero Problem with Neighbors”

Since the AKP’s rise to power in November 2002, Turkey’s involvement in the Middle East clearly started to go beyond the Kurdish issue and took a more opportunistic turn.²⁹¹ The AKP government has given high priority to the Middle East in foreign (trade) policy within the context of “zero problem with neighbors” policy and has attached more importance to the Middle East than any previous governments. The architect behind this change has been the Ahmet Davutoğlu who was appointed as the Minister of Foreign Affairs in 2009 and served as Chief Advisor to the Prime Minister Erdoğan from 2002 to 2009. As İbrahim Kalın, successor of Davutoğlu as the current chief foreign policy advisor of Erdoğan said that Davutoğlu’s book “Strategic Depth: Turkey’s International Position” came to be seen as the new bible of Turkish foreign policy.²⁹² In his book, Davutoğlu manifested five principles: (1) a balance between security and democracy; (2) zero problem policy with neighbors, (3) developing relations with neighboring regions and beyond, (4) multi-dimensional foreign policy, and (5) rhythmic diplomacy that underlie in the heart of the new Turkish foreign policy.²⁹³ By this way Davutoğlu positioned Turkey as a “center-country” in its region.

In the framework drawn by Davutoğlu, the AKP has started to pursue more active foreign (trade) policy in the region through advocating a “zero problem with neighbors” strategy. In this context, the determinants and actors of the Turkish foreign policy have considerably changed and diversified, thus economic considerations and economic actors have given priority in the making of foreign policy by the consecutive AKP governments. As highlighted before, the

²⁹¹ Altunışık, “Turkey’s Changing Middle East Policy,” p. 150.

²⁹² İbrahim Kalın, “Turkey and the Middle East: Ideology or Geo-Politics?,” *Private View*, Autumn 2008, <http://www.setav.org/public/HaberDetay.aspx?Dil=tr&hid=11010&q=turkey-and-the-middle-east->, internet access: 22.11.2011

²⁹³ Bülent Aras, “Davutoğlu Era in Turkish Foreign Policy,” *SETA Policy Brief*, No:32 (May 2009), pp.7-10; Ahmet Davutoğlu, “Turkey’s Foreign Policy Vision: An Assessment of 2007,” *Insight Turkey*, Vol. 10, No. 1 (2008), pp.79-82; Ahmet Davutoğlu, *Starejlik Derinlik: Türkiye’nin Uluslararası Konumu*, 70th ed., Küre Yayınları, İstanbul, Temmuz 2011.

transformation of the Turkish economy from an ISI driven economy to an export driven economy and growing reliance on imported energy has compelled Turkey to prioritize pragmatism and economic considerations, thus the foreign policy of Turkey started to transform into that of a “trading state” in the 2000s.

Fundamental political and economic changes in the global system throughout the 2000s have also played a decisive role in the making of the AKP’s foreign policy. Especially, the shift in the gravity center of the global economy from Euro-Atlantic axis to Asia-Pacific had significant repercussions. The AKP government considered the power shift in economic realm will spill-over to political and military realms and envisaged that Asia-Pacific will become the globe’s new geopolitical and geo-economic center in the future. In this context, the establishment of good political and economic relations with these emerging economies became one of the main objectives of the AKP government. In addition to the shift in the gravity center of the global economy, the globalization gained considerable momentum and hence the movement of capital, people and information has reached unprecedented levels in the 21st century. This rapid acceleration of globalization in the 2000s has also affected the foreign policy making of the AKP which supposed that the countries which could not keep pace with these changes will be eliminated from global challenge. In Babacan’s words, Turkey’s recent foreign (trade) policy orientation has not only stemmed from its own policy choices but also reflected an indispensable necessity due to the evolving nature of the world political and economic makeup.²⁹⁴ In other words, changing global equilibria following the end of the Cold War also helped Turkey to construct a multidimensional and multi-layer dynamic foreign policy. This new approach has clearly boosted foreign trade and other economic ties with the Middle Eastern, Central Asian and Caucasian (including Russia) nations; paved the way for entering into African and Latin American markets while maintaining the traditional relations with the European and Western countries.²⁹⁵

The AKP government’s comprehensive policy on the Middle East included the desire to have “zero problems with neighbors” as well as an emphasis on

²⁹⁴ Babacan, *op. cit.*, p. 29.

²⁹⁵ *Ibid.*, p. 10

diplomacy and economic interdependence. In Davutoğlu's words, Turkey's position must rest on four main principles: (1) security for everyone, not only for this group or that group, this country or that country, but common security for the entire region, (2) priority must be given to dialogue as a means of solving crises, (3) economic interdependence and (4) cultural coexistence and plurality.²⁹⁶

The AKP perceived regional trade as a "major synergy vehicle of continuous and sustainable economic development", especially to strengthen relations with Islamic countries.²⁹⁷ In this context, Middle Eastern markets became strategically important for Turkey.²⁹⁸ On the other hand, the rising power of the business class put additional pressure on the AKP government to open up new markets and forced the AKP to adopt the policy of "zero problem-limitless trade with neighbors". In return, this policy has strengthened the hand of AKP in during the elections.

Davutoğlu has singled out economic interdependence as the most important tool allowing Turkey "to gain depth" in its neighborhood, while pointing to the prominent role of private sector firms in driving the country's foreign policy and strategic vision.²⁹⁹ Along-side the efforts to create a broader free trade area, he has introduced a new and positive language of cooperation rather than conflict. Davutoğlu's "zero problems with neighbors" concept simply restates the foreign policy of a "trading state".³⁰⁰ Davutoğlu made an important point highly relevant to Turkey's experience, that those countries which have tried to make the transition from import substitution policies to export-oriented development models have found the need to make the pursuit of economic interests the main element of a country's diplomacy.³⁰¹ He also underlined the growing significance of economic interdependence in shaping Turkey's relations with most of the neighboring

²⁹⁶ Davutoğlu, "Turkey's Foreign Policy Vision: An Assessment of 2007," pp.84-85.

²⁹⁷ International Crisis Group, *Turkey and the Middle East: Ambitions and Constraints*, Europe Report, No. 203, 7 April 2010, p. 10, <http://www.crisisgroup.org/en/regions/europe/turkey-cyprus/turkey/203-turkey-and-the-middle-east-ambitions-and-constraints.aspx>, internet access: 17.11.2010

²⁹⁸ Davutoğlu, *Starejik Derinlik: Türkiye'nin Uluslararası Konumu*, p. 431.

²⁹⁹ International Crisis Group, *op. cit.*, pp. 9-10.

³⁰⁰ *Ibid.*, p. 10.

³⁰¹ Davutoğlu, *loc. cit.*, p. 511.

countries. In this context, as Kirişci emphasized, whether the zero problems with neighbors policy is a response to Turkey's increasing foreign trade and international economic relations or whether this increase is a function of Turkey's new foreign policy is a typical chicken and egg question.³⁰²

The new foreign policy is constructed by a multi-dimensional approach with advanced tools, highlighting Turkey's soft power. Davutoğlu's "strategic depth" conceptualization plays a vital role in realizing Turkey's commercial and economic potential as well.³⁰³ This thinking encourages deeper bilateral and multilateral relations with neighboring countries, and prioritizes dialogue and cooperation over coercion and confrontation.³⁰⁴ The AKP has tried to transform Turkey into a strong regional, and even global, actor through the exercise of the soft power. It is possible to state that this policy has indeed helped to improve relations with neighboring countries creating a climate more conducive for trade.

Within the scope of its regional policy, the AKP government has targeted to maintain the best possible relationships with Iran through engaging in an active dialogue and closer contact.³⁰⁵ As a result, in the 2000s an atmosphere of détente has gained prevalence in the relations between Turkey and Iran. In this framework, the secular-Islamist divide that was a major hindrance to the development of Turkish-Iranian relations at one time, has no longer shaped the course of relations in the 2000s.³⁰⁶ Together with the AKP's pro-Islamic discourse, this new approach has facilitated identifying common ground with Iran and strengthened the two countries' rapprochement in the 2000s.³⁰⁷

Besides, regional developments have played an important role in the growing rapprochement between Turkey and Iran. In this context, the developments before

³⁰² Kemal Kirişci and Neslihan Kaptanoğlu, "The Politics of Trade and Turkish Foreign Policy," *Middle Eastern Studies*, Vol. 47, No. 5 (September 2011), p. 715.

³⁰³ Babacan, *op. cit.*, p. 12.

³⁰⁴ Meliha Benli Altunışık, "The Possibilities and Limits of Turkey's Soft Power in the Middle East", *Insight Turkey*, Vol. 10, No. 2 (2008), pp. 50-51.

³⁰⁵ Karacasulu and Aşkar Karakır, *op. cit.*, p. 111.

³⁰⁶ Mohammed Ayoob, "Beyond the Democratic Wave in the Arab World: The Middle East's Turko-Persian Future," *Insight Turkey*, Vol. 13, No. 2 (2011), p. 65.

³⁰⁷ Elliot Hentov, "Turkey and Iran," p. 30.

and after the US invasion of Iraq in 2003, were all perceived as threats not only to the political and but also to the economic interests of Turkey and Iran. In addition, increasing terrorist attacks of PKK and PJAK³⁰⁸ in Turkey and Iran brought these countries closer on the grounds of security cooperation. Therefore, these commonalities of interests and threat perceptions concerning regional and security issues paved the way for the emergence of a common ground for cooperation between Turkey and Iran in the early 2000s, at a time when the US has been trying to isolate Iran. The rise of cooperation in the security issues created a positive atmosphere between the parties and paved the way for further cooperation in other areas of the bilateral relations. In other words, contrary to the 1990s, Turkey's lessened preoccupation with security concerns, survival and territorial integrity facilitated the rise of the "trading state" in the 2000s.

In this respect, as İbrahim Kalın underlined, although the US stigmatized Iran as one of the "rouge states" and as a member of the infamous "axis of evil", this has remained an exclusively American narrative for the AKP.³⁰⁹ Turkey's stance in this issue positively affected the Iran's perception of Turkey and Turkish-Iranian rapprochement. In this framework, Turkey's deteriorating relations with Israel and the US to a degree, along with its improving relations with its neighbors and the AKP's pro-Palestinian discourse positively affected the Turkish-Iranian relations in the 2000s.

Correspondingly, the number and intensity of bilateral dialogue and cooperation mechanisms such as reciprocal visits, meetings, conferences and fairs increased substantially in the 2000s.³¹⁰ In this context, multilateral and bilateral meetings such as the Neighboring Countries of Iraq Conference, OIC, ECO and D-8 Summits, Turkey-Iran High Security Commission and Joint Economic Commission meetings and fairs constituted main mechanisms that brought Turkey and Iran together throughout the 2000s. This high level of interaction in different areas from

³⁰⁸ PJAK (The Party of Free Life in Kurdistan-Partiya Jiyana Azad a Kurdistanê) is an offshoot of the PKK which was established in 2003 in Iran.

³⁰⁹ İbrahim Kalın, "Turkey and the Middle East: Ideology or Geo-Politics?,".

³¹⁰ Kadri Kaan Renda, "Turkey's Neighborhood Policy: An Emerging Complex Interdependence?," *Insight Turkey*, Vol. 13, No. 1 (2011), pp. 100-101.

politics to economics positively affected Turkish-Iranian relations and facilitated the rise of bilateral trade relations.

In conjunction with the priority of economic considerations in the making of foreign policy, contrary to the 1990s, the relative weight of the military and the Ministry of Foreign Affairs in shaping and making Turkish foreign policy have diminished in favor of other agencies and institutes such as the Ministry of Energy, Trade, Transportation, Treasury and Turkish International Cooperation and Development Agency (TİKA).³¹¹ The Undersecretariat of the Prime Ministry for Foreign Trade (UFT) has become one of the most influential agencies through shaping the economic and trade dimension of Turkish foreign policy under the leadership of former and current Ministers of Kürşad Tüzmen and Zafer Çağlayan.³¹² Both ministers have pursued Özal-style active foreign trade policies with a view to promote the economic and trade interests of Turkey. For instance, within the scope of new strategies such as “Neighboring and Peripheral Countries Strategy” numerous trade missions with the broad participation of businessmen were held under the leadership of Kürşad Tüzmen towards neighboring countries together with the Middle Eastern and North African countries. As a result of these trade missions, Turkish exporters have taken the opportunity to spread on a large area and penetrate into the new markets. In this framework, Tüzmen went to Iran several times together with large numbers of Turkish exporters. His successor Zafer Çağlayan has even moved ahead of Tüzmen. In 2010, 42 visits to 32 countries and in 2011, 27 visits to 21 countries were held under the leadership of Çağlayan and he was also accompanied by larger groups of business people. In this context, Çağlayan also went to Iran with Prime Minister Erdoğan together with the ever-largest trade mission consisting of a vast number of exporters from different sectors of the economy. He also hosted trade missions under the leadership of his Iranian counterparts in Turkey. During these meetings, obstacles in bilateral trade and investments was tried to be eliminated, problems of Turkish exporters and investors transmitted to the top Iranian officials, wide range of memorandum of

³¹¹ Kirişçi and Kaptanoğlu, *op. cit.*, p. 712.

³¹² *Ibid.*, p. 712.

understandings in foreign trade, customs and transportation, etc. were signed, negotiations of a Turkish-Iranian Preferential Trade Agreement were conducted and joint project proposals were put forward.

