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## **Turkey Lashing Out**

Here at Confluence, we write a lot about the rise and fall of hegemonic states – those great nations that develop enough power and influence to dominate the global economy, or at least some region of it. These superpowers use their extraordinary military might and other levers to impose order on their sphere of influence, providing the security necessary for international trade. They also provide the reserve currency that acts as a common medium of exchange for that trade. These hegemonies therefore provide the foundation on which a global or regional economy can function.

During the Cold War, the United States accepted leadership of the Free World and acted as hegemon for the non-communist bloc. After the disintegration of the Soviet Union and the demise of Soviet-style communism in 1991, the United States became a global hegemon. What is now less appreciated is that the burdens of hegemony and the demise of Soviet communism have eroded the willingness of U.S. citizens to maintain their country's leading role in the world. At the same time, the removal of the Soviet threat has encouraged other nations to once again assert their own interests and the freedom of action they sacrificed to come under U.S. protection during the Cold War. This week's report looks at one of the best examples of that dynamic, the recent discord between Turkey and the United States, which has culminated in Turkey's defiant purchase of a Russian air-defense system. We will review Turkey's political dynamics

and why its president, Recep Erdogan, has implemented a more assertive foreign policy that is putting the country at odds with the United States and the West, in general. As always, we conclude with a discussion of the resulting market implications.

### **From Kemalist to Islamist**

Modern-day Turkey arose from the ashes of the Ottoman Empire following the end of World War I. After the war, the victorious Allies tried to prevent the resurrection of the empire by occupying parts of its territory and giving autonomy to regional groups like the Greeks, the Kurds, and the Armenians. However, a group of Turkish military officers led by Mustafa Kemal Ataturk overthrew the Allies' puppet monarch in 1922 and pushed the occupying forces out, eventually creating the nation of Turkey.

What distinguished Turkey for most of its first century was a specific political culture developed by Ataturk to strengthen and modernize the country by moving it beyond its roots as an Islamic monarchy. Ataturk's "Kemalism" centered on two primary concepts, both of which were aimed at emulating the successful countries of Europe. First, the government embraced republicanism and democracy. Second, it enforced secularism and deliberately suppressed any attempt to bring Islamic influences into society. The secularist thrust of Kemalism was applied even in the conservative, Islamic-dominated hinterlands of the Anatolian peninsula, which gradually generated simmering discontent. The government and military also harshly suppressed minorities in those areas, with a particular focus on the Kurdish people

whose historic homeland straddles the Turkish-Iraqi frontier. By the late 1970s, repression of the Kurds spawned a radical, left-wing separatist movement known as the Kurdistan Workers' Party (PKK). The PKK's goals have vacillated from the establishment of an independent Kurdish state to simply achieving equal rights and autonomy for the Kurds within Turkey. However, the PKK has often used terrorist methods, so it is seen as an existential threat to the government in Ankara.

During the Kemalist period, the government's Westernization efforts included a program of industrialization, but economic performance was generally unimpressive and often erratic. Turkey's per-capita gross domestic product (GDP) grew at a modest average annual rate of just 1.1% in those years, and inflation often surpassed 75%. To improve economic prospects, Turkey and the European Union (EU) signed a cooperation agreement in 1963 and a limited customs union in 1995. Turkey applied for full admission into the EU in 1987, but EU leaders have continually blocked action on the application on the grounds that Turkish human rights violations and weak rule of law would be incompatible with EU norms. Turkey's frustration over its lack of access to the European market has been an important factor in turning public opinion away from the West.

International security policy also became a source of Turkish frustration in the Kemalist period. As shown in Figure 1 below, Turkey's geographical position separating the southwest flank of the Soviet Union from the oil fields of the Middle East made it supremely vulnerable to Soviet incursion, while its control of the Bosphorous Straits put it into position to bottle up the Soviet Navy in the Black Sea. Turkey was

therefore highly valuable to the North Atlantic Treaty Organization (NATO), and it was admitted to the alliance in 1952. Turkey spent decades as a linchpin of Western security. After the fall of the Soviet Union, however, Turkey became much less valued by Western allies. Even as it loyally supported the First Gulf War in 1991 (which further irritated the country's restive Islamists), the government chafed at its loss of status in global affairs.

