Director of Central Intelligence

(b)(3)

~~Top Secret~~

[redacted]

# National Intelligence Daily

*Monday*
*29 September 1980*

~~Top Secret~~

[redacted]

(b)(3)

*29 September 1980*

*Copy* 220

SPECIAL ANALYSIS

## TURKEY: Economic Outlook

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*Turkey's economic outlook should improve in the near term because of the military takeover but will continue to hinge on firm implementation of the stabilization program, backed by continued foreign aid. Even with tight adherence to such austere economic policies, however, Turkey will require at best two years before it can get by without emergency aid. The balance-of-payment deficit is too large to overcome quickly.* [redacted] (b)(3)

Soon after the coup, the military announced that Turkey would continue former Prime Minister Demirel's stabilization program and that Turkey would honor all its foreign economic commitments. The military leaders realize that the struggling economy is being kept afloat by foreign aid, much of which is contingent on Turkey's continuing to meet policy performance guidelines laid down by the International Monetary Fund. [redacted] (b)(3)

The new government probably will continue Demirel's key innovation of frequent small devaluations to maintain a competitive lira. In addition, Ankara has ordered striking workers back to their jobs and may implement by decree the tax reform that was bogged down in parliament. The military regime can put more pressure on state firms to become more self-sufficient through price increases and personnel reductions. [redacted] (b)(3)

### Demirel's Stabilization Program

The generals will carry out the conservative, market-oriented stabilization program more rigorously than Demirel was able to do. The program, which was introduced on 24 January, represented a sharp break with economic policy of recent years. [redacted] (b)(3)

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The centerpiece of the program was a major devaluation of the lira. Other important elements included a sharp cut in subsidies to State Economic Enterprises and a concomitant reduction of the overall budget deficit; removal of price and interest rate controls; slower monetary growth; increased export incentives; tax reform; and opening the economy to private foreign investment. [redacted] (b)(3)

Initial Encouraging Signs

The program evidently was beginning to work. Demirel's initial devaluation of the lira on 24 January was as large as the successful devaluation in 1970 and much larger than the failed devaluations in 1978 and 1979. [redacted] (b)(3)

The devaluation put the lira at an economically realistic level for the first time since the oil price hikes in 1973. Furthermore, that position has been maintained for the past six months by a series of small devaluations, something no previous government had been willing to do. [redacted] (b)(3)

The balance of payments has improved since the program began in January. Worker remittances rose sharply--up 98 percent comparing the six-month period following the devaluation with the previous six-month period--to an annual rate of $2 billion. [redacted] (b)(3)

Seasonally adjusted exports jumped 22 percent in value in the first quarter, compared to fourth quarter 1979. They rose an additional 14 percent during the second quarter to an annual rate of $2.6 billion. Imports declined 3 percent during the first quarter, then rose only 1 percent during the second to an annual rate of $5.5 billion. [redacted] (b)(3)

Shortages for the most part have been alleviated due to the sizable amounts of foreign aid and to higher prices bringing supply and demand back into balance. Government subsidies to State Economic Enterprises are lower and, as a result, the budget deficit has been reduced. [redacted] (b)(3)

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The stabilization program has had its most visible impact on the inflation rate. Immediately after its introduction, prices soared because controls were removed and state sector prices were increased to levels in line with costs. Since April both consumer and wholesale prices have been rising at annual rates of around 40 percent--about half the pace recorded during the latter part of 1979. [redacted] (b)(3)

The program has not done well in getting industrial production back on track largely because of tight credit and labor disruptions. The industrial slump, a rapidly growing labor force, and the pressure on state enterprises to lay off surplus workers means that unemployment will continue to increase in the short term. Officially the unemployment rate is now 15 percent; unofficial estimates place it at 20 to 25 percent. [redacted] (b)(3)

## Outlook

If the stabilization program is maintained, the economy should continue its slow improvement. The road ahead, however, is long and uncertain. Disruption of Iranian and Iraqi oil supplies--on which Turkey is heavily dependent--could nip economic recovery in the bud. [redacted] (b)(3)

Assuming the recovery program is not derailed by a cutoff of oil, Turkey still will need additional infusions of foreign aid next spring. Turkey has enough aid pledges to cover its financial gap in 1980, and donors apparently will honor their commitments. By about March, however, Turkey will need new aid pledges for 1981--particularly from the members of the Organization for Economic Cooperation and Development. [redacted] (b)(3)

Prospects for fresh inflows of private capital remain poor. Private banks will remain reluctant to grant new loans or to reschedule--for a second time--Turkey's outstanding debts. The banks already feel overextended in Turkey and two recent studies of international creditworthiness both ranked Ankara in the bottom 10 percent. [redacted] (b)(3)