In addition to these new actors from the public sector, business people, business associations and NGOs have emerged as the new actors of the foreign policy during the tenure of the AKP.³¹³ In line with the new perspective for state-society and state-capital relations, the economic elite have pressured for new policy formulations not only in domestic affairs but also in foreign policy.³¹⁴ In Özcan's words, increasing involvement of non-state actors in Turkish foreign policy making-process has become one of the novel aspects of the politics.³¹⁵ As newly emerging yet strong actors begin to exert growing influence over the foreign policy issues, the official apparatus has been losing its prominence in economic and financial affairs.³¹⁶ In an interview granted to *Turkishtime*, Davutoğlu went as far as noting how the business world has become a primary driver of foreign policy. In many ways it can be argued that it is in response to growing demands coming from within Turkey and especially from business interest groups that economics and trade issues came to prominence in his foreign policy agenda.³¹⁷

Furthermore, Turkey's "trading state" policies have been reinforced by a rise in the number of new foreign diplomatic missions and commercial counselors in surrounding countries and in newly emerging centers of global economy, a liberalization of visa regime and a proliferation in the international flights of Turkish Airlines (THY). In this respect, the AKP government took the decision to liberalize Turkey's visa regime for the nationals of numerous Middle Eastern and African countries, in a significant deviation from previous practice.³¹⁸ Turkish Minister of

³¹³ Kararları elit kadrolar değil işadamları alıyor, 17.05.2009, <http://www.yazete.com/Haber/12069>, internet access: 29.11.2011.

³¹⁴ Kutlay, *op. cit.*, p.76.

³¹⁵ Gencer Özcan, "Turkey's Changing Neighbourhood Policy," *The Turkish Yearbook*, Vol. 35, 2004, p. 13.

³¹⁶ *Ibid.*, p. 13.

³¹⁷ Kirişçi and Kaptanoğlu, *op. cit.*, pp. 710-711.

³¹⁸ Kirişçi and Kaptanoğlu, *op. cit.*, p. 709

Foreign Affairs Davutoğlu openly stressed the importance of the free movement of people and the creation of free trade areas to foster greater economic activity and integration in the region.³¹⁹ Turkey's decision to encourage "flows of people, trade and ideas" has pointed out the abandoning of a "realist view of balance of power and a zero-sum understanding" of international relations in favor of a "liberal idea of opening and interdependence."³²⁰ The visa-free travel has made positive contributions to the increase of cross-border and intra-regional trade. In this context, Turkey's attempt to compensate for its trade imbalance with Iran also explains why Ankara is eager to maintain visa-free travel with Iran.³²¹ As a result, in the 2000s the number of Iranians that entered Turkey jumped by nearly 5 times, from 381 thousand in 2000 to almost 2 million in 2010. In this context, the number of Iranians who came to Turkey with the purpose of conducting commercial relations, shopping and participating into fairs, meetings and conferences and have also increased. In 2010, the number of Iranians that entered Turkey exceeded the number of people from the whole Arab world. The rapprochement between Iran and Turkey can also be seen from this rapid increase.

As underlined by the Kirişci and Kaptanoğlu, the growth of Turkey's economic engagement of its neighborhood must be seen in the light of this parallel growth in the movement of people into Turkey.³²² As a result of this policy, the number of direct or indirect flight routes of THY have sharply increased in the 2000s. These flights in themselves demonstrate the extent to which Turkey is becoming integrated with the world and its neighborhood. It is important to note that, there has been a close correlation between the distribution of the newly opened routes and the newly determined target countries of Turkey's export strategy.

³¹⁹ Yeni Bir Ortadoğu Doğuyor, *Milliyet*, 10.06.2010, <http://www.milliyet.com.tr>, internet access: 29.11.2011

³²⁰ Kemal Kirişci, "Turkey's 'Demonstrative Effect' and the Transformation of the Middle East," *Insight Turkey*, Vol. 13, No. 2 (2011) p. 44.

³²¹ Kemal Kirişci, Nathalie Tocci and Joshua Walker, "A Neighborhood Rediscovered: Turkey's Transatlantic Value in The Middle East," *German Marshall Fund Paper Series*, March 2010, p.22. <http://www.gmfus.org/publications/index.cfm>, internet access: 06.11.2011

³²² Kirişci and Kaptanoğlu, *op. cit.*, p. 709.

Businessmen are now easily conducting their relations with counterparts via direct flights to the new capitals in Africa, Asia and Europe.³²³

4.2.2. Energy Issues

One of the most significant indicators of Turkey's evolving and developing relations with Iran in the 2000s has been the cooperation in the field of energy. Turkey's increasing energy hunger and Iran's rich natural gas (world's second largest reserves of natural gas after Russia) and crude oil reserves (world's fourth-largest proven oil reserves) have provided the strategic common ground for cooperation. Indeed, the crude oil and natural gas imports from Iran have constituted a large portion of Turkey's total imports from Iran. In this context, the average share of natural gas and crude oil imports from Iran in total imports from Iran was 88.6% in the 2000s.

After overcoming American opposition to the Turkish-Iranian natural gas connection Turkey finally has begun to import Iranian natural gas in December 2001, despite the disagreements and tensions between the parties. In fact, the initiation of natural gas imports from Iran has indicated the dawn of a new period of economic and political interdependence between the two countries.

However, the disputes between the two sides about either the volume or the price of the gas have continued since the beginning of natural gas imports from Iran and the parties have halted their exports and imports several times. In this context, gas flows from Iran to Turkey have interrupted in 2002, 2003 and 2004 because of gas pricing dispute, in 2005 due to technical reasons, in 2006 owing to cold weather, in 2007 as a result of explosions on both sides of the border caused by the PKK and PJAK, and finally in 2008 subsequent to cut off gas deliveries from Turkmenistan to Iran which forced the latter to use its own gas for domestic demand.³²⁴ However, any interruption in gas delivery from Iran to Turkey has occurred in 2009 and 2010.

³²³ Babacan, *op. cit.*, p. 11.

³²⁴ Elin Kinnander, "The Turkish-Iranian Gas Relationship: Politically Successful, Commercially Problematic," *Oxford Institute for Energy Studies*, No. 38 (January 2010), pp. 9-11.

In this framework, Turkey halted Iranian gas imports with a view to renegotiate the price and/or the take-or-pay terms of the contract. The new AKP government intended to re-negotiate the earlier agreement, and finally a delegation was sent to Tehran in December 2003 for consultations on decreasing natural gas prices. During these years, despite declining natural gas prices in the global markets, Iran did not adjust the prices according to these price swings. The Turkish move to stop buying gas altogether paid off and Iran finally agreed to decrease the prices.³²⁵ Since then, natural gas flow from Iran has run smoothly to a great extent. Between 2004 and 2010, Turkey's natural gas imports from Iran increased 5 times and reached \$2.5 billion in 2010. As a result of this sharp increase, Iran has improved its share in Turkey's total natural gas imports from 12% in 2004 to 18% in 2010. During this period, Iran has remained among the top three natural gas suppliers with an average share of 10% after Russian Federation (avg. share was 43%) and Algeria (avg. share was 26%).

The increasing energy demand due to the considerable economic development in Turkey motivates the AKP government seeking new suppliers while playing the card of a natural transmitter in terms of energy transfer routes.³²⁶ In recent years, Turkey has come to the conclusion that control of energy pipelines is no less important than who controls the energy sources.³²⁷ On the other hand, natural gas and energy projects have seen as an instrument which will contribute to balance the foreign trade between Turkey and Iran.³²⁸ In this context, the AKP government has tried to turn Turkey into a regional energy hub through building several multi-billion-dollar transit pipelines to carry crude oil and natural gas from the major suppliers of the Caspian Basin and Central Asia to the major consumers of Europe. In this framework several joint agreements were signed to transport natural gas from

³²⁵ Aydın and Aras, "Political Conditionality of Economic Relations Between Patrimonial States: Turkey's Interaction with Iraq, Iran and Syria", p. 32.

³²⁶ Babacan, *op. cit.*, pp. 13-14.

³²⁷ Yoel Guzansky and Gallia Lindenstrauss, "Turkey and Iran: The Politics of Strange Bedfellows," *Strategic Assessment*, Volume 14, No. 1 (April 2011), p. 102.

³²⁸ Alpar: Turkey-Iran relations gain speed, *Turkish Daily News*, 05.09.2002, <http://www.hurriyetdailynews.com>, internet access: 03.12.2011.

Iran through Turkey. Nevertheless, the realization of some of these agreements is far from certain, due to the intensified sanctions imposed on Iran.

In this framework, Iranian gas was planned to be transferred to Bulgaria via Turkey in August 2002.³²⁹ Furthermore, in July 2004, Turkish and Iranian Energy Ministers have given instructions to work out plans to transport Iranian natural gas to wealthy European markets via Turkey. The idea, promoted during Erdogan's visit to Tehran, may well serve Turkey's aspirations to become an energy bridge between the East and West but translating it into reality is not an easy task because the road to the European heartland is long and lacking any functioning pipeline that would link Turkey to European destinations.³³⁰ In addition, Turkey and Greece have agreed to connect their energy pipeline networks in 2003. Turkey-Greece Interconnector became operational as of November 2007. However, the Greek pipeline system is not yet connected to the Western European network. In this context, a Memorandum of Understanding which will link the European Union countries Greece and Italy via Turkey to Caspian and Middle Eastern natural gas resources was signed in June 2010 in İstanbul. A second network that would transport Iranian gas to European markets would be the existing pipelines that run through Bulgaria, Romania and Hungary up to Austria. But this line also has required serious investment given its current decrepit situation.³³¹ In addition, Turkey and Iran have verbally agreed to seal two separate deals in the energy field in February 2007. The development came after talks between Turkey's Energy Minister Hilmi Güler and Iran's visiting Foreign Minister Manouchehr Mottaki on the sidelines of the Turkish-Iranian Joint Economic Commission meeting. One of the planned agreements provides the Turkish Petroleum Corporation (TPAO) with the opportunity to explore oil and natural gas in Iran, an offer Tehran has rejected for more than a decade, while the second is about the transfer of Turkmen natural gas via Iranian territory, a move that is expected to

³²⁹ Iran gas to be transferred to Bulgaria through Turkey, *Turkish Daily News*, 30.08.2002, <http://www.hurriyetdailynews.com>, internet access: 03.12.2011.

³³⁰ Iran gas deal fraught with problems, *Turkish Daily News*, 29.07.2004, <http://www.hurriyetdailynews.com>, internet access: 03.12.2011.

³³¹ Iran gas deal fraught with problems, *Turkish Daily News*, 29.07.2004, <http://www.hurriyetdailynews.com>, internet access: 03.12.2011.

concern Washington which is against bypassing the Caspian in terms of gas transfer.³³² In line with these developments, Turkey and Iran signed a Memorandum of Understanding on transferring Iranian and Turkmen natural gas to Europe via Iran and Turkey in July 2007. This move is seen as a response to Russia who tried to hinder the European Union's plan to decrease its dependency on Russia by building a new pipeline, Nabucco, to carry Central Asian natural gas to Europe. The agreement also includes a plan for the TPAO to develop Iran's South Pars gas field in three phases and extract 20 billion cubic meters of gas from there. Meanwhile, energy experts were a little skeptical about the materialization of the Memorandum of Understanding between Turkey and Iran.³³³ Turkey has put a premium on its recent deal with Iran that allows for the possibility of developing Iranian natural gas fields in cooperation with Turkish companies. In this context, Turkey, inked a \$3.5 billion preliminary deal to develop South Pars Phases 22nd-24th in 2008, however Turkey and TPAO, had not inked a final deal with Iran despite a deadline to do so in late 2009. During the Prime Minister's visit to Iran in October 2009, Iran and Turkey signed a number of deals to facilitate the efficient flow of gas through Turkey to Europe, including accords on allocating some of Iran's South Pars gas field to the TPAO, allowing Iranian gas to be transported via Turkey and allowing Turkmenistan's natural gas to be pumped to Turkey via Iran. In his speech Turkish Minister of Energy Taner Yıldız said the deals provided advantages for Turkey in the use and the sale of some phases of the South Pars gas field and added that its conditions and prices will be negotiated later.³³⁴

Another important possible cooperation ground for Turkey and Iran is the Nabucco pipeline project which has been designed to carry Caspian and perhaps Middle Eastern and Central Asian natural gas to the heart of Europe via Turkey by completely bypassing Russia. However, while its route is established, its suppliers

³³² Turkey, Iran set to increase energy ties, *Turkish Daily News*, 22.02.2007, <http://www.hurriyetdailynews.com>, internet access: 03.12.2011.

³³³ US, Russia concerned with Turkish-Iranian gas deal, *Turkish Daily News*, 17.07.2007, <http://www.hurriyetdailynews.com>, internet access: 03.12.2011.

³³⁴ Turkey, Iran sign strategic deal to carry gas to Europe, *Today's Zaman*, 30.11.2009, <http://www.todayszaman.com>, internet access: 03.12.2011.

have yet to be fully determined.³³⁵ In this respect, Turkish politicians sometimes claim that Iranian gas could help to fill Nabucco. For instance Prime Minister Erdoğan said “We want Iran to join the project when conditions will allow, and also hope for Russia’s participation in it”.³³⁶ Furthermore, Chairman of BOTAŞ, Turkey’s state-pipeline company and a Nabucco shareholder, said the project would need to turn to countries such as Iran in the future in order to secure enough gas to fill its capacity.³³⁷ Nonetheless, due to the US insistence on excluding Iran from every possible pipeline project including Nabucco in parallel with its strategy to isolate Iran in the region³³⁸, other Nabucco consortium members have said loud and clear that they do not want Iranian gas in their pipeline.³³⁹ Yet, some analysts argue that increasing inelastic energy demand of the EU will compel the European decision makers to diversify gas suppliers including Iran and this necessity will force some European countries and companies to re-evaluate their ties with Iran in the future. Turkey also supported the idea of including Iran among the suppliers of Nabucco.