**Figure 1.**



*Source: Canadian Broadcasting Corp.*

### **Enter Erdogan**

Disillusion with the West, economic underperformance, and the rise of Islamism finally brought anti-Kemalists to power in 2002, but the transition itself further delegitimized the Kemalist elites and Turkey's supposed Western allies. In that year's elections, Recep Tayyip Erdogan and his Justice and Development Party (AKP) won a sweeping mandate for their proposed program of nationalism and increased respect for Islam. However, Turkey's electoral authorities initially prevented Erdogan from taking power on the grounds that he had publicly read a prohibited "Islamic" poem eight years earlier. The ban was reversed in 2003, allowing Erdogan to take power, but the damage was done. The episode further eroded public support for the Kemalist elites and the Western governments that did little to support Erdogan in his post-election legal battle. Disillusionment with the West grew even

more as the United States and its allies enlisted the help of Kurdish forces against Iraq in the Second Gulf War in 2003.

### **New Frustrations**

The discussion above shows that many in the Turkish electorate were already disillusioned with the West and its values prior to Erdogan's ascension to power. Indeed, dissatisfaction with the status quo is what helped make Erdogan's program so appealing. Since coming to power, however, Erdogan and the Turks have faced a range of new frustrations with the West that have made them more interested in finding new allies, culminating in Turkey's purchase this month of a new air-defense system from Russia. Those new frustrations have included the following:

***Failure of the Arab Spring.*** The anti-government protests and uprisings that spread throughout the Arab world in the early 2010s (the "Arab Spring") initially seemed to herald an Islamist awakening like Erdogan was promoting in Turkey, but he and much of Turkish society came to see Western support for the Islamist protestors to be insufficient. That was especially the case as the uprisings in Libya, Egypt, Syria, and other countries petered out or were suppressed. The case of Egypt was especially galling since the popularly elected government of President Mohamed Morsi and his Muslim Brotherhood were toppled in a July 2013 coup with little U.S. or Western complaint. At almost the same time, the Western media strongly criticized what they saw as Erdogan's increasing authoritarianism. The Western media criticism reached a fever pitch after Erdogan's heavy-handed dispersal of Turkish protestors trying to stop one of his signature construction projects in Istanbul's Gezi Park. Not only did Erdogan interpret the lack of U.S. or Western support for

Morsi as a betrayal, but the complaints about his handling of the Gezi protests were interpreted as outright hypocrisy.

***Syrian Civil War.*** As the civil war in neighboring Syria intensified in 2014, the Turkish government saw its interests best served in supporting radical Al Qaeda-linked Islamist groups as they battled both the forces of President Bashir Al Assad and the Syrian-based Kurds. In contrast, the U.S. government chose to support the Kurds. Given the Turkish government's view that the PKK constitutes a mortal threat, the U.S. stance has been a growing irritant up to the present. In fact, the dispute over the PKK in Syria nearly produced a U.S.-Turkish military confrontation in early 2018 when Turkish forces launched an operation against Kurdish forces in the Syrian enclave of Afrin. While Russia offered its encouragement for the Turkish attack, the U.S. government forced Turkey into a humiliating backdown.

***Failed Coup and Break with Gulen.*** As bad as those events were for U.S.-Turkish relations, they paled in comparison to the failed coup attempt against Erdogan in the summer of 2016. One irritant was that Erdogan simply didn't think the U.S. government supported him enough in his hour of need. Erdogan has also chafed against U.S. criticism of his post-coup roundup of political opponents and his effort to get his hands on a moderate Islamist religious leader named Fethullah Gulen, who has been living in self-imposed exile in Pennsylvania since 1999. Gulen had provided important political support to Erdogan during his rise to prominence, but just as Western opinion turned against Erdogan following the Gezi protests, Gulen also became critical and publicly broke with him. Erdogan, along with many other Turks, saw a conspiratorial link between the

