

Chapter 61

Predicting Financial Crises in a Globalized World: The Case of the Turkish Banking Sector

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ABSTRACT

This chapter highlights the facts about financial crises and their fundamental causes on specific incidents, including the 1929 Great Depression that lasted until the early-1940s, 1997 Asian Financial Crises, 1998 Russian Financial Crises, and the Liquidity Crises of 2008, and makes a comparison among them and their various outcomes. In doing so, the study specifies the cues that emerge in the financial system that may help governments predict upcoming financial crises through those early warning signals. This case study specifically analyses the Turkish Banking System that was restructured after the enormous financial crises in Turkey in 2001, which caused many Turkish banks to collapse. However, the precautions taken in the aftermath of the financial turmoil allowed them to survive the liquidity crises in 2008. The indicators of an upcoming crisis are examined, the lessons learned from this case are analyzed, and important recommendations to overcome banking crises are provided.

INTRODUCTION

Globalization and deregulation processes worldwide accelerated the integration procedure of national and international financial markets, particularly after the 1990s. As a result of globalization, investment decisions and locations of investments have changed, and various countries' regulations influenced other countries. In some countries, authority over the financial markets has been lessened by eliminating regulations to ease transactions and thus improve the ease of doing business. On one hand, the liberalization of financial markets significantly increased the flow of the capital between countries. Yet, on the other hand, this tendency caused long term financial crises whose violence and scope are rapidly expanding. Financial crises take place in many different countries contagiously on a regular basis, and are triggered by continuously varying factors.

The term financial crisis is applied broadly to a variety of situations in which some financial institutions or financial assets suddenly lose a large part of their value. Many financial crises in the 19th and early 20th centuries were caused by panics pertaining to banks and banking systems (i.e., banking panics), which then ended with recession in the global economy (Brunnermeier, 2016). There are also other types of financial crises stemming from stock market crashes, bursting financial bubbles, currency crises and sovereign defaults. Many economists have offered theories about how financial crises develop and how they could be prevented. Yet there is little consensus, as to which theory holds true with reference to the development and prevention of financial crises. Financial crises are still a regular occurrence around the world, and continue to have negative impacts on the growth rates of the countries that encounter and have to deal with crises. The Great Depression between the late 1929s and the early 1940s, The Asian Financial Crises in 1997, the Russian Financial Crisis in 1998 and the Liquidity Crisis of 2008 are examples of crises that have affected the growth of the major economies (Castiglionesi & Lorenzoni, 2017).

GLOBALIZATION AND FINANCIAL CRISES

Globalization is accepted as a process that removes geographical boundaries and enables the economic integration and interdependence of national economies into the international economy through trade, foreign direct investments, capital flows and migration. Globalization initiates the widening of international trade, transformation of financial sources, increasing foreign investment and joint enterprises, generating interdependency. Today, countries become dependent on each other economically due to technological advancement, digitalization, and easy and fast communication. Since the 1990s, financial globalization removed boundaries, opened up financial markets to international competition, and increased international capital flows. Yet, the increase in the short-term capital movements as an inevitable result of globalization increased the volumes of financial crises.

Economic crises are unexpected, powerful, and sudden events that can have serious implications, which may arise with consequences, seriously affecting a country's macro economy and the firms in the micro economy (Aktan & Huseyin, 2001). The United Kingdom's Department for Business, Enterprise and Regulatory Reform (2008) describes a crisis as "*an abnormal situation, or even perception, which is beyond the scope of everyday business, and which threatens the operation, safety, and reputation of an organization.*" A crisis is a major, unpredictable event that threatens an organization and its stakeholders. Although crises are unpredictable, they are not unexpected.

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