In a nutshell, energy issue has constituted one of the most important grounds for cooperation between Turkey and Iran during the 2000s. Natural gas and crude oil have become increasingly vital for Turkey to sustain its economic development through industrial production in the 2000s. In this regard, secure and sustainable access to these energy raw materials at favorable prices became one of the most important priorities of Turkey. To achieve this goal and reduce its heavy reliance on some countries, Turkey which was surrounded by the energy rich neighbors and regions, has chosen to diversify its suppliers. In this context despite the US rejection and European discontent Turkey has cooperated with Iran subsequent to the completion of Tabriz-Erzurum gas pipeline, Turkey started to import Iranian natural

³³⁵ Gordon Feller, “Nabucco Chief Sees Pipeline Pumping Iranian Gas,” *Pipeline & Gas Journal*, July 2008, p. 127, www.pgjonline.com, internet access: 03.12.2011

³³⁶ Turkey hopes Russia, Iran will join Nabucco gas pipeline project, *Ria Novosti*, 13.07.2009, <http://en.rian.ru>, internet access: 03.12.2011.

³³⁷ Feller, *op. cit.*, p.127.

³³⁸ Bezen Balamir Coşkun and Richard Carlson, “New Energy Geopolitics: Why does Turkey Matter?,” *Insight Turkey*, Vol. 12, No. 3 (2010), p. 209.

³³⁹ Katinka Barysch, “Should the Nabucco Pipeline Project be Shelved?,” *Transatlantic Academy Paper Series*, May 2010, p. 14, <http://www.transatlanticacademy.org>, internet access: 05.12.2011.

gas in 2001 and the flow of Iranian gas to Turkey has increasingly continued despite occasional disruptions. On the other hand through TPAO and BOTAS, Turkey tried to cooperate with Iran in the new joint investment projects, especially in the context of South Pars natural gas field and Nabucco pipeline project. Furthermore, in the 2000s, as part of its grand strategy to become an energy hub that transmit Caspian, Central Asian and Middle Eastern natural gas and crude oil to European markets and enjoy the take-off rights of transit states, Turkey tried to serve as an energy corridor between Western markets and Iranian natural gas and crude oil resources. Turning into an energy hub has also considered as an instrument which will contribute to narrow the considerable foreign trade deficit of Turkey in favor of Iran. Aside from these economic considerations, being an energy hub could create a strategic advantage and leverage for Turkey to increase its political power in Europe and in the region.

4.2.3. Nuclear Issue and Sanctions

In the course of 2000s, nuclear issue has increasingly constituted another common ground for cooperation between Turkey and Iran. From the beginning, in harmony with its new foreign policy stance and economic interests, Turkey has pursued a compromising attitude towards Iran. In the 2000s, Turkey's position towards the Iranian nuclear issue has evolved from a passive stance to the facilitator and to the mediator respectively.³⁴⁰ In the first half of the 2000s, while the great powers adopted different approaches from a stringent containment policy to a policy of diplomatic engagement and negotiation to a policy of developing political and technical cooperation; Turkey has followed a "wait and see" policy. Since a solution could not be reached through negotiations between the conflicting parties, the nuclear issue was brought to the UN Security Council agenda in the early 2006. From then on Turkey compelled to abandon its wait and see policy and to make a

³⁴⁰ Bayram Sinkaya, "Turkey and the Iranian Nuclear Issue: From a Passive Stance to the Actual Contributor to the Peaceful Solution?," *ORSAM Foreign Policy Analysis*, 3 December 2010, <http://www.orsam.org.tr>, internet access: 05.12.2011

choice between its Western allies and its raising neighbor. Under this circumstances Turkey avoided to taking side and adopted a facilitator position by encouraging Iran and the group of 5+1 (The five permanent members of the UN Security Council plus Germany) to reach a solution through negotiations. In parallel with its new stance, Turkey met with conflicting parties several times until the proposal of Turkey to mediate between the US and Iran in late 2008. At first, Turkey's proposal was welcomed by the US but rejected by Iran. However, subsequent to a failure of the negotiations Turkey's actual mediation started in October 2009 and Brazil also involved in Turkey's mediation efforts. Finally, the two mediators achieved to persuade Iran to sign a framework agreement in May 2010.³⁴¹ However the US and its allies rejected the agreement and after consultations with Russia, China and other major parties, the US submitted a draft UN Security Council Resolution that would tighten sanctions against Iran for its failure to cooperate with the IAEA.³⁴² Outraged by the US decision, Turkey rejected to approve the new resolution in the UN Security Council that imposing a fourth round of sanctions against Iran, including tighter financial measures and an expanded arms embargo.³⁴³

In sum, from the beginning, Turkey has recognized the right of Iran to develop nuclear technology for peaceful purposes and encouraged Iran to cooperate the International Atomic Energy Agency (IAEA). On the other hand, the government has explicitly stated that it will take a stance against any initiative of the Middle Eastern countries to obtain nuclear weapons and the region must be freed from nuclear weapons while recognizing the right of developing nuclear energy for peaceful aims.³⁴⁴ In parallel with this stance, in the international arena the government has continuously supported to reach a settlement through diplomatic engagement and negotiations between conflicting parties rather than imposing new

³⁴¹ Nuclear fuel declaration by Iran, Turkey and Brazil, *BBC*, 17.05.2010, <http://news.bbc.co.uk>, internet access: 04.12.2011.

³⁴² US, partners agree to sanctions on Iran, *Washington Post*, 19.05.2010, <http://www.washingtonpost.com>, internet access: 04.12.2011.

³⁴³ UN Votes for New Sanctions on Iran over Nuclear Issue, *BBC*, 09.07.2010, <http://www.bbc.co.uk>, internet access: 04.12.2011.

³⁴⁴ Erdoğan'dan İran'a hem destek, hem uyarı, *Milliyet*, 20.10.2009, <http://www.milliyet.com.tr>, internet access: 04.12.2011.

sanctions to Iran and has strictly opposed the use of any military means against Iran. During the 2000s, Turkey has committed to comply with the UN sanctions but has not conformed to the more comprehensive sanctions individually taken by the US or the EU against Iran.

From the very beginning, numerous pragmatic political and economic considerations have motivated Turkey to pursue a compromising stance towards Iran in the nuclear issue, to involve in facilitation or mediation efforts between Iran and West and to cast a “no” vote, rather than “abstention” against Iranian sanctions at the United Nations Security Council. First of all, Turkey which had bitterly experienced the outcomes of sanctions in the case of Iraq before, has actually been rather skeptical about the effectiveness of the UN Security Council sanctions on Iran and repeating of sanctions has meant an unpleasant déjà-vu for Turkey.³⁴⁵ Secondly, during the 2000s Iran’s share in Turkey’s foreign trade increased gradually and Iran became both an important energy supplier and export market of Turkey. Therefore, not only Iran but also Turkey, as a rising trade partner of Iran, would suffer from sanctions. In addition, Turkey’s current and prospective investments in Iran, especially million dollars’ worth investments in Iran’s natural gas sector could be negatively affected by the sanctions. In this context, heavy sanctions imposed on Iran or any the probable use of any military means will pave the way for further radicalization of the Iranian regime at the expense of regional security and escalation of conflicts in Turkey’s immediate neighborhood in which Turkish trade and investment relations have expanded substantially. Not to mention the fact that, trade and investments inevitably require a stable, secure and predictable environment in which they can spring up. In other words, greater stability and security would indeed serve Turkey’s business and trade interests much better than a neighborhood stuck in conflict and Turkey’s stance in the Iranian nuclear issue can also be understood in the light of these realities.³⁴⁶

³⁴⁵ Meliha Benli Altunışık, “Turkish Policy towards Iran: What is at Stake?,” *Middle East Institute*, April 29, 2010, pp. 1-2, http://www.mei.edu/Portals/0/Content%20Edition%20P&E/Turkey%20and%20Iran_Altunisik_04292010_1.pdf, internet access: 06.10.2011

³⁴⁶ Kirişçi and Kaptanoğlu, *op. cit.*, pp. 716-717.

During the period, Turkish exporters and importers, especially the Anatolian Tigers who push for more trade with Iran despite the economic sanctions³⁴⁷, have resisted the sanctions and put considerable pressure on the government. As the representative of the Turkish Petroleum Refineries Co, (TÜPRAŞ, Turkey's only oil refinery and gasoline exporter) clearly stated: "For us, Iran is more important than America, because we get crude oil from them and we don't get anything from America."³⁴⁸ In addition to TÜPRAŞ representative, the Director of the TUSKON, the powerful representative of a wide range of Turkish companies, called for the settlement of the problem before the situation further deteriorate otherwise, the losses of the Turkish business community increased.³⁴⁹ Furthermore, Turkish President and Minister of Foreign Affairs both clearly noted that sanctions were against Turkey's economic interests, however, they also underlined that Turkey would abide by the terms of the Security Council decisions but not with unilateral sanction decisions.³⁵⁰

In conclusion, the recently improved political atmosphere between Turkey and Iran has culminated in more foreign trade. Even if there has not been a trade boom between Turkey and Iran, in correlation with the improved and stabilized political relations, bilateral trade relations have significantly and gradually developed in the 2000s. The AKP government's sensitivities towards Iran and its deep-rooted interests in developing trade relations with its neighbor have naturally contributed to the improvement of bilateral relations.³⁵¹ In the 2000s, Turkish-Iranian relations have been no longer under the monopoly of politicians and diplomats and it has been increasingly driven from below by key economic actors.³⁵² And the political will

³⁴⁷ Turkish Tigers press Iran trade amid sanctions fears, *The Daily Star*, 28.06.2010, <http://www.dailystar.com.lb>, internet access: 29.11.2011

³⁴⁸ Anna Newby, South Korea and Turkey resist sanctions against Iran, 12.08.2010, <http://csis.org/blog/south-korea-and-turkey-resist-sanctions-against-iran>, internet access: 29.11.2011

³⁴⁹ İran ambargosu bankaları kilitledi, 29.10.2010, <http://www.finansgundem.com>, internet access: 29.11.2011

³⁵⁰ Kirişçi and Kaptanoğlu, *op. cit.*, p. 717.

³⁵¹ Aydın and Aras, *loc. cit.*, p. 36.

³⁵² Ziya Öniş, "Multiple Faces of the 'New' Turkish Foreign Policy: Underlying Dynamics and a Critique," *Insight Turkey*, Vol. 13, No. 1 (2011), p. 55.

together with improved political relations has pushed economic relations forward.³⁵³ However, this does not mean that bilateral economic or political relations free from challenge or competition. In fact, Turkey's relations with Iran have influenced by both economic and political interests at the very same time. But in the course of 2000s, despite the existence of diverging economic and political interests, Turkey and Iran has put forward the converging economic and political interests and chosen to concentrate on them.³⁵⁴ A growing assertion of business ties and strategic interests nowadays is redefining Turkey's external relations with Iran, Russia and other states in the region. These developments require a layered and more complex role for the country in its region and beyond. This will not only benefit Islamic leaning business groups but also Turkey's old family conglomerates and others.³⁵⁵

4.3. Turkey's Economic Relations with Iran in the 2000s

During the 2000s, in parallel with the developing political relations between Turkey and Iran, bilateral economic relations have also grown, deepened and as a result strengthened. This period has witnessed the return and rise of pragmatism after a decade long time-lag. In this context, economic considerations such as foreign trade, investment opportunities and energy supplies started to re-shape the course of foreign (trade) policy towards Iran.

This transformation in both political and economic relations is generally attributed to the AKP government and its foreign (trade) policies. However the process has actually started before the reign of the AKP, in the period of İsmail Cem, but it has gained substantial momentum during the consecutive governments of the AKP. Throughout the 2000s, AKP government's foreign policy of "zero problems

³⁵³ Meliha Benli Altunışık and Özlem Tür, From Distant Neighbors to Partners: Changing Syrian-Turkish Relations, *Security Dialogue*, Vol. 37, No. 2 (June 2006), p. 230.

³⁵⁴ Oleg Svet, "Turkey's 'Zero Problem' Foreign Policy: An Untenable Balancing Act," *NIMEP Insights*, Vol. II, (Spring 2006), p. 73.

³⁵⁵ Gül Berna Özcan and Hasan Turunç, "Economic Liberalization and Class Dynamics in Turkey: New Business Groups and Islamic Mobilization," *Insight Turkey*, Vol. 13, No. 3 (2011), p. 83.

with neighbors” has been reflected in foreign trade in the shape of “zero problem-limitless trade with neighbors.”