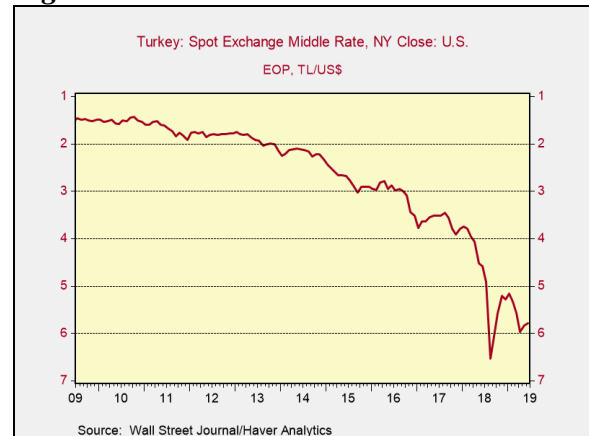
Western criticism and Gulen’s actions. Convinced that Gulen masterminded the coup, Erdogan has demanded his extradition, but the U.S. has consistently rejected the request on grounds of insufficient evidence.

**Imposition of Steel Tariffs.** Although the irritants listed above are mostly political, there have also been economic disputes between Turkey and the West. In 2018, a major point of contention was the U.S. imposition of punitive import tariffs on Turkish steel imports. The U.S. tariffs of 25% were imposed on various countries on the grounds that their exports of steel and aluminum were a threat to U.S. national security. However, when Erdogan’s post-coup roundup of political opponents ensnared a U.S. missionary named Andrew Brunson, President Trump doubled the tariffs to 50% for Turkey, helping push its steel exports to the U.S. down by almost 40% in 2018. Given that Erdogan’s economic policy had long centered on investment fueled by foreign borrowing, the Turkish economy was already fragile. The new U.S. tariffs helped spark a sharp crisis. Investors stampeded out of Turkish assets, and its currency, the lira, plunged (see Figure 2). The U.S. tariffs were cut back down to 25% after Brunson’s release in May 2019, but even at that level the duties remain a significant sore point for Erdogan. Further adding to Erdogan’s frustrations, the Trump administration also removed Turkey from a special program offering preferential benefits for certain developing countries.

**Cypriot Gas Drilling.** The island nation of Cyprus has been a flashpoint for Turkey since 1974, when Turkish forces invaded to protect its ethnically Turkish community after a coup aimed at unification with Greece. Although the northern half of the island remains under Turkish control,

Cyprus officially joined the European Union in 2004. In the latest source of tensions, the Cypriot government in recent years has allowed international energy firms to explore for natural gas in the waters around the island, ignoring Turkey’s demand that such exploration be prohibited until the island is united and resources can be shared fairly. To underscore the point, Ankara has sent Turkish drilling ships to explore in Cypriot waters, drawing EU sanctions and a rebuke from the United States.

Figure 2.



**Turkey’s Pushback**

From the discussion above, it should be clear that Erdogan and his government see plenty of reasons to be irritated with the U.S., and, more broadly, with the West. What’s significant is that the Turks have pushed back against those irritants much more forcefully than they would have during the peak of U.S. hegemony during the Cold War and immediately after. The Turks have been actively taking steps to signal their displeasure, thumb their noses at the West, and build new alliances with other strategic partners. The arrest of Pastor Brunson was widely seen as revenge against the U.S. for its lukewarm support during the coup, and as an effort to gain a bargaining chip for the extradition of Fethullah Gulen from Pennsylvania. Erdogan has also become a [stalwart supporter of embattled Venezuelan](#)



[strongman Nicolás Maduro](#), publicly urging him to “stand up tall” against U.S. efforts to force him from power. Turkey reportedly imported nearly \$1 billion in gold from Venezuela in 2018, providing Venezuela with a significant amount of hard currency as it struggles against its sliding oil output and U.S. sanctions.