There have been a number of reasons behind this transformation in relations between Iran and Turkey. In this context leadership has played an important role. During the 2000s, the number and density of high-level visits to Iran have jumped substantially. The visits of State Ministers responsible for Foreign Trade (Kürşad Tüzmen, and Zafer Çağlayan), Ministers of Foreign Affairs (İsmail Cem, Abdullah Gül and Ahmet Davutoğlu) Prime Minister (Recep Tayyip Erdoğan) and Presidents (Ahmet Necdet Sezer and Abdullah Gül) have been economically decisive and commercially lucrative in terms of enabling rapprochement with Iran. For instance, in May 2000, the then Undersecretary of Foreign Trade Kürşad Tüzmen visited Iran together with 110 businessmen and 30 bureaucrats as part of the new “Neighboring and Peripheral Countries Strategy” which has been initiated by the Undersecretariat for Foreign Trade (UFT) with a view to develop commercial and economic relations with these countries.³⁵⁶ His meetings with Iranian officials covered various issues including the establishment of a Turkish-Iranian Business Committee, the cracking down on the illegal fuel oil trade and the proposition of the Iranian authorities to turn the Economic Cooperation Organization (ECO) into a common market.³⁵⁷ In addition to Kürşad Tüzmen’s approach, the notion of İsmail Cem which attached a great deal of importance to economics had positive impacts in bilateral commercial relations with Iran. In this respect, his visit in Iran in February 2001 indicated a fresh restart of relations. İsmail Cem, was accompanied by a delegation of businessmen and devoted considerable time to trade issues during his visit to Tehran.³⁵⁸ In this framework, İsmail Cem discussed a number of economic, political and security issues in a bid to help improve troubled relations and called on both Turkish and Iranian businessmen

³⁵⁶ İran’la ekonomik yumuşama, *Milliyet*, 25.05.2000, <http://gazetearsivi.milliyet.com.tr>, internet access: 28.11.2011.

³⁵⁷ Aydın and Aras, *loc. cit.*, p. 32.

³⁵⁸ Iran should be our friend and partner, *Turkish Daily News*, 14.02.2000, <http://www.hurriyetdailynews.com>, internet access: 28.11.2011

to make efforts to increase the trade volume between the two countries.³⁵⁹ During this visit several economic agreements was signed and a parties agreed on the establishment of the Turkish-Iran Business Council.³⁶⁰ Thus in November 2001, in parallel to this new approach which gained a momentum to create new opportunities for cooperation in bilateral economic and commercial relations, Turkish-Iranian Business Council was established by signing of an agreement between DEİK and Iranian Chamber of Commerce, Industry and Mining.³⁶¹ The purpose of the business council was to develop bilateral relations in the fields of foreign trade, transportation, construction and investments including third countries. The first meeting of the Council took place in Tehran during Turkish President Ahmet Necdet Sezer's visit in June 2002.³⁶² During the 2000s, Turkish-Iranian Business Council has come together in several times and discussed the opportunities, problems, and new projects in related areas. As stated, another turning point in bilateral relations was the visit of the President Sezer which held in June 2002.³⁶³ A simultaneous visit was also held by the DEİK which gathered up over 80 business people. Interestingly, the controversy and accusations between Turkish and Iranian Presidents over the past 10 years has been replaced by the rapprochement and praise between Sezer and Khatami.³⁶⁴ In October 2003, the State Minister Tüzmen visited Tehran with 300 businessmen, who managed to sign \$200 million worth of contracts with their Iranian counterparts. During this visit, Iran promised to reduce all the customs and taxes on Turkish goods to around 4% within five years, beginning in 2004 and agreed to set up new border

³⁵⁹ Cem's visit opens new page in Turkish-Iranian economic relations, *Turkish Daily News*, 14.02.2000, <http://www.hurriyetdailynews.com>, internet access: 28.11.2011

³⁶⁰ İran ile yeni bir başlangıç, *Milliyet*, 15.02.2001, <http://gazetearsivi.milliyet.com.tr>, internet access: 28.11.2011.

³⁶¹ http://www.DEİK.org.tr/Pages/TR/İK_AnaSayfa.aspx?IKID=80, internet access: 26.11.2011

³⁶² İran Ülke Bülteni, DEİK, Ocak 2011, http://www.DEİK.org.tr/Pages/TR/İK_BultenDetay.aspx?bDetId=248&IKID=80, internet access: 26.11.2011.

³⁶³ 23 yıl aradan sonra İran'da, *Milliyet*, 23.06.2002, <http://gazetearsivi.milliyet.com.tr>, internet access: 28.11.2011.

³⁶⁴ Sezer'e sevgi seli, *Milliyet*, 19.06.2002, <http://gazetearsivi.milliyet.com.tr>, internet access: 28.11.2011.

trade centers.³⁶⁵ Moreover in February 2004, President Sezer went to Iran to attend the D-8 Summit in order to discuss a set of measures to increase efficiency and influence of the D-8, to strengthen the cooperation and solidarity among member nations.³⁶⁶ Furthermore, a committee of experts on investment and commerce also convened for the first time with this meeting. In May 2008 and 2009, Kürşad Tüzmen visited Tehran again as the State Minister responsible for Foreign Trade. In 2008, Tüzmen was accompanied by the representatives of nearly 60 Turkish companies.³⁶⁷ During his visit Tüzmen hold bilateral discussions with Iranian President Mahmud Ahmadinejad, Iranian Commerce Minister Masoud Mirkazemi, Minister of Foreign Affairs and the Co-chairman of the Turkey Iran Joint Economic Comission (JEC) Manuchehr Mottaki, Minister of Industries and Mines Ali Akbar Mehrabian and Minister of Energy Parviz Fatah. As it is understood from this long list, a number of issues from the measures that can be taken in an attempt to further increase bilateral trade to finding immediate solutions to the obstacles to trade and investments; from consultations about the implementation of Economic Cooperation Organization Trade Agreement (ECOTA) which envisaged a comprehensive liberalization of trade among the members to the exchange of views in the fields of border trade, investments, construction services, banking, transportation, energy, and customs were all handled during this visit. Again in January 2009, under leadership of Kürşad Tüzmen a trade mission which was jointly organized by the UFT and DEİK with the purpose of boosting the commercial and economic cooperation and increasing the market shares of Turkish exporting companies went to Iran. A great deal of companies from several sectors such as iron and steel, automotive spare parts, electronic and electrical machinery, plastics and rubber products, cosmetics, textiles and leather products, house and kitchenware,

³⁶⁵ Aydın and Aras, *loc. cit.*, p. 32.

³⁶⁶ Sezer Tahran'da konuştu: D-8 etkin olmalı, *Hürriyet*, 18.02.2004, <http://hurarsiv.hurriyet.com.tr>, internet access: 28.11.2011.

³⁶⁷ Ahmedinecad'la dostluk tazeledi, *Milliyet*, 09.05.2011, <http://www.milliyet.com.tr>, internet access: 28.11.2011.

furniture and construction came together with their Iranian counterparts.³⁶⁸ An estimated \$550 million worth trade deals were signed between Turkish and Iranian companies during this visit. Furthermore, President Gül participated into the 10th ECO Summit held in Tehran in March 2009. During this summit, the global economic and financial crisis, its impacts and possible measures taken to overcome the crisis were discussed by the ECO member states along with the regional and international issues.³⁶⁹ In September 2009, Turkish Minister of Foreign Affairs Davutoğlu paid an official visit to Iran, during which he met Iranian President Mahmud Ahmadinejad, Foreign Minister Manouchehr Mottaki, and Iran's chief nuclear negotiator Saeed Jalili. During the visit Davutoğlu outlined many areas that boosting bilateral relations, ranging from economic cooperation to security. Davutoğlu also highlighted the flourishing economic activity between the two countries despite the global economic crisis. In addition to discussing cooperation in various areas, the two main items on Davutoğlu's agenda were the nuclear issue and energy cooperation.³⁷⁰ In the same year, Turkish Prime Minister Erdoğan held an official visit to Iran in October with an aim of boosting bilateral relations between the two neighboring countries. During his visit, Erdoğan was accompanied by the Ministers of Foreign Affairs, Energy, Foreign Trade and Economy, Members of Parliament, journalists along with a large number of venturesome business people. This was the ever-largest Turkish mission that visited Iran.³⁷¹ During this visit the leaders of the two countries put forward the objective of increasing the volume of bilateral trade to \$30 billion by the year 2015.³⁷² In a speech delivered at the Turkish-Iranian Business Forum, Prime Minister Erdoğan said "Turkey does not considered

³⁶⁸ İran'a düzenlenecek heyet ziyareti, http://DEİKweb.neosistem.com/KonseYIcerik/1076/%C4%B0ran_a_d%C3%BCzenlenecek_heyet_ziyareti.html, internet access: 28.11.2011

³⁶⁹ Cumhurbaşkanı Gül İran'a gitti, *Hürriyet*, 10.03.2009, <http://hurarsiv.hurriyet.com.tr>, internet access: 28.11.2011.

³⁷⁰ Nükleer ziyaret, *Hürriyet*, 13.09.2009, <http://hurarsiv.hurriyet.com.tr>, internet access: 28.11.2011.

³⁷¹ Bayram Sinkaya, "Başbakan Erdoğan'ın Tahran Ziyaretinin Sonuçları ve Türkiye-İran İlişkilerinin Sınırları," *Ortadoğu Analiz*, Vol. 1, No. 11 (Kasım 2009), p. 19.

³⁷² Bayram Sinkaya, "Türkiye-İran İlişkileri ve Cumhurbaşkanı Gül'ün Ziyareti," *Ortadoğu Analiz*, Vol. 3, No. 27 (Mart 2011), p. 26.

to be a contractor in the economy. We totally left this field to the business people and investors, because this is their job. We only expand the horizon and eliminate the barriers to trade.”³⁷³ Actually, this speech clearly reflected the transformation of Turkish foreign policy and “the rise of the trading state” in the 2000s. During the last decade, not only trade has started to be used as a tool of diplomacy but also diplomacy has started to be used as a tool of trade. And this brings the chicken or the egg causality dilemma to mind. In other words, it became futile to identify which comes first in the 2000s. However, the picture of bilateral relations was totally different than the previous decade during which the political concerns explicitly came first while the commercial concerns were of secondary importance. In sum, these visits are very useful for showing the eagerness of Turkish governments to improve trade relations along with political relations with Iran throughout the period. A similar attitude has also been adopted by the Iranian side. In this framework successive Presidents, Ministers of Foreign Affairs and Foreign Trade also held visits to Turkey.

During the 2000s there have been a number of new cooperation projects on the joint agendas of Turkey and Iran. The most promising of these projects has been the Turkish-Iranian Preferential Trade Agreement. Since Iran is not a member of WTO and its market is still highly protected, especially the industrial products, signing of a Preferential Trade Agreement and subsequent implementation of it will highly-likely ignite Turkish exports to Iran. Furthermore, although it seems like a remote possibility in the near future, signing of a Turkish-Iranian Free Trade Agreement has gained currency from time to time. Iranian side has used this kind of opportunities as an indicator of discounting its isolation imposed by the US and its allies. In addition, using of national currencies and implementation of a barter system in bilateral trade between parties besides establishment of a joint free organized industrial zone have also been among the other cooperation projects. However, they could not be put into practice and remained unfulfilled.

³⁷³ Erdoğan, Türk-İran İş Forumu’nda konuştu, *Hürriyet*, 27.10.2009, <http://hurarsiv.hurriyet.com.tr>, internet access: 28.11.2011.

Despite all, still there have been a number of trade and investment irritants in bilateral economic relations. One of the most important problems has been the relatively higher customs duties imposed by Iran. One of the main reasons behind the imbalances between Turkey's exports to and imports from Iran has been disparity between tariffs.³⁷⁴ Iran has imposed high tariffs on Turkish industrial goods, ranging from 40 to 100% for some items, while the average level of Turkish tariffs was less than 4%. Besides tariff barriers, there has been also a great deal of non-tariff barriers to trade in Iran. Furthermore, Iran's business culture has made economic and commercial relations difficult in general. In addition, reference pricing system implemented by Iran adversely affected Turkish fresh fruits and vegetables exports. Moreover, Turkish transportation companies faced difficulties in Iran as a result of the differential pricing of fuel.

Although there have been some difficulties to trade and investments in bilateral economic relations along with serious strains and obstacles in bilateral political relations, Turkey has continued to strengthen its political and economic bonds with Iran. In this framework, foreign trade and the foreign direct investments have constituted the main veins through which the bilateral economic relations have improved. Consequently, bilateral trade has broken historic records by the end of the 2000s.

As can be seen from the table below, Turkey's exports to Iran substantially increased during the 2000s. Exports to Iran which were around \$236 million in 2000 increased by 13 times and reached \$3 billion in 2010. On the other hand, imports which were around \$816 million in 2000 soared by 9 times and reached \$7.6 billion in 2010. However, as a result of the global economic crisis Turkey's imports from Iran dropped by almost 60% in 2009. One of the reasons behind this decline was the falling global energy prices, both in oil and natural gas; and the other one is the shrinking demand of Turkey as a result of the downturn in the real sector production. In parallel with the imports and exports, the volume of bilateral trade jumped by 10

³⁷⁴ Turkey urges Iran to cut tariffs to balance trade, *Hürriyet Daily News*, 21.02.2007, <http://www.hurriyetdailynews.com>, internet access: 28.11.2011.

times from \$1.1 billion in 2000 to \$10.7 billion in 2010. As a chronic disease, the gap between imports and exports widened to the detriment of Turkey during the 2000s and deteriorated from \$600 million to \$4.6 billion in 2010. In addition, the proportion of imports covered by exports fluctuated between 20% and 60%. In other words, as a result of the growing imbalances in bilateral trade with Iran, exports financed on average 34% of the imports throughout the decade, while the overall exports of Turkey covered 65% of its total imports from world in the same period.

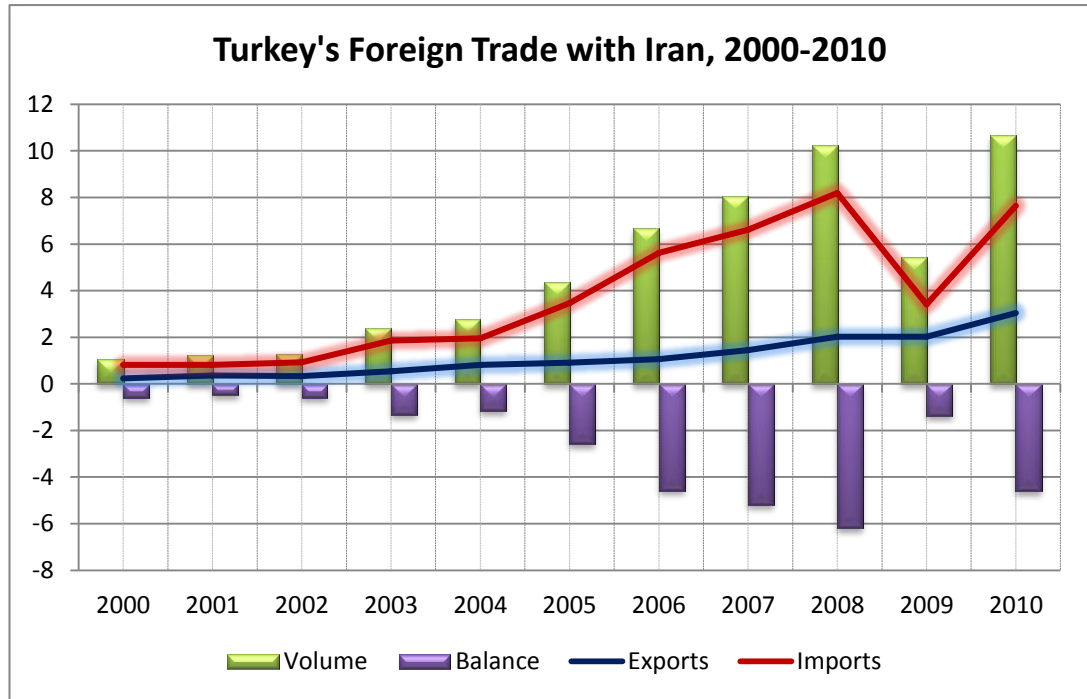
Table 7 Turkey's Foreign Trade with Iran, 2000-2010

Turkey's Foreign Trade with Iran, 2000-2010									
Years	Exports		Imports		Volume		Balance		Proportion of Imports covered by Exports (%)
	Value	Change (%)	Value	Change (%)	Value	Change (%)	Value	Change (%)	
2000	0.2	49.4	0.8	28.3	1.1	21.3	-0.6	32.5	28.9
2001	0.4	52.9	0.8	3.0	1.2	14.2	-0.5	-17.4	42.9
2002	0.3	-7.4	0.9	9.7	1.3	4.5	-0.6	22.5	36.3
2003	0.5	59.8	1.9	102.0	2.4	90.8	-1.3	126.0	28.7
2004	0.8	52.3	2.0	5.4	2.8	15.9	-1.1	-13.4	41.4
2005	0.9	12.3	3.5	76.8	4.4	57.9	-2.6	122.5	26.3
2006	1.1	16.9	5.6	62.2	6.7	52.7	-4.6	78.3	19.0
2007	1.4	35.1	6.6	17.6	8.1	20.4	-5.2	13.5	21.8
2008	2.0	40.8	8.2	23.9	10.2	27.0	-6.2	19.2	24.8
2009	2.0	-0.2	3.4	-58.5	5.4	-46.9	-1.4	-77.6	59.5
2010	3.0	50.3	7.6	124.5	10.7	96.8	-4.6	233.1	39.8
2000-10		1,191.1		837.2		916.5		693.3	

Source: Republic of Turkey Ministry of Economy, 2000-2010, Billion US \$, Annual Change (%).

As illustrated in the graph below, during the 2000s, the real increase has been recorded in the imports from Iran. When compared with imports, the increase in exports has remained minor but more stable. What is more salient is that the widening gap between volume and balance of foreign trade. Average growth rate of exports and imports were 33%, 36% while the average growth rates of volume and

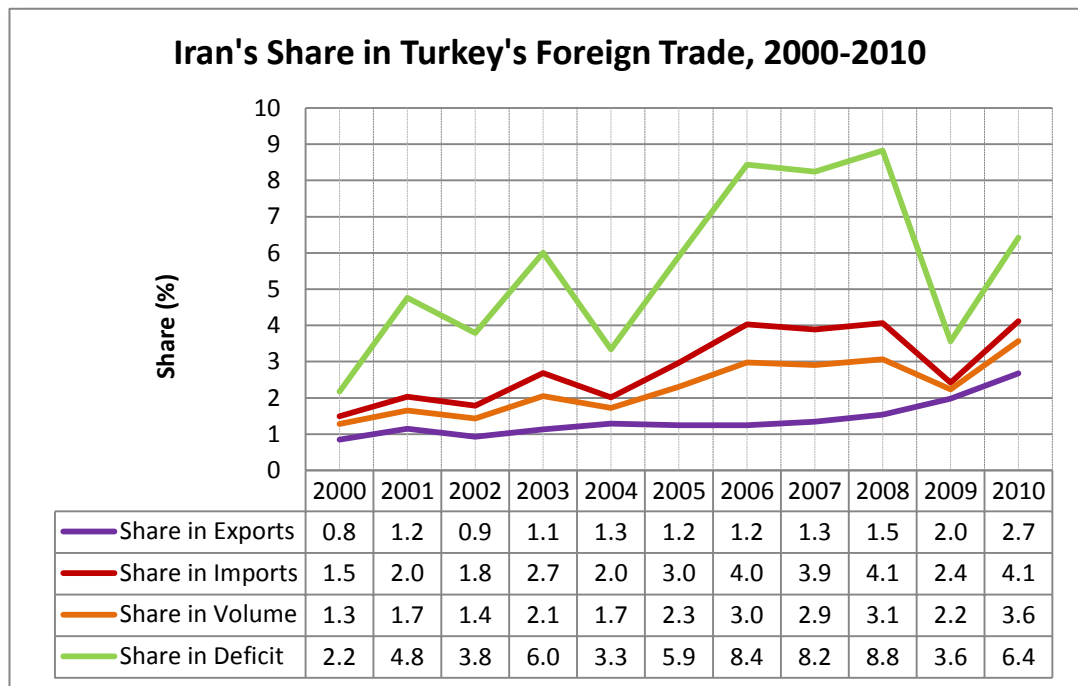
deficit were 32% and 49% respectively. In other words, Turkey's asymmetric dependence to Iran has been increased throughout the decade. In this respect the most imbalanced year of the 2000s was the 2008. This kind of an asymmetric dependence brings to mind the probable repercussions on the political independence of Turkey against Iran.



Source: Republic of Turkey Ministry of Economy, 2000-2010, Billion US \$.

Figure 16 Turkey's Foreign Trade with Iran, 2000-2010

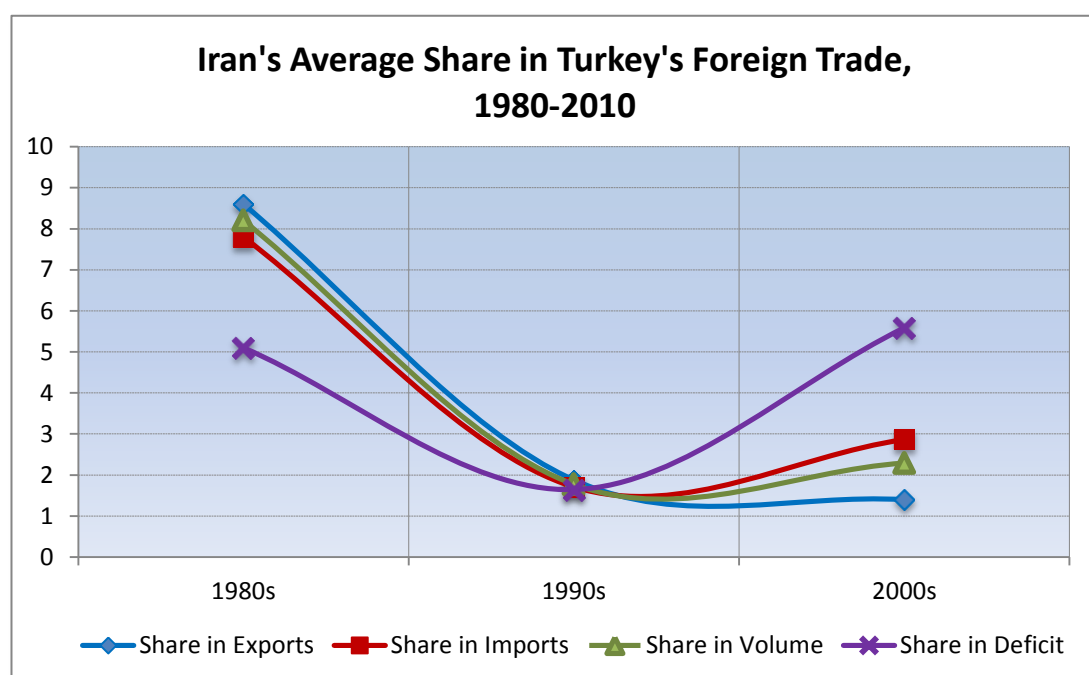
As depicted in the graph below, during the period, Iran's average share in Turkey's exports increased from 0.8% in 2000 to 2.7% in 2010. A similar upward trend also prevailed on the imports. Iran's share in total imports jumped from 1.5% in 2000 to 4.1% in 2010. In accordance, Iran's share in overall foreign trade increased two times and reached 3.6% in 2010. However, what is more gripping was the increase in Iran's share in foreign trade deficit. During the period, Iran's share in foreign trade deficit fluctuated between 2% and 9% and finally reached 6.4% by the end of the decade.



Source: Republic of Turkey Ministry of Economy, 2000-2010, Share (%).

Figure 17 Iran's Share in Turkey's Foreign Trade, 2000-2010

As can be seen from the figure below, Iran's average share in exports fell from 8.6% in the 1980s to 1.9% in the 1990s and finally 1.4% in the 2000s. Contrary to exports, Iran's average share in imports recovered to 2.3% in the 2000s after declined from 7.8% in the 1980s to 1.7% in the 1990s. As a result, Iran's average share in Turkey's total volume of trade decreased from 8.2% in 1980s to 1.8% in 1990s while its average share in trade deficit fell from 5.1% to 1.6%.



Source: Republic of Turkey Ministry of Economy, 1980s, 1990s, 2000s, Average Share, (%).

Figure 18 Iran's Average Share in Turkey's Foreign Trade, 1980-2010

Moreover, it can be useful to have a look at the rank of Iran among other export and import markets of Turkey to understand the relative rise and fall of Iran. In parallel with the developments in the share of Iran in Turkey's total exports, despite increase in exports to Iran, Iran did not placed among top 10 export markets of Turkey during the 2000s. In that sense, Iran has positioned between 24th and 14th and finally became the 10th biggest export market in 2010. This decade has witnessed the revival of Iraq, the rise of Russian Federation, United Arab Emirates and Greece as neighboring and peripheral countries along with the traditional Western markets namely Germany, United Kingdom, Italy and the US in terms of exports. As in the previous decade, Germany was the number one export partner of Turkey during the whole 2000s. On the imports, during the first half of the period Iran could not achieve to be one of the biggest 10 supplying markets of Turkey, however, in the rest of the period, it became the 7th supply market of Turkey and has preserved its position to the end of the 2010. In harmony with global trade patterns and Turkey's increasing energy requirements, the 2000s has witnessed the sharp and rapid rise of

the Russian Federation and China, alongside the traditional Western suppliers such as Germany, Italy and the US. The biggest supplier country of the 1990s, Germany was replaced by the Russian Federation in the second half of the period, thus retreated to the 2nd rank; however currently, China, the 3rd supplier, has been challenging Germany.