The most dramatic example of Turkey’s pushback against the U.S. and the West is its decision to buy and deploy Russia’s advanced S-400 air defense system, the [first shipments of which arrived in Turkey during July](#). The Turkish purchase came after the Obama administration denied Ankara’s request to buy an advanced U.S. system – the Patriot – mostly because of Turkey’s demand that the deal include joint production and development of the system. Politically, Turkey’s purchase of the S-400 from a mortal enemy of the West is a body blow to NATO’s cohesion. Just as important, U.S. officials fear the S-400 equipment could [give the Russians insight into the capabilities of the F-35](#), the next-generation stealth fighter that is being sold to dozens of U.S. allies and is due to be a backbone of Western defense in the years to come (see Figure 3). Turkey has already made a down payment of more than \$1 billion for a fleet of F-35s, and it has taken delivery of several units. It has also sent pilots to train on the jet at Luke Air Force Base in Arizona. It had even secured a deal in which Turkish firms were supplying some 6% of the value of each jet. In response to the S-400 purchase, however, the Trump administration has [halted any further sales of the F-35 to Turkey and is ending the Turkish firms’ participation](#) in the program.

As mentioned above, we take an even broader view of the evolving rupture between Turkey and the U.S. and its allies. We think this rupture is perhaps the best

current example of what happens when a global hegemon begins to lose influence around the world. Sometimes, that influence begins to erode because the global or regional environment becomes less threatening. For example, Turkey has become much less reliant on the U.S. and NATO security umbrellas since the disintegration of the Soviet Union and its replacement with a Russian government that is relatively less threatening and more pragmatic. At other times, the hegemon loses influence when its people tire of bearing the costs of global leadership. This “hegemonic fatigue,” as interpreted and channeled by the Trump administration, is ultimately why the U.S. imposed its protectionist import tariffs against Turkish steel in 2018. Finally, the hegemon’s ability to influence other countries can erode when its long dominance breeds a certain hubris and it begins to ride a bit too roughshod over its partners’ interests, especially when it is simultaneously pulling back on the benefits it provides. For Erdogan and his Islamist supporters, we suspect they see precisely that kind of infuriating insensitivity and duplicity in the U.S. partnership with Kurdish fighters in Syria and Iraq and its refusal to extradite Gulen.

**Figure 3.**



*F-35 performing inverted fire test.  
(Source: Lockheed Martin Corp.)*

**Ramifications**

For Turkish assets, Erdogan's decision to accept the Russian S-400 system and otherwise de-align with the U.S. and the West will probably not have a major immediate impact. However, we think Turkey's growing estrangement from its allies will exacerbate the headwinds arising from Erdogan's mismanagement of the economy over time. Erdogan's economic strategy has been to boost growth through massive real estate investment fueled by foreign borrowing. The policy has left Turkish firms saddled with a huge amount of dollar-denominated debt, sparking the plunge in the lira last year after the U.S.-imposed steel tariffs. Inflation and unemployment have skyrocketed, but rather than imposing financial discipline the Erdogan administration is trying to right the ship using unorthodox measures like price controls and [pressure on the central bank to lower interest rates](#). Those developments would be negative enough for Turkey's stocks, bonds, and currency. Increasingly acrimonious ties with the U.S. and Europe will further sour investor sentiment toward Turkish assets, especially if Erdogan decides to precipitate a new immigration crisis in

Europe by allowing free passage to Syrian refugees through Turkish territory.

More broadly, we think the gradual erosion of U.S. hegemony over the global economy will remain a cloud over a broad swath of assets. As the U.S. loses or deliberately rejects its influence over other countries, the world is likely to become a more chaotic place. International rivalries that were long submerged by U.S. power will likely surface once again, as they [already have between Japan and South Korea](#), and between Germany and many other EU nations. Just as troubling, global economic policies are likely to become less stable and predictable, perhaps extending to even further trade protectionism and currency wars. This isn't to say all assets will be challenged in the coming years. However, navigating within the new environment will probably require paying close attention to the evolving geopolitical and economic landscapes.

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