Furthermore, in parallel to its place in total exports, during the 2000s, Istanbul has preserved its position as the biggest exporter city of Turkey to Iran. Throughout the 2000s, the traditional suppliers of the Iran did not changed, but its average share dropped from 60% in the 1990s to 50% in the 2000s. İstanbul was followed by İzmir, Kocaeli, Bursa and Ankara respectively in terms of their shares in total exports to Iran. However, the Anatolian tigers has strengthened their position and share in exports to Iran. As mentioned before, in the 1990s some Anatolian cities such as Gaziantep and Adana were rising. But in the 2000s, a range of new Anatolian tigers such as Konya, Kayseri, Denizli, Ordu, Sakarya and Hatay rapidly increased their exports to Iran. On the other hand, as the bordering neighbor of Iran, Hakkari became one of ten biggest supplier cities of Iran throughout the whole 2000s. Although the extent of the “border trade” has been narrowed gradually during the 2000s on the grounds of smuggling, security and distortive effects on domestic market, Hakkari achieved to increase its exports to Iran. Furthermore, it has been followed by other border cities, Ağrı and Van. Rising border trade has played an important role behind this increase. On the imports side, as being the heart of the petrochemical industries and one of the biggest industrial cities, Kocaeli preserved its position as the biggest importer of the Iranian products. Nevertheless, similar to the biggest exporter Istanbul, the share of Kocaeli in total imports from Iran decreased from 75% in the 1990s to 70% in the 2000s. And Kocaeli has been followed by Ankara and İstanbul respectively, in terms of their shares in total imports from Iran. During the period traditional importers of Iranian products did not change but, their shares in total imports from Iran declined while the new Anatolian centers emerged and increased their imports from Iran. In this context, Gaziantep, Kayseri, Sakarya, Denizli and Adana have become the pioneers of the emerging and growing cities of Anatolia in the 2000s. In addition to these cities, Van has also increased its imports during the

period and rank among the first ten importers from Iran. However, imports of the border cities have been more affected by the narrowing efforts of the scope of “border trade”.³⁷⁵



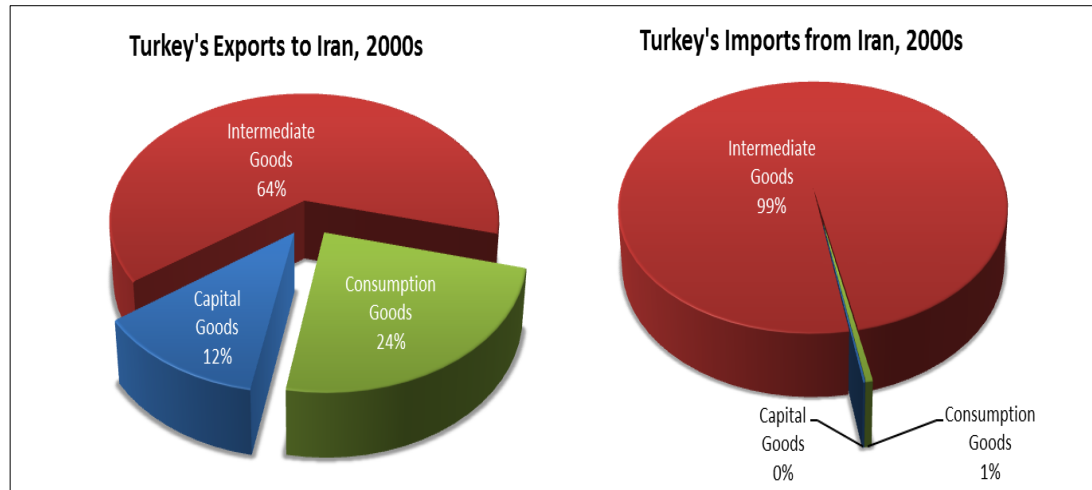
Source: Republic of Turkey Ministry of Economy, 1990-2010.

Figure 19 The Number of Turkish Companies Trading with Iran, 1990-2010

In parallel with the remarkable increase in both exports and imports and the diversification of products and also markets, the number of Turkish companies trading with Iran has also increased during the 2000s. As can be seen from the graph above, this rise in the number of companies has drawn attention when compared to the 1990s. At this point, it can be reasonable to think that these companies has improved their power through a number of aforementioned business associations and has gradually become more demanding from the government to facilitate trade by improving bilateral relations with Iran and lifting the tariff and non-tariff barriers on trade.

³⁷⁵ Border trade limited to border only, *Turkish Daily News*, 05.08.2000, <http://www.hurriyetdailynews.com>, internet access: 28.11.2011.

When the structure of the foreign trade with Iran is considered, according to SNA (System of National Accounts) classification, it is clear that Turkey's exports to Iran have become more balanced during the 2000s. In this framework, besides preserving its position as the largest part of Turkey's exports to Iran, the average share of intermediate goods in Turkey's exports to Iran dropped from 82% in the 1990s to 64% in the 2000s. Contrary to this decline, the average shares of consumption and capital goods increased notably. While the average share of consumption goods increased from 15% in the 1990s to 24% in the 2000s, the average share of capital goods soared from 3% to 12% in the same period. On the imports side, the structure of imports from Iran did not change. The average share of intermediate goods was 99% and the share of consumption goods was 1% throughout the period as it used to be. In other words, although Turkey's imports from Iran increased rapidly than the exports to Iran, Turkey has succeeded to diversify and balance its exports, while Iran has failed to diversify its exports and it has remained heavily relied on exports of its raw materials, crude oil and natural gas.



Source: Republic of Turkey Ministry of Economy, Average Share (%), SNA (System of National Accounts).

Figure 20 Structure of Turkey's Foreign Trade with Iran in the 2000s

During the 2000s, not only quantity but also diversity of export goods increased substantially. Although the main export products have not changed, new products have started to be exported to Iran. During the period, iron and steel and articles thereof, parts and accessories for tractors and motor vehicles, wood and articles of wood, tobacco and manufactured tobacco substitutes, glass and glassware, woven fabrics were among the leading export items. On the other hand, the structure of Turkey's imports from Iran hardly changed. During the decade, the place of mineral fuels and oils as the most imported item from Iran did not change, and even the average share of mineral oils and fuels in Turkey's total imports from Iran was increased from 89% in the 1990s to 93% in the 2000s. In addition to the mineral fuels and oils, refined copper or copper alloys, plastics and articles thereof, aluminum and articles thereof, ores, slag and ash, raw hides and skins, were the other most important products imported from Iran.

Furthermore, during the decade according to international standard industrial classification of all economic activities (ISIC Rev.3), the average share of manufacturing products in Turkey's total exports to Iran decreased from 98% in the 1990s to 93% in the 2000s, while the share of agricultural and forestry products increased from 2% to 5% and the share of mining products has remained unchanged at 1%. On the imports side, data indicated a minor diversification of imports. Throughout the period, according to ISIC (Rev.3), the average share of manufacturing products in total imports from Iran decreased from 82% in the 1990s to 80% in the 2000s. Similarly, the average share of agricultural and forestry products decreased from 4% to 3%. On the other hand, the average share of mining and quarrying products in Turkey's total imports from Iran increased from 13% to 14%. In addition, the average share of wholesale and retail trade rose from 2% in the 1990s to 3% in the 2000s.

Table 8 Technologic Structure of Turkey's Foreign Trade with Iran, 2000-2010

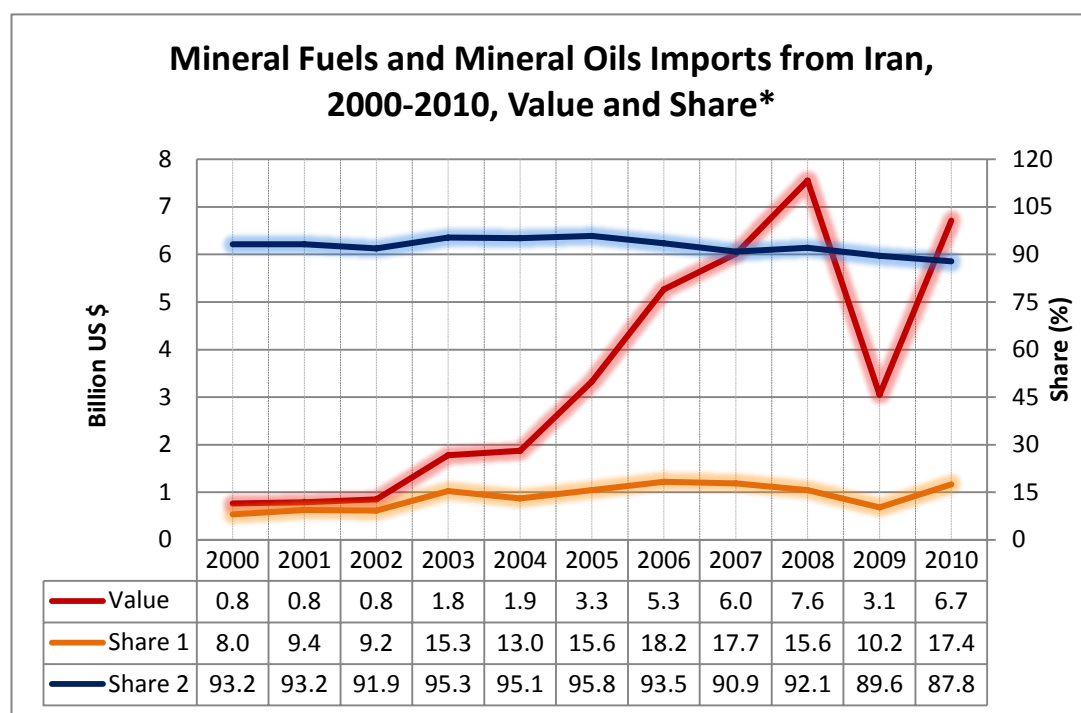
Technologic Structure of Turkey's Foreign Trade with Iran, 2000-2010								
Years	Low Tech Products		Medium-Low Tech Products		Medium-High Tech Products		High Tech Products	
	Exports	Imports	Exports	Imports	Exports	Imports	Exports	Imports
2000	40%	13%	26%	71%	33%	16%	1%	0%
2001	29%	22%	21%	41%	26%	37%	25%	0%
2002	25%	21%	20%	51%	39%	27%	15%	1%
2003	31%	26%	28%	43%	39%	30%	2%	1%
2004	31%	26%	34%	19%	34%	51%	1%	5%
2005	33%	13%	28%	34%	38%	53%	1%	0%
2006	36%	8%	29%	25%	33%	66%	1%	1%
2007	35%	6%	28%	57%	35%	37%	2%	1%
2008	30%	6%	33%	61%	35%	33%	2%	0%
2009	33%	7%	29%	42%	37%	51%	1%	1%
2010	25%	4%	42%	49%	32%	46%	1%	0%
Average	32%	14%	29%	45%	34%	41%	5%	1%

Source: Republic of Turkey Ministry of Economy, 2000-2010.

* Share in total exports to and imports from Iran, Percentage (%).

When the technological structure of Turkey's exports to and imports from Iran are considered, it is seen that during the 2000s the most exported products to Iran were medium-high tech products and it was followed by the low and medium-low tech products respectively. On the imports side, the most imported products from Iran were medium-low tech products and it was followed by the medium-high and low tech products respectively. As can be seen from the table below, high tech products in both exports and imports remained minimal during the decade, except exports in 2001 and 2002. The main reason behind these exceptions was Turkey's powered aircraft (helicopters and aeroplanes) exports to Iran. During the decade, despite fluctuations the share of medium-high tech products in Turkey's exports have remained stable, while the share of low tech products have decreased and the share of medium-low tech products have increased. Actually, this pattern fits in the production patterns of rising Anatolian tigers, which consist of mainly SMEs, to a large extent. On the other hand, the share of medium-high products in total imports

from increased notably, while the low and medium-low tech products have lost their market shares.



Source: Republic of Turkey Ministry of Economy, Value: Billion US \$, Share: Percentage (%).

*Share1: Iran's share in Turkey's total imports of mineral fuels and mineral oils.

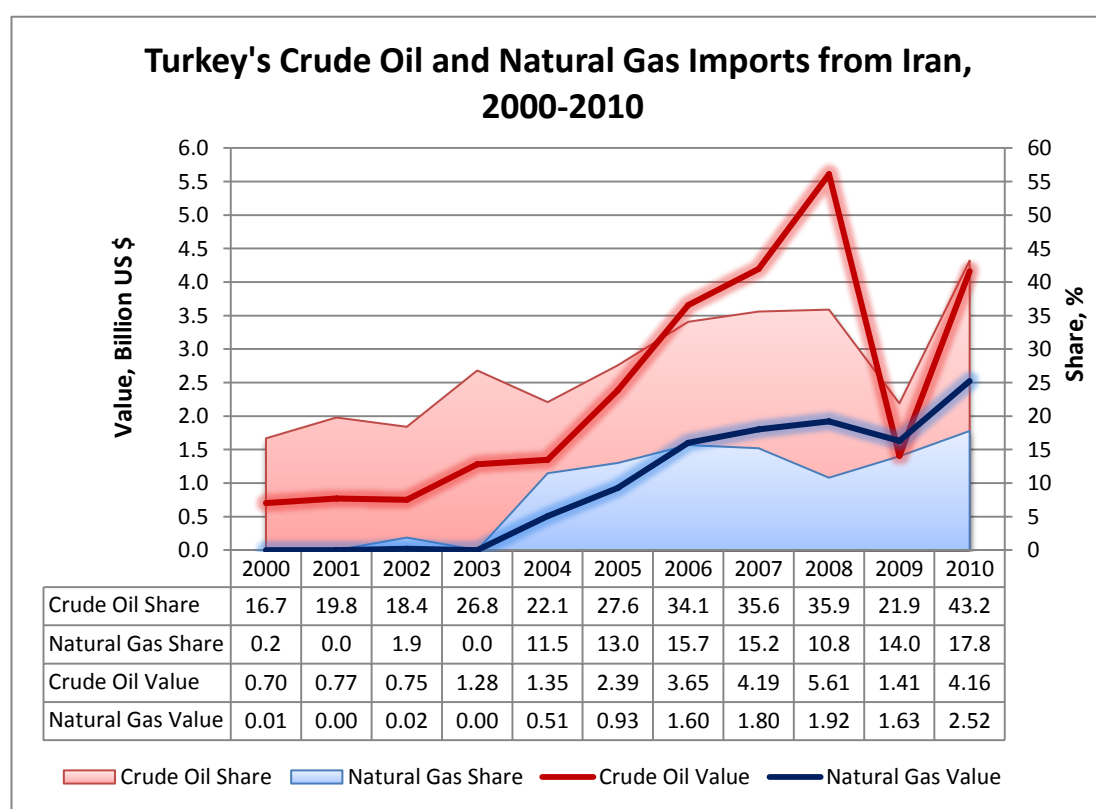
Share2: Share of mineral fuels and mineral oils in Turkey's total imports from Iran.

**Figure 21 Mineral Fuels and Mineral Oils Imports from Iran, 2000-2010,
Value and Share**

As shown in the graph above, although the share of mineral fuels and mineral oils in Turkey's total imports from Iran slightly decreased during the 2000s, it has still constituted the largest part of the imports like in the 1990s. During the 2000s, the value of mineral fuels and oils imports from Iran sharply increased except from 2009. One of the reasons behind this decline was the declining global energy prices including oil and natural gas. Crude oil prices reached a record high of US\$ 147 per barrel (US\$/b) in July 2008 on the back of a six-year commodity boom cycle driven mostly by demand from developing countries.³⁷⁶ However, by the end of 2008 and

³⁷⁶ United Nations Economic and Social Commission for Western Asia (UN-ESCWA), "The Impact of the Global Financial Crisis on the World Oil Market and Its Implications for the GCC Countries,"

2009, as demand for energy declined, especially in the Organization for Economic Cooperation and Development (OECD) countries, international prices of oil, natural gas and coal sharply plunge as well. Another reason is the dwindling oil demand as a result of the stagnation of Turkish economy because of the deepening global crisis. Even so, imports of mineral fuels and oils from Iran increased 7 times from \$800 million in 2000 to \$6.7 billion in 2010. In accordance with these developments, Iran's share in total mineral fuels and oils imports increased remarkably from 8% in 2000 to 17% in 2010. And throughout the 2000s, Iran has become one of the top three crude oil and natural gas suppliers of Turkey.



Source: Republic of Turkey Ministry of Economy, Value, Billion US \$,
 Share as a percentage of Turkey's total crude oil and natural gas imports from world.
 * HS Codes: Crude Oil-2709, Natural Gas-2711

Figure 22 Turkey's Crude Oil and Natural Gas Imports from Iran, 2000-2010

March 2009, p. 1, <http://www.un.org/regionalcommissions/crisis/escwacri1.pdf>, internet access: 28.11.2011.

As depicted in the graph below, between 2000 and 2010, Turkey's crude oil imports from Iran which holds the world's fourth-largest proven oil reserves,³⁷⁷ increased 6 times and reached \$4.2 billion. In parallel with this rapid growth, Iran's share in total crude oil imports of Turkey has also jumped from 17% in 2000 to 43% in 2010. During the 2000s, Iran enlarged its market share of crude oil in Turkey and has become one of the top three crude oil suppliers of Turkey, and it has been the number one supplier during the half of the decade. The first two rivals of Iran have been the Russian Federation and the Saudi Arabia during the 2000s.

After overcoming American opposition to the Turkish-Iranian natural gas connection Turkey finally has begun importing Iranian natural gas as of December 2001. Despite disagreements and tensions between the parties during the 2000s, Turkey has continued to buy natural gas from Iran. In fact, the initiation of natural gas imports from Iran has indicated the dawn of a new period of economic and political interdependence between the two countries. However, the disputes between the two sides about either the volume or the price of the gas have continued since the beginning of natural gas imports from Iran and the parties have halted their exports and imports several times.

Between 2004 and 2010, Turkey's natural gas imports from Iran, which holds the world's second largest reserves of natural gas after Russia,³⁷⁸ increased 5 times and reached \$2.5 billion in 2010. As a result of this sharp increase, Iran has improved its share in Turkey's total natural gas imports from 12% in 2004 to 18% in 2010. During this period, Iran has remained among the top three natural gas suppliers with an average share of 10% after Russian Federation (avg. share was 43%) and Algeria (avg. share was 26%).

In a nutshell, during the 2000s, in parallel with the improved political relations, Turkey's bilateral trade with Iran has grown strikingly. However the large part of this growth has been experienced in imports from Iran, particularly in crude oil and natural gas imports. Thus, Turkey's dependence on Iran has increased by

³⁷⁷ Energy Information Administration, "Country Analysis Briefs: Iran," 21 November 2011, p. 1, <http://www.eia.gov/emeu/cabs/Iran/pdf.pdf>, internet access: 28.11.2011.

³⁷⁸ *Ibid.*, p. 1.

growing energy imports, but this dependence has not been able to transform into an interdependence, on the grounds of reciprocity or win-win principles. In other words, by exporting large amounts of crude oil and natural gas to Turkey, Iran has gained a strategic advantage, a powerful leverage and thus an important bargaining power in bilateral relations.

In addition, Turkey's involvement in Iran has not been realized solely in the shape of foreign trade. Turkish companies have also been investing in Iran and directly contributing to employment and growth in the country.

Table 9 FDI Flows between Turkey and Iran, 2000-2010

Years	FDI Inflows from Iran to Turkey	Iran's Share (%)	FDI Outflows from Turkey to Iran	Iran's Share (%)
2002	0.0	0.0	3.0	1.2
2003	0.0	0.0	3.0	0.6
2004	0.0	0.0	4.0	0.5
2005	0.0	0.0	3.0	0.3
2006	12.0	0.1	0.0	0.0
2007	3.0	0.0	0.0	0.0
2008	25.0	0.2	128.0	4.9
2009	30.0	0.5	3.0	0.1
2010	42.0	0.6	12.0	0.7

Source: CBRT, 2002-2010, Value: Million US \$, Share: Percentage (%).

During the 2000s, foreign direct investments (FDI) flows from Turkey to Iran totaled at \$156 million, while FDI inflows from Iran reached \$122 million. However, as seen from the table below, the FDI inflows to Turkey from Iran and FDI outflows from Turkey to Iran remain minimal throughout the decade. FDI inflows from Iran started in the second half of the period and increased slightly. Although remained minimal, its share in FDI inflows to Turkey increased from 0.1% to 0.6%. On the other hand the share of FDI outflows to Iran have fluctuated during the whole period between 0.3% and 4.9%, and realized at 0.7% on an average basis. Furthermore,

Turkish investments in Iran have not been free from problems. It is important to note that, although the parties signed an investment agreement in 1996, it has entered into force in April 2005 after almost ten years.³⁷⁹ For example, after having built Tehran's Imam Khomeini International Airport, TAV Airports Holding -the leading Turkish airport construction and management company- failed to secure the right to manage it. Because, some of the hardline politicians denounced the appointment of the foreign consortium, and voiced concerns about the Turkish company's business links to Israel. In a similar way, the Turkish mobile phone operator Turkcell was not allowed access to the Iranian market. These kinds of problems have exacerbated the concerns about the investment risks in Iran and negatively affected the FDI outflows to Iran. In fact, the largest proportion of FDI inflows to Turkey come from Europe during the 2000s and these inflows have usually been accompanied by the transfer of valuable industrial know-how. On the other hand, FDI inflows from the Gulf States increased rapidly but as Kirişci and Kaptanoğlu put it, these investments have not matched with the investments from the EU in terms of size and industrial expertise.³⁸⁰

In addition to bilateral investments, Turkish contractors have disposed to joint investments with their Iranian counterparts in Afghanistan.³⁸¹ In this context, ECO has supported the reconstruction of Afghanistan through active cooperation and participation of member states. For instance, leaders of the ECO member countries gathered in Istanbul and discussed Afghan development issue in 2002 and Afghan leader Hamid Karzai urges ECO members to help the reconstruction of his war-ravaged country.³⁸²

After all, during the 2000s the overall outlook of the bilateral trade between Turkey and Iran has shown that political convergence between the parties positively

³⁷⁹ *Resmi Gazete*, Date: 25.02.2005, No. 25738, <http://www.resmigazete.gov.tr>, internet access: 28.11.2011.

³⁸⁰ Kirişci and Kaptanoğlu, *op. cit.*, 718-719.

³⁸¹ Turkish contractors ready to cooperate with Iranian counterparts in Afghanistan, *Hürriyet Daily News*, 21.02.2002, <http://www.hurriyetdailynews.com>, internet access: 03.12.2011

³⁸² ECO focuses on Afghanistan, *Hürriyet Daily News*, 15.10.2002, <http://www.hurriyetdailynews.com>, internet access: 03.12.2011.

and thoroughly affected the bilateral trade and led to a substantial increase in both exports and imports in terms of value, volume, diversity and share. Despite remained minimal when compared with the Europe or GCC, FDI investments inflows to Turkey and outflows to Iran increased during the period. During the 2000s, economic relations between Turkey and Iran not only increased but also deepened *vis-à-vis* the 1990s. Thus a more profound interdependence has created between the parties. However, Turkey's heavy reliance on Iran in terms of crude oil and natural gas has turned the scale in favor of Iran and unfortunately Turkey could not achieve to create such a dependence in its favor but this is a bit normal since Iran is an energy-rich country and one of the biggest energy suppliers of the world. In this context, thanks to its geopolitical position, Turkey tried to become an energy hub and act like a synapse for Iran to transmit two of its major export products, crude oil and natural gas which are vital not only for Iran but also for Turkey and Europe as well. In addition, increasing level of Iran's isolation compelled Iran to approximate and engage with Turkey. As a result, by this way, Turkey has achieved another kind of a dependence in its favor, although to a lesser extent when compared to Iran.

The expansion of bilateral economic relations between Turkey and Iran has been nourished via two main arteries during the 2000s. First artery is the transformation in foreign policy of Turkey and the other one is the changing structure of the Turkish economy and its socio-political repercussions. But both of them has been signaling the rise of the "trading state". During the decade, the degradation of the levels of national security alert *vis-à-vis* the 1990s paved the way for a revival of the process of becoming a "trading state" which was originally started in the 1980s but largely suspended during the 1990s. As Kirişçi indicated, by the 2000s the balance between the politics and the economics once more began to change, as policies much more closely associated with a trading state began to make a comeback and started to transform traditional foreign policy determinants and makers as well.³⁸³

³⁸³ Kirişçi, "The Transformation of Turkish Foreign Policy: The Rise of the Trading State," p. 45.

Transformation of domestic economy along with the tectonic shifts in the global trade and investment patterns, increasing influence of exporters in the decision-making process through the business associations, the rise of the economic and trade diplomacy, the “new” Turkish foreign policy approach introduced by Ahmet Davutoğlu, initiation of the “zero problems with neighbors” policy in line with this new approach, resultant “zero problems, limitless trade with neighbors” policy, in foreign trade have all encouraged deeper bilateral (commercial) relations and interdependence with neighboring Iran and prioritizes dialogue and cooperation via creating an atmosphere more conducive for trade.

CHAPTER 5

CONCLUSION

The long history of Turkish-Iranian political and economic relations has been full of ups and downs. From the beginning, the pendulum has swung between cooperation and competition and none of them managed to dominate the course of relations on its own, rather there have been aspects of both cooperation and competition at the same time. In addition, it is seen that there has been a strong correlation between political and economic relations in general. This study found out that, for the most part of the history, political considerations have predominated over economic considerations and determined the course of Turkish-Iranian relations. However, this structure has begun to transform in the 1980s, immediately after the declaration of January 24 Decisions and the adoption of the export-oriented economy policies. In the 1990s, as a result of the escalation of security concerns, threat perceptions and strained political conditions, the process of becoming a “trading state” is interrupted for a while. Nevertheless, the “trading state” has made a stronger comeback in the 2000s. Contrary to the 1990s, Turkey’s lessened preoccupation with issues of survival and territorial integrity facilitated the rise of the “trading state” in the 2000s. Therefore, the course of Turkish-Iranian relations is largely determined by economic considerations which reached unprecedented levels in the last decade.

This study argued that, from the establishment of the Turkish Republic in 1923 to the 1980s, the role of foreign trade in determining the course of bilateral relations remained minimal. Indeed, throughout the first 60 years of the Republic, Turkey’s foreign trade relations with Iran has been very limited in itself and Iran’s share in Turkey’s foreign trade did not show an impressive outlook at all. During the 1923-1979 period, Iran’s average share in Turkey’s total exports and imports were 0.4% and 0.8% respectively. Until the 1980s, political relations between these countries have been relatively good in general despite some problems like the border issue, the Kurdish problem and regional competition. Although the “traditional friendship” between Turkey and Iran has been frequently emphasized by the parties,

this friendship was far from a multi-dimensional and robust partnership which was based on long term common interests, goals and mutual interdependence. During these years, the profiting party of the bilateral trade was Iran to a great extent and foreign trade could not be relieved from its unbalanced structure which was in favor of Iran, mainly due to crude oil. Nevertheless, when the diversification of export products is considered, it has been clear that the advantageous party was not Iran. Because, almost all of the imports from Iran have consisted of one single item, crude oil, and Iran could not manage to sell almost anything to Turkey other than the “black gold”. On the contrary, Turkey has diversified its exports to Iran in parallel with its domestic economic transformation. In this context, Turkey which had exported some basic agricultural products to Iran initially, enriched its agricultural products exports to Iran. Furthermore, as a result of the ISI policies and rising industrial production, the share of manufactured goods in Turkey’s exports to Iran started to increase. However, owing to the industrialization, Turkey’s energy need and hence crude oil imports from Iran have also accelerated. Therefore, the rise and diversification in exports to Iran has fallen short of narrowing the foreign trade deficit and rising global oil prices further deteriorated the situation for Turkey. Although the 1970s, it is possible to see a growing willingness on the side of Turkish businessmen to increase trade relations with Iran, mainly in order to benefit from Iran’s rising oil revenues, this has remained unfulfilled action.

By the late 1970s, both of the countries got tied up with internal political, social and economic problems which have culminated in the Islamic revolution in Iran in 1979 and the coup d’état in Turkey in 1980. These developments presented the two major challenges to the stability of Turkish-Iranian foreign (trade) relations. However, contrary to expectations, bilateral relations, especially trade relations between Turkey and Iran developed from then on. But it is important to emphasize that, neither the revolution nor the coup d’état was the real reason behind this development. As the study argued, Turkish-Iranian foreign (trade) relations rapidly developed with the ignition of the January 24 Decisions and export-led growth strategy adopted through it, Iran-Iraq War and the facilitation of the new leadership

headed by Özal, which all culminated in the process that started Turkey's journey towards becoming a trading state.

With January 24 Decisions, Turkey abruptly abandoned the ISI policies and started to integrate into the world economy via export oriented economic policies. As a result of the economic liberalization, the significance and magnitude of foreign trade substantially increased. Moreover, this also became a period when both newly emerging actors, mainly the exporters who benefited from the new economy policies, have increased their influence in foreign policy making. In other words, Turkey has begun to transform into a "trading state" in the 1980s. As the study showed, the more foreign trade increased, the more it determined the course of economy and the more it determined the course of economy, the more it determined not only the domestic, but also the foreign policy. Furthermore, despite the political incompatibilities and tensions, economic issues and interests were given prominence throughout the period and the emergence of political problems was delayed for some time between Turkey and Iran.

This shift compelled Turkey to find new markets for selling its goods. In such an environment, Iran-Iraq War turned to a golden opportunity for Turkey to increase its exports and to achieve the objectives of export-led growth. The pragmatist elite of Turkey did not miss this opportunity and Turkey became the major trading partner of both warring countries. Thereby, Iran increasingly turned to Turkey to take a breath and satisfy its import needs through its oil incomes. As a result, Turkey's exports to and imports from Iran rapidly increased in the 1980s and accordingly, Iran's share in Turkey's foreign trade showed an impressive development and has substantially increased.

In this context, official visits between Iran and Turkey increased during the 1980s. The willingness of conducting foreign trade relations under an institutional framework brought the two parties to establish Turkish-Iranian Joint Economic Commission where they met every year, within the scope of improving economic cooperation in the fields of trade, banking, investments, transportation, industry and agriculture, etc. and several memorandum of understandings were signed, whose the objectives could not be achieved totally. It is important to note that, Turkish

exporters started to be represented institutionally by DEİK in the JEC meetings. This is an important reflection of becoming a “trading state” and the rising influence of businessmen and their organizations.

Nevertheless, this positive atmosphere in bilateral trade did not last long and security and political problems began to adversely affect the economic relations by the mid-1980s. On the one hand, Islamic Revolution and 1980 coup d'état, constituted a stress point in relations. Thus, ideological and political incompatibility between Iran and Turkey negatively affected the economic relations despite counter efforts. On the other hand, the emergence of the PKK issue and mounting terrorist attacks in Turkey posed serious political problems between Turkey and Iran. Moreover, Iran increasingly complained about the low quality and expensiveness of Turkish products. In addition, the transformation of the Regional Cooperation for Development (RCD) to Economic Cooperation Organization (ECO) in 1985 did not meet expectations in of progress and the commitment to lift the customs tariffs and other barriers to trade were not materialized.

As the Iran-Iraq War was coming to an end and as the mutual interdependence between the parties diminished, the economic and commercial relations between Turkey and Iran started to degrade. At the same time, political disagreements which were not spoken out due to heavy interdependence during the War began to be heard more often. As the political problems came to light, tension between the two countries has escalated and these tensions adversely affected the economic relations. In parallel with these developments, volume of bilateral trade began to shrink towards the end of period. Because, during the period mutual interdependence between Turkey and Iran could not be created. In order to increase exports, a short term perspective was adopted and the medium and long term perspectives were neglected. In addition, fundamental political and ideological differences between the parties were underestimated. Even sometimes, on behalf of increasing exports, important political concessions were given or the important political problems were ignored and were not brought up. However, this attitude proved to be unsustainable. As the political problems become serious and non-negligible together with the disappearance of favorable and compelling conditions

which was created by the War, not only political but also economic relations started to deteriorate.

By the 1990s, the pragmatism and optimism of the 1980s faded away. Political, ideological and security problems together with rivalry have put additional burden on bilateral relations, thus Turkey and Iran had difficulties in finding common grounds to cooperate. Under these compelling circumstances “trading state” yielded in favor of the “military-political state”. Unlike the 1980s, the main parameters that have been decisive on Turkish-Iranian relations have been mainly political in nature rather than economic in the 1990s. The course of foreign trade between Turkey and Iran did not constitute an exception in that sense and political issues have been decisive on trade relations.

In this new chaotic era, the shifts in international, regional and domestic systems had profoundly affected the relations between Turkey and Iran. On the one hand, the end of bipolarity, the collapse of the Soviet Union and the emergence of new states in the Central Asia and Caucasus added new variables and unknowns to the equation of Turkish-Iranian relations. This new geopolitics of Turkey and Iran drove them into a fierce competition and a limited cooperation. On the other hand, Middle Eastern sub-system slid into chaos with the Gulf War which wrecked the balance of power in the region. In addition, the Kurdish question and intensification of the PKK terrorism poisoned the relations. Within this environment, Turkey’s growing ties with Israel and deterioration of its relations with Syria - ally of Iran - further alienated the two countries. In bilateral relations, together with these changing parameters, ideological controversy between the secular Turkey and the theocratic Iran, the rise of political Islam and Islamic capital in Turkey, mutual distrust between the two countries, counter-statements and fierce criticisms, assassination of some prominent Turkish intellectuals where Iran was considered to have a role, support for the Iranian opposition groups and the use of PKK as a trump card all strained not only political but also economic relations.

In the 1990s, all of these political developments posed a huge obstacle for the expansion of bilateral trade relations. As the “high politics” occupied the top of the agendas of Turkey and Iran, “low politics” and thus economic and commercial

interests were overlooked to some degree. Under these conditions, the strengthening and deepening of commercial relations could not be achieved, bilateral trade relations between Turkey and Iran rapidly deteriorated and Iran's share in Turkey's overall foreign trade diminished despite the willingness of some business circles, especially the rising pro-Islamist businessmen, especially the Anatolian Tigers and MÜSİAD. In other words, deterioration of political relations did not mean that no effort was made to develop economic relations, but under such harsh political conditions, it was not easy to advocate the economic interests. In addition, the lack of a clear and constant political will towards improving economic relations negatively affected the progress of trade. In fact, it was impossible to cut off trade relations altogether since the parties continued to be economically interdependent to some degree. Turkey was dependent on Iran as it was in dire need of new markets to sell its products and needed to import energy which was vital for its economy. On the other hand, Iran was dependent on Turkey to reach both Turkish and more importantly, European markets to sell its crude oil and natural gas in return for the required capital, intermediary and consumer goods. In this context, signing of agreements concerning the supply of natural gas and the construction of a pipeline between Turkey and Iran, constituted the most important and long-lasting developments of the 1990s. ECO, D-8 and border trade were the other issues on the bilateral trade agenda of Turkey and Iran.

In sum, during the 1990s political tensions and security concerns negatively and profoundly affected the bilateral trade and paved the way for a substantial and mutual decline in foreign trade by means of value, volume, diversity and share. Since the process of becoming a "trading state" was interrupted by the preponderance of ideology with military-political and territorial considerations, foreign (trade) relations between Turkey and Iran deteriorated. However, as the study confirmed, the economic interdependency between these neighbors, notably the continued reliance of Turkey on Iranian crude oil, the deep-rooted and already continuing commercial attachments and finally the lobbying of both the traditional but mostly the newly emerging business circles in Turkey and Iran, prevented the bilateral trade from a

further decline and ensured the continuity of minimal pragmatism in commercial relations which kept the foreign trade alive.

However, by the late 1990s the degree of tension started to decline and as of 2000 cursors slowly shifted to the direction of economy and trade again. Thus, by the late 1990s but especially by the 2000s the balance began to change once again and as policies much more closely associated with a “trading state” began to make a comeback and started to transform determinants and makers of the foreign trade relations between Turkey and Iran. In other words, the shift in bilateral political and economic relations has mainly stemmed from, *inter alia*, the transformation of the Turkish foreign policy and the rise of the “trading state”. Therefore, economic considerations such as foreign trade, investment opportunities and energy supplies have begun to re-shape the course of foreign (trade) policy towards Iran during the 2000s. Thus, Turkey has abandoned its remote stance towards Iran in favor of an unprecedented level of political and economic engagement and Turkish-Iranian relations have started to improve again in the 2000s.

In the course of the 2000s, fundamental parameters of Turkish-Iranian relations profoundly changed and created an environment conducive to advance relations on the basis of foreign trade. First of all, the shift in the global system from a unipolar to a multipolar world and the increasing pace of globalization facilitated the rise of the “trading state”. At the regional level, the strategic environment in which Turkish-Iranian relations was shaped changed profoundly. The US invasion of Iraq has upset all the balances and brought Turkey and Iran closer. At the domestic level, since the AKP’s rise to power, Turkey’s domestic and foreign politics has undergone a sea change. The new leadership set about altering the character of the Turkish state in a manner that diminished the role of military-bureaucratic elite as well as the ideological differences between Turkey and Iran within the scope of “zero problem, limitless trade with neighbors” strategy, advocated by Ahmet Davutoğlu.

In this framework, the number and substance of actors in domestic and foreign policy increased and changed substantially. During the 2000s, subsequent AKP governments have used greater volumes of trade, especially exports and investments as instruments of its foreign policy towards Iran. As a natural result,

exporters and industrialists emerged as the partners of the AKP governments. In harmony with its economic mentality, the AKP has come closer to the private sector than any government before and in return it has been staunchly supported by large segments of the private sector. In this context, the AKP governments have closely cooperated with business associations such as TİM, TOBB, DEİK, MÜSİAD, TUSKON and ASKON which have constituted a crucial part of the AKP's electorate. Relations with TUSİAD have been more limited. Since, the support of the numerous SMEs (small and medium enterprises) which spread country-wide, were important especially for elections, the AKP has focused on the demands of this group. So to say, in the 2000s business associations started to function as foreign policy actors and their role in the foreign policy making substantially increased under the leadership of the AKP. In Kutlay's words, Turkish businessmen have turned into one of the "practical hands" of Turkish diplomacy in the course of the 2000s.

As the thesis argued, in parallel with these developments, this period has witnessed the revival of pragmatism and the relative retreat of ideology in Turkish foreign policy towards Iran and this new mentality has profoundly and positively affected Turkish-Iranian relations. Furthermore, Turkey's deteriorating relations with Israel and limitations on its relations with the US, developing relations with Middle Eastern countries and AKP's pro-Islamic discourse has been welcomed by Iran and generated a positive atmosphere in which Turkey and Iran began to cooperate closer. In this context, cooperation between Turkey and Iran gained momentum in the areas such as the security, energy and the nuclear issue. As a result the number and intensity of bilateral dialogue and cooperation mechanisms such as reciprocal visits, meetings, conferences and fairs increased substantially. In this context, Turkey-Iran High Security Commission and Joint Economic Commission meetings and fairs constituted main mechanisms that brought Turkey and Iran together. This high level of interaction in different areas from politics to economics positively affected Turkish-Iranian relations and facilitated the rise of bilateral trade relations and *vice versa*.

As a result, the recently improved and stabilized political atmosphere and lessened security concerns between Turkey and Iran has culminated in more foreign trade. However this does not mean that bilateral economic relations are free from challenge or competition. Turkey's exports to Iran increased by 13 times and imports from Iran soared by 9 times during the 2000s. As a result, volume of bilateral trade increased by 10 times and exceeded the \$10 billion. However, as a chronic disease, the gap between imports and exports widened to the detriment of Turkey during the 2000s. In other words, Turkey's asymmetric dependence on Iran has been increased throughout the decade. Moreover, the large part of this growth has been realized by the booming crude oil and natural gas imports from Iran. Thus, Turkey's dependence on Iran has increased as a result of growing energy imports.

This dependence has not been able to transform into interdependence, on the grounds of reciprocity or win-win principles. In other words, by exporting large amounts of crude oil and natural gas to Turkey, Iran has gained a strategic advantage, a powerful leverage and thus an important bargaining power in bilateral relations. To a lesser extent, Turkey tried to overcome this dependency by using its geopolitical position suitable for becoming an energy hub between Iran and Europe, but the results of this is still yet to be seen.

In conclusion, although the relations between Turkey and Iran advanced almost in all aspects in the 2000s, they are not free from obstacles. Changing balance of power, the future of the nuclear issue, escalating tensions between Iran and the West and dubious future of the Middle East constitute main stress points in the Turkish-Iranian relations. And it is not clear whether the rise of the "trading state" and economy-driven foreign (trade) strategies towards Iran are sustainable and will grow strong enough to overcome the possible obstacles in the future. In this context, analyzing bilateral relations between Turkey and Iran from an Iranian perspective will complement this thesis and shed light on the future of the Turkish-Iranian relations.

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APPENDICES

Appendix A:

TEZ FOTOKOPİSİ İZİN FORMU

ENSTİTÜ

Fen Bilimleri Enstitüsü

☐

Sosyal Bilimler Enstitüsü

☒

Uygulamalı Matematik Enstitüsü

☐

Enformatik Enstitüsü

☐

Deniz Bilimleri Enstitüsü

☐

YAZARIN

Soyadı : Eruysal

Adı : Esra

Bölümü : Orta Doğu Araştırmaları

TEZİN ADI (İngilizce) : Economic Relations between Turkey and Iran from 1990 to 2010: A Turkish Perspective

TEZİN TÜRÜ : Yüksek Lisans

☒

Doktora

☐

1. Tezimin tamamından kaynak gösterilmek şartıyla fotokopi alınabilir.

☒

2. Tezimin içindekiler sayfası, özet, indeks sayfalarından ve/veya bir bölümünden kaynak gösterilmek şartıyla fotokopi alınabilir.

☐

3. Tezimden bir bir (1) yıl süreyle fotokopi alınamaz.

☐

TEZİN KÜTÜPHANEYE TESLİM TARİHİ: