

# THE ECONOMICS OF TURKEY-RUSSIA RELATIONS

Soli Özel | Academic Director

Gökçe Uçar | Secretary General

*I would like to note that Russia and Turkey are key partners in trade and investment. Last year, bilateral trade increased by 16 percent, reaching \$25.5 billion. We have achieved good results in agriculture. In 2018, trade in this sector was up 7 percent, reaching \$3 billion. Mutual investment stands at about \$20 billion...the Russian Direct Investment Fund will sign an agreement with the Turkish sovereign wealth fund on creating a joint investment platform of \$1 billion to be invested in promising sectors of the two countries' economies.*

**Vladimir Putin,**

High Level Russian-Turkish Cooperation meeting,  
8 April 2019, Moscow

*Ever since the 1990s, economic and trade relations have become the driver behind Russia-Turkey relations. Today, we have discussed trade, economic and cultural relations, as well as our contacts in all other areas at the delegation level. My dear friend and I have already set a target benchmark of \$100 billion, and so we need to find new approaches... Together we have broken ground on the Akkuyu nuclear power plant, and completed construction of the offshore section of the TurkStream gas pipeline... This year, we mark the Year of Culture and Tourism...*

**Recep Tayyip Erdoğan,**

High Level Russian-Turkish Cooperation meeting,  
8 April 2019, Moscow

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The Turkish-Russian relationship has improved considerably since a period of tensions and near proxy-war in Syria after Turkey downed a Russian SU-24 bomber in November 2015. Turkey's deal to purchase the Russian S-400, a long-range air and missile defense system can be regarded as the latest big strategic/military *cum* economic activity since the attack. This rapprochement was followed by the completion of talks on two infrastructure projects in the energy sector – the Turk Stream pipeline and a Russian-built, owned and operated nuclear reactor in southern Turkey. The post-jet crisis period during which Russia stood by the Turkish President during a botched coup attempt in July of 2016; the Russian ambassador in Ankara was murdered in plain sight of exhibition visitors and Iran-Russia-Turkey initiated the Astana Process to bring stability in Syria the total volume of trade in commodities between the two countries has significantly increased. Russian tourist arrivals in Turkey has returned to their pre-crisis levels. The two countries' reaffirmed desire to expand their bilateral economic engagements particularly in the defense sector have raised concerns in the West.

To assess whether Russia can be an alternative major trade partner for Turkey amid Turkey's strained relations with the West, this paper seeks to identify the drivers of Turkey and Russia's economic relations in the context of their historical trajectory. We will look to the developments and diversification of trade, energy, tourism and foreign direct investment flows and the evolution of the economic strategies of both partners.

Most analyses about Russia-Turkey relations focus on the historical strategic dimension. Both countries are legatees of now defunct empires that were once each other's nemeses. Their mutual perceptions have been shaped by the wars they fought against one another for centuries. In the last two hundred years of their rivalry the Russian Empire expanded at the expense of the Ottoman one. The period following the Revolution and the Bolshevik takeover in Russia and the launching of the Independence War by the Ankara National

Assembly Government in Turkey changed the nature of their interactions. The two new and fragile regimes recognized their counterpart's usefulness for their own prospects and throughout the inter-war period, remained in solidarity with one another and enjoyed close relations despite their antithetical regimes, on the basis of a shared concern, fear and disdain of imperialism. In fact, when the young Turkish Republic undertook its industrialization policy, the Soviets helped it with loans, know-how and expertise in industrial planning.

The dominant position of the Soviet Union in Eastern and Central Europe at the end of the war and its claims on Turkish sovereignty and territory played a determining role in Turkey's strategic choice as the Cold War order began to take shape. Assessing a vital threat to its security, Turkey launched its close strategic relation with the United States and joined the Atlantic Alliance by doggedly pursuing it and even sending troops to Korea in order to attain that goal. During the Cold War Turkey's anti-communism both domestically and in its foreign policy considerations was relentless. Turkey was and remained a staunch NATO ally and when the military intervened and overthrew the elected government the putschists started their work by reiterating their commitment to NATO and while it was still alive, CENTO.

Despite this political and ideological hardline, Ankara had in a way its own "*Nordpolitik*" in the 1960's. While anti-communism continued to determine the policies of successive governments and military juntas the two countries had a growing economic relation that mainly benefited Turkey. Ankara sought to further its industrialization and launch its heavy industry in the 1960's and needed both know-how and capital that its Western allies were not enthusiastic to advance. Following the unprecedented visit of the then Soviet Prime Minister Alexei Kosygin, the two Cold War rivals signed a number of economic agreements that began to bear fruit in the 1970's. Naturally, both German policy of "*Ostpolitik*" and the period of *détente* between the

USA and the Soviet Union facilitated this peculiar thaw in relations. Ankara's estrangement from Washington due to the arms embargo imposed upon the former by the American Congress in the wake of the Turkish intervention in Cyprus also played a role in a tilt towards "third-worldism" by the social-democratic government in the second half of the 1970's.

The Iranian Revolution and the invasion of Afghanistan terminated *détente* and brought back the logic of the hard Cold War. Turkey's geopolitical importance increased as a result and the United States reconfigured its policy vis a vis Turkey in more accommodating, supportive and instrumental ways. Even during this period, as we will present in more detail, Turkish-Russian economic relations and trade deals continued. The Gorbachev era expanded the economic relations between the two countries and an economically ambitious Turkey started using the Soviet route, with a stop in Alma Ata (later Almati) in Kazakhstan for its national carrier THY to reach East Asia. In a sense the much vaunted "compartmentalization" of the post-Cold War years was in a more limited way operational within the confines of the Cold War as well.

In the immediate aftermath of the dissolution of the Soviet Union and the emergence of the "post-Soviet space", the two countries entered a new stage of strategic competition. Turkey was particularly interested in the Caucasus and Central Asia. These regional ambitions clashed with those of the Russian Federation during the 1990's, as other articles in this report analyze in detail. Political relations were tense but began to ameliorate after 2000 and currently enjoy a closeness that draws much attention both in the Atlantic Community and around the world. Yet even during that period of tension and intense competition, meddling in each other's domestic minority problems and strife, economic relations carried on. These relations did not solely consist of the growing energy trade. They included the "suitcase" (or "shuttle") trade as well as an informal "industry" of Russians as well as post-Soviet Republic citizens working in Turkey primarily as domestic help but also as skilled labor.

Despite this background, most observers consider the scope and nature of the economic dimension of the relations

peculiar to the current state of business between the two countries. Economic ties brought Russia and Turkey closer and led them to separate their strategic issues/conflicts from their growing economic interdependence. As the quotes from the two Presidents during their joint press conference at the 8<sup>th</sup> "High Level Russian-Turkish Cooperation Council" indicate the declared centrality of the economic dimension in bilateral relations continues. These relations of "asymmetric interdependence"<sup>1</sup> have steadily deepened since the late Prime Minister (then President) Turgut Özal had the foresight to sign an agreement with the Soviet Union whereby Turkey would get natural gas from its historical rival and pay for that by selling goods that it produced. But that pathbreaking agreement and the terms that made it operational were themselves a culmination of previous periods of economic cooperation between the two countries.

Öniş and Yılmaz rightly argue that "the Natural Gas Agreement of 1984 triggered budding trade and investment ties...The Turkish private sector made a concerted effort to enter Soviet markets, capitalizing on the benefits offered by the Natural Gas Agreement. The way the agreement had been negotiated opened space for Turkish firms to operate in the tightly regulated and restrictive economic environment of the USSR."<sup>2</sup> That opening and Turkey's nearly insatiable appetite for natural gas would place energy relations to the center of economic interactions and would account for the preeminence of Turkish contracting companies in the Russian market.

The centrality of energy in bilateral relations was accentuated in a dramatic fashion in the wake of the downing of a Russian SU-24 fighter jet by a Turkish F-16 and the killing of a co-pilot by a Turkish nationalist militant fighting alongside Syria's Turcomans as he was parachuting. The harsh sanctions imposed on Turkey by the Russian government did not include even a reduction in the amount of gas supplied to Turkey and did not harm the ongoing agreements on pipelines and the building of a nuclear power plant. What led to the suspension of the talks on Turkish Stream between state owned Turkish gas giant Botaş and Gazprom was serious disputes over pricing and in fact the suspension took place in July 2015, four months prior to the downing of the Russian fighter jet.<sup>3</sup>

1 Seçkin Köstem, "The Political Economy of Turkish-Russian Relations: Dynamics of Asymmetric Interdependence", *Perceptions*, Summer 2018, v. XXIII, Number 2, pp. 10-32

2 Ziya Öniş and Şuhnaz Yılmaz, "Turkey and Russia in a shifting global order: cooperation, conflict and asymmetric interdependence in a turbulent region", *THIRD WORLD QUARTERLY*, v. 37, n. 1,

3 Gareth Winrow, "Turkey and Russia: The Importance of Energy Ties", *Insight Turkey*, v.19, n.1 p.23

This episode showed that just as Turkey depended heavily on Russia for reliable and plentiful energy supplies, the Russian Federation as well depended on securing the Turkish gas market -second only to Germany and growing. Turkey's importance as an alternative route<sup>4</sup> that would enable Russia to avoid Ukraine and maintain its dominance on European supplies also played a role in this exemption. The importance of energy in these trade relations also sets the limit of their magnitude. Even in the best of years Turkish exports did not exceed \$7 billion (in 2013) and in 2018 it stood at \$3.4 billion. Unless energy prices skyrocket or Turkey develops the capacity to sell high value-added technology products the volume of trade is unlikely to reach the heights desired by the two countries' leaders.

Currently, Turkey is the Russian Federation's second largest gas market after Germany and Moscow's main pipeline alternative to the Ukrainian route to transport Russian gas to European markets. Both Russian President Vladimir Putin and the Turkish President Tayyip Erdogan repeatedly make ambitious statements and call for a trade volume target of \$100 billion between their respective countries but that is more wishful thinking than a goal that is easily attainable.

Having reached a peak of \$38 billion in 2008, currently the trade volume is somewhere between \$23-26 billion with a trade balance favoring Russia and is unlikely to move much beyond the high levels attained before, barring a major jump in energy prices, due to reasons that will be explored further<sup>5</sup>.

The bulk of the trade figure is Turkey's gas imports from the Russian Federation. In addition to trade, economic relations include industrial and construction investments and tourism. Mostly ignored in analyses of Turkish-Russian economic relations is the aforementioned so-called "suitcase trade" that began in the age of Perestroika and prospered in the 1990s when the Russian economy suffered immensely both from the dissolution of the Soviet Union and the onslaught of neoliberal economic policies. This informal trade which gradually declined over the years as a result of restrictive measures imposed by Moscow, still amounted to around \$8.5 billion worth of Turkish exports to Russia in 2014.<sup>6</sup> In the process this trade naturally built its own network of persons and organizations that conducted their cash transactions mainly on the basis of trust.

## I. A brief history of Soviet Union-Turkey economic relations: From the solidarity of two Revolutionary regimes to Cold War adversity to the path of interdependence

Although the scope and volume of economic activities today are unprecedented, their existence is not a total novelty. The two countries actually had important economic relations throughout the last century even when they were strategically and ideologically bitter opponents. In fact, the history of Turkey's economic development could not be written without reference to Soviet loans, transfer of know-how and barter trade agreements that predate the all-important 1984 agreement the two parties signed in Ankara on September 18 that year<sup>7</sup>.

The Turkish War of Independence received considerable support from the Bolsheviks who were fighting their own existential war against the White Forces. Under the conditions of the Civil War the Bolshevik government financially aided the struggling Ankara government that represented an alternative center of power in Anatolia to the Ottoman administration in occupied Istanbul. During the War of Independence, the Bolsheviks sent gold to the Ankara government along with weapons. Following the Moscow Agreement of 16 March 1921, the Soviets committed to give

<sup>4</sup> Mitat Çelikpala, "'Rusya Gazı Keser mi?': Son Gelişmeler Işığında Türkiye-Rusya Enerji İlişkilerine Bakmak", in Kuşku ile Komşuluk: Türkiye ve Rusya İlişkilerinde değişen dinamikler, Gencer Özcan, Evren Balta, Burç Beğgül, eds. (İstanbul: İletişim yayınları, 2017)

<sup>5</sup> Russian International Affairs Council (RIAC) Report. New Stage of Russia-Turkey Economic Relations, Moscow 2016; Rus-Türk Ticaret Evi, "Rusya-Türkiye Dış Ticareti", <http://www.ros-t.com/bilgilendirme-detay-rusya-turkiye-dis-ticareti-4>

<sup>6</sup> Kelkitli, Turkish-Russian Relations, p. 109 cited in Mustafa Aydın, "Transformation of Turkish- Russian Relations; Rivalry and Cooperation in Eurasia and Levant", in Fyodor Lukyanov and Soli Özel, eds., Turkish-Russian relations: past and prospects, forthcoming

<sup>7</sup> See inter alia, Okan Yardımcı, "Energy Cooperation in the History of Turkish-Russian Relations", <https://www.linkedin.com/pulse/energy-cooperation-history-turkish-russian-relations-okan-yardimci>

10 million rubles/year to the Turkish government.<sup>8</sup> In May of 1922 the first trade agreement between the parties was signed. In 1925 *Vnestorgbank* opened a branch in Istanbul. With the signing of the Trade and Navigation Agreement in March 1927 trade volume doubled but as the Soviet Union moved towards policies of collectivization the agreement became problematic and some of its articles were altered in 1931.<sup>9</sup>

Prime Minister İsmet İnönü's lengthy 1932 visit to Russia resulted in the first substantive cooperation and financing agreement between the two parties. The Soviets extended an interest free loan of \$10 million, to be paid in twenty years with Turkish exports. The loan was then used to build two textile factories in Nazilli and Kayseri whose engineers were trained in the Soviet Union. Soviet technicians assisted in the building of the factories and trained the personnel on location. The Turkish delegation impressed by what they saw of the Soviet industrialization and having launched a policy of "étatisme" at home to meet the challenges of the Great Depression decided to prepare an industrialization plan. The first five-year plan was drafted with assistance from Soviet experts and was made public in 1934.<sup>10</sup>

During the Second World War and its aftermath Turkish-Soviet economic relations did not register much activity or improvement save for the Çayırova glass factory that was established with Soviet credit.<sup>11</sup> In fact Moscow's demands for two Turkish provinces and joint control over the naval traffic going through the Turkish straits pushed Ankara to align itself with the United States. Therefore, the decade of the 1950s was one of Cold War animosity and lack of economic cooperation, as historically rooted anti-Russian sentiment

combined with a relentless anti-communism to shape and reinforce the "Russian enemy" image. This situation began to change in the 1960s as Turkey moved to a developmental model based on planning that privileged heavy industry for which ambitions, she did not receive a warm response from her allies. In urgent need for funding and technology, the center-right developmentalist government of Süleyman Demirel turned to the Soviet Union. This was the background to Prime Minister Alexei Kosygin's visit in Turkey in 1966.<sup>12</sup> During this visit the Soviets made a commitment to finance and provide technical assistance to Turkey's heavy industry and energy investments. Turkey received a loan of \$200 million "for building iron and steel plants in İskenderun as well as the Seydişehir aluminum factory, the Aliğa oil refinery plant and the Bandırma Sulphur acid factory".<sup>13</sup>

Ten years later, two more agreements were signed to improve economic relations and to move forward with scientific and technical cooperation. The Russians would help with the construction of Arpaçay dam, expand İskenderun Iron and Steel Plant as well as the Seydişehir Aluminum Plant. A thermal power plant in Orhaneli would be built. A Black Sea Oil Refinery Project was also discussed.<sup>14</sup> In all these deals that were important for Turkey's industrialization drive, Turkey made its loan payments by exporting goods to the Soviet Union, mainly traditional agricultural produce. In 1982, the parties signed another agreement to change payment conditions. Accordingly, at least part of the payments was henceforth to be made in freely convertible currency; the deliveries of goods were to be made at current prices of the main world markets for corresponding goods which were to be expressed in freely convertible currency.<sup>15</sup>

<sup>8</sup> Ülkü Çalışkan, "Türk Kurtuluş Savaşında Sovyet Rusya'nın Mali ve Askeri Yardımları" (Soviet Russia's Financial and Military Aid during the Turkish War of Independence), *Karadeniz Araştırmaları*, Sayı 9 (Bahar 2006)

<sup>9</sup> İmren Arbaç, "1923-1938 yılları arasında Türk-Sovyet ekonomik ve siyasi ilişkileri: (Turkish-Soviet Economic and Political Relations between 1923-1938), paper presented at YEDİTEPE ÜNİVERSİTESİ TARİH BÖLÜMÜ II. ULUSLARARASI TÜRK KÜLTÜRÜ VE TARİHİ SEMPOZYUMU,

<sup>10</sup> *ibid.*

<sup>11</sup> Nigyar R. Masumova, "Russia and Turkey: Resetting Economic Partnership", *Perceptions*, Summer 2018, v.XXIII, n.2, p.34

<sup>12</sup> Mehmet Altan, *Süperler ve Türkiye (Superpowers and Turkey)*, İstanbul: Afa Yayınları

<sup>13</sup> Nigyar R. Masumova, *ibid.*, p.35

<sup>14</sup> Yardımcı, *op. cit.*, "Under the given agreements, the USSR supplied Turkey with the necessary expertise, equipment, materials, and technical services for its industrial development (the conditions of the İskenderun Project can be seen in Doc. 3). The financial value of the USSR's support was considered a debt incurred by Turkey. For example, the USSR supplied \$200 million to fund the expansion of the Seydişehir Aluminium Plant, under the condition of a 5% yearly interest rate over a 10-year repayment period.[iv] The USSR likewise provided \$53 million to fund the construction of the Orhaneli Thermal Power Plant, under the condition of a 3.5% yearly interest rate over a 10-year repayment period.[v] In addition to the two countries' cooperation in industrial construction, the two countries cooperated in the energy market, with Turkey importing oil and oil products from the USSR."

<sup>15</sup> *ibid.*

These existing economic ties, payment models and modes of cooperation laid the groundwork for the critical agreement signed in September 1984. The Soviet Union was to sell natural gas to Turkey starting in 1987 using a route through Romania and Bulgaria. The length of the agreement, with a provision for auto-renewal every five years, was to be 25 years. The price for the initial amount of 1.5 million cubic meters was to be determined by BOTAŞ and SOYUSGAZ. The payments as in earlier agreements were to be made by merchandise and commodity exports.<sup>16</sup>

As suggested earlier on several counts this agreement signed between the two countries on opposing camps of the strategic divide and while the Reagan administration was reigniting the furies of the Cold War was path breaking. It did not just initiate the ever-closer energy relations between Turkey and Russia that today made the latter the primary supplier of natural gas to the former. The Gas agreement

paved the way for pipeline construction that, with the end of the Cold War inspired the Turkish governing elite to try to turn their country into a transit route for Caucasian and Central Asian gas if not an energy hub, however unrealistic this latter ambition may still be. As importantly, because on the Turkish side private businesses under the coordination of Foreign Economic Relations Board (DEİK) spearheaded the improvement in economic relations many leading companies, particularly in the construction industry established themselves as prominent businesses first in the Soviet Union, then in Russia and the post-Soviet space and helped expand bilateral trade relations. As Öniş and Yılmaz note, “Developments in the second half of the 1980s, well before the collapse of the USSR and the end of the Cold War, constituted a genuine turning point in Turkish-Russian relations and created the basis of the strong economic partnership that has emerged over the course of the past three decades”.<sup>17</sup>

## II. After the Fall: From the Union of Soviet Socialist Republics to the Russian Federation

The unexpected dissolution of the Soviet Union ushered in a new era in world politics and naturally in Turkish-Russian relations. Some of the trends evident in the last few years of the Soviet Union were more accentuated and began to shape the patterns of the 1990s, arguably a very turbulent decade for the two countries both economically and politically.

Economic relations between Russia and Turkey had grown both formally and informally in this decade. The informal trade

networks that began to be established in the last years of the Soviet Union continued to grow and registered a relatively considerable volume of trade between Turkey and both Russia and the new states that just became independent. The so-called “suitcase trade” centered in the conservative district of Laleli in Istanbul is usually ignored in the analyses of Turkish-Russian economic relations but we believe that it deserves serious treatment in order to complete the picture of bilateral economic relations.

<sup>16</sup> *ibid*

<sup>17</sup> Öniş and Yılmaz, *op. cit.* p. 75

## a) The suitcase trade between Turkey and Russia

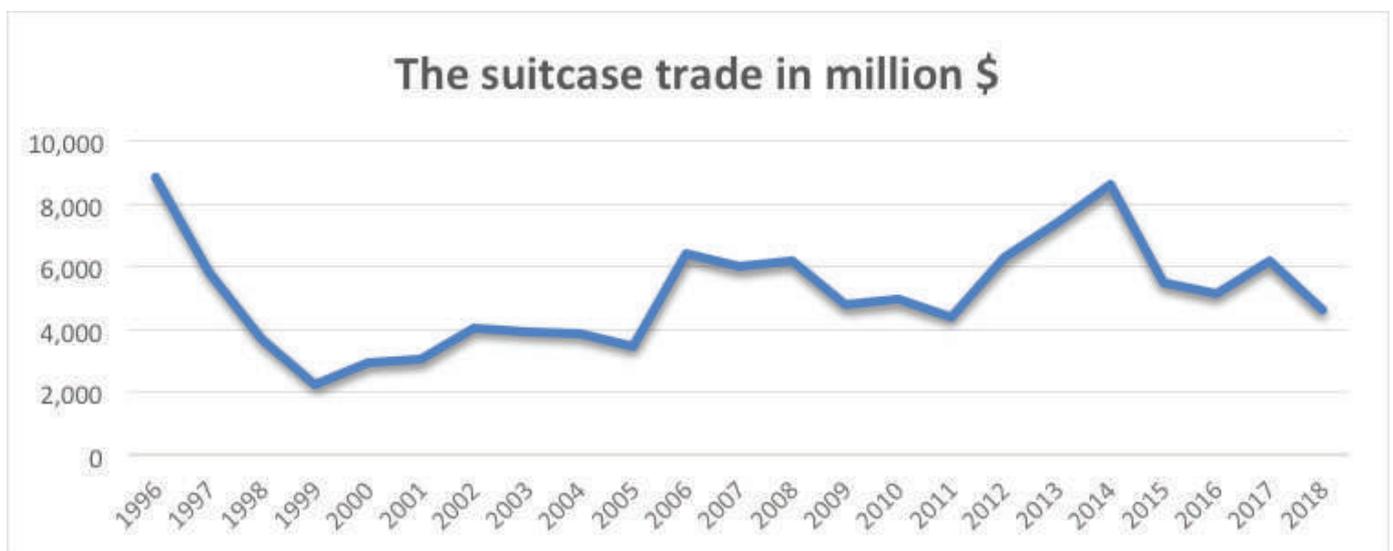
The economic dimension of Turkey's relations with Russia at the bilateral level was very impressive throughout the 1990s. The shuttle trade- or the "suitcase trade" - took a large part in this development of bilateral economic relations. The shuttle trade began in the age of Perestroika and prospered in the 1990s when the Russian economy suffered immensely both from the dissolution of the Soviet Union and the onslaught of neoliberal economic policies. This informal trade, which gradually declined over the years due to restrictive measures imposed by Moscow, still had an export value of \$ 8.5 billion in 2014 for Turkey.

In the late 1980s, Laleli settled into the role of a district with medium sized, medium-quality hotels, with small to medium-sized shops and lower quality goods. The collapse of the Soviet Union and the opening of the borders between the former Soviet republics and Turkey engendered the shuttle trade, starting a new trans-border informal trading network.

Turkey's exports to Russia through this informal network were a welcome development for Russian consumers as they became able to buy these relatively cheaper products at a time of major economic crisis that affected their daily lives. In this context, the 'shuttle trade' continued to prosper Turkey's trade with Russia until 1998 financial crisis in Russia. It severely affected the tradesmen in the Laleli district of Istanbul and their suppliers in some of Turkey's provincial cities.

The goods sold in this trade network were mainly consumer goods -in textiles, leather goods, and household products<sup>18</sup>. At its peak in 1995, the volume of suitcase trade reached an estimated \$10 billion, and Turkey was believed to have gained roughly \$5 billion in sales for the estimated 5,000 shops in Laleli in the same year (Figure 1)<sup>19</sup>. Even after the ruble crisis in 1998, shuttle trade accounted for 10.3 percent of Russia's foreign trade turnover.

**Figure 1: The suitcase trade**



Source: Own elaboration based on calculations from the Turkish Central Bank data (2019)<sup>20</sup>

<sup>18</sup> Aydin K., Oztig L.I. & Bulut E. International Business Research; Vol. 9, No. 3; 2016. The Economic Impact of the Suitcase Trade on Foreign Trade: A Regional Analysis of the Laleli Market

<sup>19</sup> Little official information is available on the suitcase trade between 1991 and 1996. The official data on the suitcase trade is available from 1996 onwards.

<sup>20</sup> <http://www.tcmb.gov.tr/wps/wcm/connect/609ef884-3b3c-4bc3-84fe-9254244c3490/odemelerdenyesi.pdf?MOD=AJPERES&CACHEID=ROOTWORKSPACE-609ef884-3b3c-4bc3-84fe-9254244c3490-mdtsMuZ>

Despite relatively declining profit margins, several bankruptcies and constantly changing regulatory customs regime, these transnational networks have grown distinctively resilient<sup>21</sup>. Although, it is “fragile” and “transient” in its nature, the network has mostly been addressed as a *transnational business community* due to its common practical, and normative frameworks<sup>22</sup>. The way in which economic agents established business ties and built trust in Laleli was fairly characteristic of such practices. This Laleli trade network continued its operations for more than twenty years as a hub for transnational traders<sup>23</sup>. Indeed, the concept of trust plays a key role in our understanding of informal relationships between the economic agents that established business ties in Laleli<sup>24</sup>.

The participants in Laleli's transnational market have been driven largely by a combination of macroeconomic factors, such as poverty and lack of sufficient jobs at home on the part of the shuttle traders, and the lack of domestic demand and markets on the part of the shopkeepers. Due to the trade liberalization that started in the 1980s and

financial liberalization that followed in the 1990s, the Turkish economy has increasingly lowered its regulatory barriers to foreign direct investments, equity flows, and commodities<sup>25</sup>. Intensive deregulation in the economy has created a fertile environment for informalization<sup>26</sup>. This was particularly important because it reduced the need to depend on or trust the state<sup>27</sup>, which then gave rise to a growing level of interactions built on the trust established between people who engage in informal activities.

Eder, Yakovlev and Çarkoğlu note that the financial shocks of 1994 (Turkey), 1998 (Russia) and 2001 (Turkey) have forced both the traders and shopkeepers to be much better organized, much more risk-averse and resilient<sup>28</sup>. Despite this, Laleli was hit hard when the recent political downturns affected the sales resulting a decline in 2014 to \$8.6 billion— in the year Crimea was annexed, and the sanctions were imposed. Then plummeted to \$5.5 billion the following year<sup>29</sup>. As Figure 2 shows below that the decline in suitcase trade is accompanied by a decrease in total Turkish exports (from \$168 billion in 2014 to \$151 billion in 2015).

<sup>21</sup> *ibid.*

<sup>22</sup> Eder M., Yakovlev A. and Çarkoğlu A. Suitcase Trade Between Turkey and Russia: Microeconomics and Institutional Structure. Working paper WP4/2003/07 — Moscow: State University— Higher School of Economics, 2003. — 32 p. (in English).

<sup>23</sup> *ibid.*

<sup>24</sup> Eder, Yakovlev and Çarkoğlu, *op. cit.* p. 96

<sup>25</sup> Eder and Öz, *op. cit.* p. 89

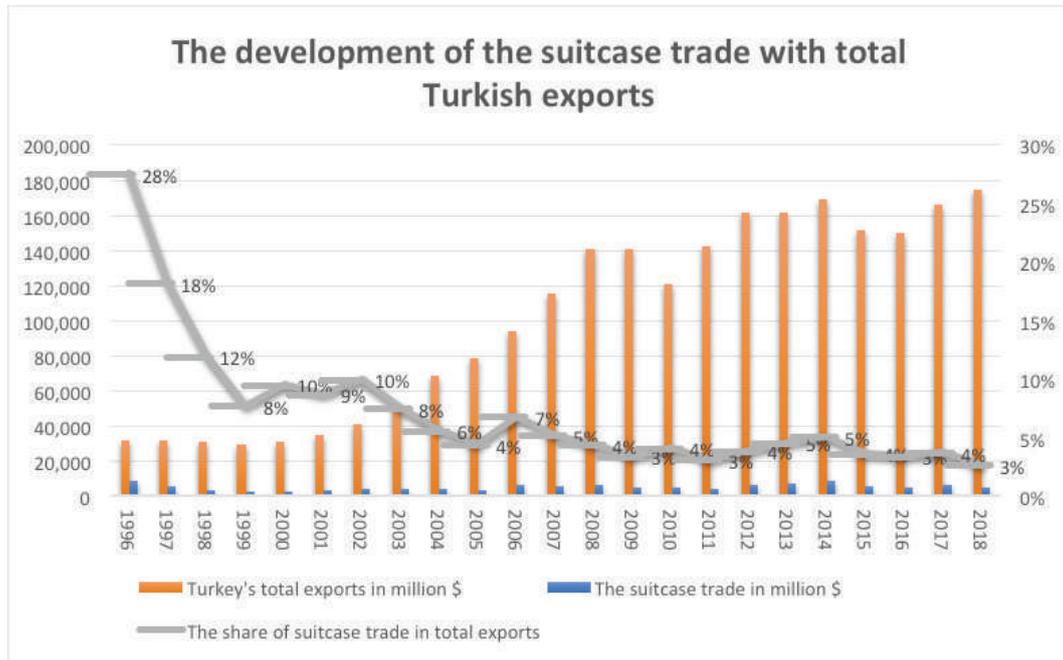
<sup>26</sup> *ibid.*

<sup>27</sup> Eder, Yakovlev and Çarkoğlu, *op. cit.* p. 25, “Laleli shopkeepers appear to choose informality for two reasons. One is the lacking capacity of the state to respond to the demands of Laleli community. From municipality services to traffic, all shopkeepers have complained about the bad service. Second is the illegal aspect of informal trade which is done for very high profit margins. According to Gambetta (1993), the inability of the state to resolve disputes fairly and efficiently creates a search for alternatives (See also, among others; Varese, 1994). In decreased legitimacy of the state's formal ties to citizens and lack of competence therein, “people may trust each other because of close personal ties that depend on kinship, business links or friendship” (Rose-Ackerman, 1999, 97)”.

<sup>28</sup> *ibid.*

<sup>29</sup> <https://eurasianet.org/istanbul-storied-suitcase-trade-with-ex-ussr-remains-resilient-despite-downturn>

Figure 2: The development of the suitcase trade with total Turkish exports<sup>30</sup>



Source: Own elaboration based on calculations from the Turkish Central Bank data (2019).<sup>31</sup>

## b) Formal Trade, BSEC, Investment, Construction and Tourism

The Turkish government anticipated the fundamental changes that would take place geo-politically and geo-economically in its immediate vicinity as the Soviet Union under Mikhail Gorbachev undertook its ambitious, but ultimately futile and destructive economic restructuring program.<sup>32</sup> Accordingly, Turkish economic bureaucracy and some diplomats started looking at the Soviet economic space as an area to be explored and exploited to further Turkey's economic interests<sup>33</sup>. In this light, one of the most important Turkish initiatives in the early 1990's was the founding of an organization for the ostensible goal of creating a zone

of economic integration in the Black Sea region. Turgut Özal, elevated to the Presidency of the Turkish Republic on the day the Berlin Wall fell and effectively brought the Cold War to an end, saw this development as presenting important opportunities for Turkey. A true Cobdenian in his approach to international relations, Özal believed that with the waning of the Cold War and the transformation of the Soviet economic system in a market-oriented direction there were new venues opened for economic cooperation in regions bordering Turkey.

<sup>30</sup> The blue pillar of Figure 2 show the revenue of the suitcase trade, total Turkish exports (orange pillar) between 1996 and 2018. While the revenues of the suitcase trade in 1996 and 2018 are approximately the same (between 8 and 9 billion dollars), their percentages in total Turkish exports plummeted dramatically from 28% in 1996 to 3% in 2018 (grey line). This decrease could be associated with an increase in total Turkish total exports from 1996 to 2018. While in 1996, total Turkish exports was 23.2 billion dollars, in 2018 it rose to 174.6 billion dollars.

<sup>31</sup> <http://www.tcmb.gov.tr/wps/wcm/connect/609ef884-3b3c-4bc3-84fe-9254244c3490/odemelerdengesi.pdf?MOD=AJPERES&CACHEID=ROOTWORKSPACE-609ef884-3b3c-4bc3-84fe-9254244c3490-mdtsMuZ>

<sup>32</sup> "Turkey's relations with Moscow began improving rapidly after the election of Gorbachev as president. This was not a simple coincidence since Gorbachev's approach to foreign policy involved the improvement of economic co-operation rather than competition with the capitalist world. For Turkey, this meant that the long-feared Soviet threat was disappearing. Of course, this helped Özal and contributed to Turkey's policy of developing its trade with the Soviet Union as much as possible. Parallel with trade, diplomatic relations also showed a steady development. In July 1986, Özal visited Moscow and signed several agreements concerning trade, along with others regarding commercial, technological and scientific co-operation. Gorbachev and Özal agreed that the Soviets would finance the construction of two hydroelectric plants in Turkey, and that Turkey would buy natural gas from the Soviet Union and would pay 70 per cent of the gas bill through the export of Turkish products. If the gas did not reach the required level, the Soviets would employ Turkish contractors in the Soviet Union." Şaban Halis Çalış, *Turkey's Cold War*, (London: I.B. Tauris 2017), p. 192

<sup>33</sup> Dr. Şükrü Elekdağ, "From Geopolitics to Geo-economics", Private View, *The Quarterly Journal of TÜSİAD*, January 1996, n.1

The Black Sea Economic Cooperation was meant to become a multilateral organization to integrate the economies of both riparian countries and those in the periphery that were interested in such a project. As Davut Han Aslan and Muhammadqosim Sharapov note, "It was the initiative of Ankara to gather states having borders at the Black Sea and broaden it after the collapse of the iron curtain. The main motivation of Ankara was to create an atmosphere of cooperation based on economy so as to prevent future conflict prospects in the Black Sea region. In addition to that, Turkey, basically aimed to increase its economic influence in the post-Soviet region while easing its access to raw materials and energy resources. Initially the main objective of the BSEC was to create a "free trade zone" in the Black Sea region, yet aftermath it was adapted to an economic cooperation project."<sup>34</sup>

In the event BSEC did not become what its originators intended it to be. Öniş and Yılmaz acknowledge that "BSEC is a project that has had limited success". They identify four reasons for it to have remained just a loose integration scheme: "First, none of the key states involved was willing to delegate national state authority to a supranational entity... Second, a more institutionalized and rigid membership of the BSEC would involve significant delegation of authority to a supranational body...Third, a deeper element that constrained more formal and institutionalized interaction between states in the Black Sea region was the absence of common norms or a common identity...Fourth, the region lacks the financial resources for significant intra-regional

transfers, a conduit to greater delegation of autonomy and a more formal integration process."<sup>35</sup>

Just as BSEC was founded, Turkey and the newly minted Russian Federation signed their first agreement in 1992 "on the basic principles of relations between Russia and Turkey (that) initiated deeper political, economic and cultural cooperation between the two countries".<sup>36</sup> It is interesting to note that 1992 was the year when the then Chief of Staff of CIS, Marechal Yevgeny Shaposhnikov warned about the outbreak of the 3d World War if Turkey intervened militarily in the Nagorno-Karabagh conflict between Armenia and Azerbaijan.<sup>37</sup> More than 20 agreements were signed between 1992 and 1996 encompassing economic, technological, scientific, cultural issues and tourism. Balta and Özkan note that the Turkish-Russian Joint economic Commission that laid the foundations of current economic relations was also founded in 1992.<sup>38</sup> Trade between Russia and Turkey grew steadily in the 1990s and took off in the 2000s despite problems caused by the geopolitical competition between the parties. Whereas trade stood at \$1.84 billion in 1992<sup>39</sup> in 2018 it reached \$25.5 billion as President Putin stated, after having seen a peak of nearly \$38 billion in 2008 and a sharp break in the wake of Russian sanctions that penalized Turkey for the downing of a Russian jet. Whereas the trade was by and large balanced in the 1990s, in later years Turkey registered a consistently large trade deficit vis a vis Russia because of its high dependence on energy imports (Figure 3).

<sup>34</sup> Davut Han Aslan and Muhammadqosim Sharapov, "Turkey and the Black Sea Economic Cooperation (BSEC)", [http://cejsh.icm.edu.pl/cejsh/element/bwmeta1.element.desklight-fdfa942c-349f-49be-bbc0-9dd658239a5b/c/Zeszyty-naukowe-34\\_2014.126-136.pdf](http://cejsh.icm.edu.pl/cejsh/element/bwmeta1.element.desklight-fdfa942c-349f-49be-bbc0-9dd658239a5b/c/Zeszyty-naukowe-34_2014.126-136.pdf)

<sup>35</sup> Öniş and Yılmaz, op. Cit. Pp. 80-81

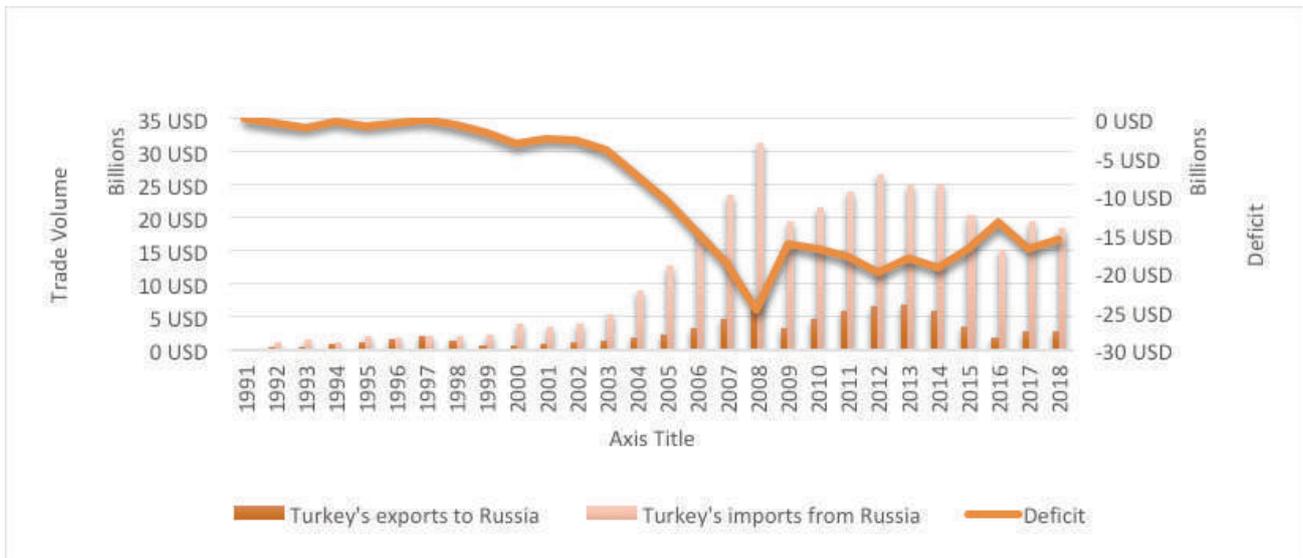
<sup>36</sup> Masumova, op. Cit., p.36

<sup>37</sup> Şener Aktürk, "Türkiye'nin Rusya ile İlişkilerinin Yükselişi ve Gerilemesi, 1992-2015" in Gencer Özcan, Evren Balta, Burç Beşgül eds., *Kuşku ile Komşuluk*, İstanbul. İletişim Yayınları, 2018

<sup>38</sup> Evren Balta-Behlül Özkan, "Türkiye-Rusya ilişkilerine 'Tarih' ile Bakmak", Boğaziçi Üniversitesi-TÜSİAD Dış Politika Forumu Araştırma Raporu, İstanbul, 2016

<sup>39</sup> Aydın, op.cit.

**Figure 3: Trade between Turkey and Russia**



Source: Own elaboration based on calculations from TUIK data (2018).

Mitat Çelikpala identifies the visit by the Russian Prime Minister Mikhail Kasyanov in October 2000 as a turning point in the relations between the two sides. During that visit Kasyanov pronounced that “Russia and Turkey are not rivals. We are partners and our governments will develop our bilateral relations according to this principle”. For Çelikpala this was the moment when the two countries put aside their geopolitical conflicts of the 1990’s that hampered their economic ties, decided to compartmentalize their relations and move ahead in a framework of improved economic and commercial ties.<sup>40</sup> It is also worth noting that in 2001 two important steps towards institutionalizing these relations were taken. Upon the recommendation of the then Foreign Minister İsmail Cem a working group to be formed by what he called the “strategic triangle” of Moscow-Ankara-Central Asia was to “determine the areas for political and economic cooperation”. Later in 2001, during the UN General Assembly meetings, the foreign ministers of the two countries signed “Cooperative Action Plan between the Republic of Turkey and the Russian Federation: From bilateral cooperation to multidimensional partnership”.<sup>41</sup> Such initiatives would continue throughout the decade, visa exemptions would be instituted and the trend for closer relations would be crowned by the formation of the High Level Russian-Turkish

Cooperation Council in 2010.

The growth in trade was more visible after 2000 for the following reasons as well: Under President Putin, the Russian economy started to recover. Both because, in the aftermath of the financial collapse in 1998 the management of the economy got better, and more importantly rising oil prices enabled Russia to recover financially. Given the fact that Turkey, in the wake of its own financial crisis in 2001 speedily recovered and started to grow rapidly meant that its energy needs grew considerably. Second only to China globally in rising energy needs and electricity, Turkey’s deep dependence on Russian gas meant that its imports grew significantly in that period. By the global financial crisis of 2008-9 the bilateral trade grew to the aforementioned \$38 billion, a figure that was not recovered since then (Figure 3).

We will return to the role of energy, pipelines and Turkey’s disproportionate dependence on Russia for its energy needs and whether or not that constitutes a security threat as well in the following sections. As things stand, the imbalance in trade relations will continue for the relevant future. IN fact, in 2018 Russia ranked 12<sup>th</sup> among Turkey’s export destinations with a volume of \$3.4 billion<sup>42</sup> (Figure 4) and it was number

<sup>40</sup> Çelikpala, op.cit

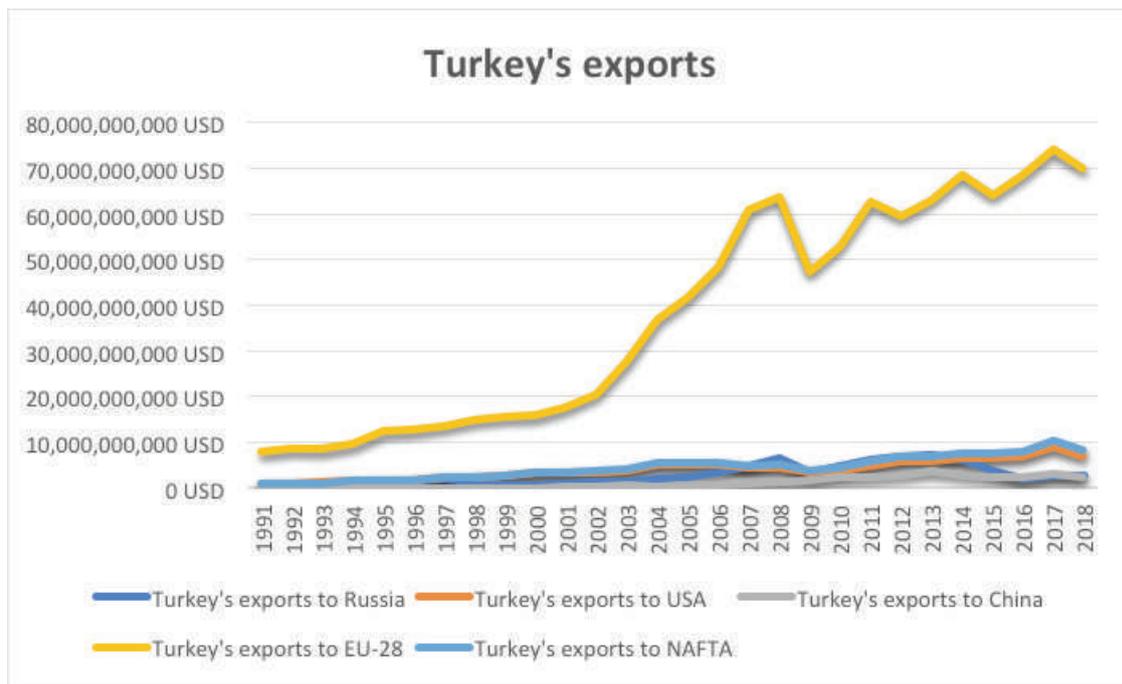
<sup>41</sup> Balta and Özkan, op. Cit.

<sup>42</sup> TUIK, <http://tuik.gov.tr/UstMenu.do?metod=temelist>

one for imports with a volume of \$21,989 billion.<sup>43</sup> The composition of Turkish exports consists of textiles (around 20%), machinery and equipment (23%), food (around 22%) and household appliances.<sup>44</sup> Köstem argues that “while the Turkish media has primarily paid attention to the Russian ban on Turkish tomatoes, the sectors that were

most severely damaged by the Russian sanctions...are the automobile industry, and machinery and equipment.”<sup>45</sup> The trade imbalance is unlikely to disappear so long as Turkey is unable to diversify its energy sources and/or so long as its export bill does not include high value added, high technology goods that are not easily substitutable.

**Figure 4: Turkey’s exports from 1991 to 2018**



Source: Own elaboration based on calculations from TUIK data (2018).

### c) Contractors and their work

The scope of economic relations is not limited to trade. Turkish companies, particularly contractors have been active in the Russian Federation since the 1984 agreement by taking advantage of its clauses. Most of them established stellar reputations in their own industry. Turkish contractors have completed more than \$65 billion worth of contracts in Russia by the end of 2017 and have invested around \$10 billion in the country. In return, Russian investments in Turkey, excluding the Akkuyu Nuclear Power Plant, equaled that figure.<sup>46</sup> Köstem notes that “Russian investments in Turkey concentrate on sectors such as energy, metallurgy, banking and the automotive industry, which are of higher strategic importance and added value compared to Turkish

investments in Russia. Turkish investments...concentrate on the construction sector...as well as low to medium technology sectors such as alcoholic beverages, chemicals and glass production.”<sup>47</sup> By the end of 2016, there were over 2000 Russian firms operating in Turkey and around 1500 Turkish firms operating in Russia. And as of 2018, Russia remains the country with the highest turnover of Turkish contractor companies abroad (Figure 5). Major Turkish companies that do business in Russia include Anadolu Efes (alcoholic beverages), ENKA (construction), Renaissance (Construction) Şişecam (glass), Eczacıbaşı (tiles and ceramic ware), Hayat (consumer goods and wood products) and Zorlu (household appliances and energy).<sup>48</sup>

<sup>43</sup> [https://countries.bridgat.com/Turkey\\_Trade\\_Partners.html](https://countries.bridgat.com/Turkey_Trade_Partners.html)

<sup>44</sup> RIAC, op. Cit., p.7

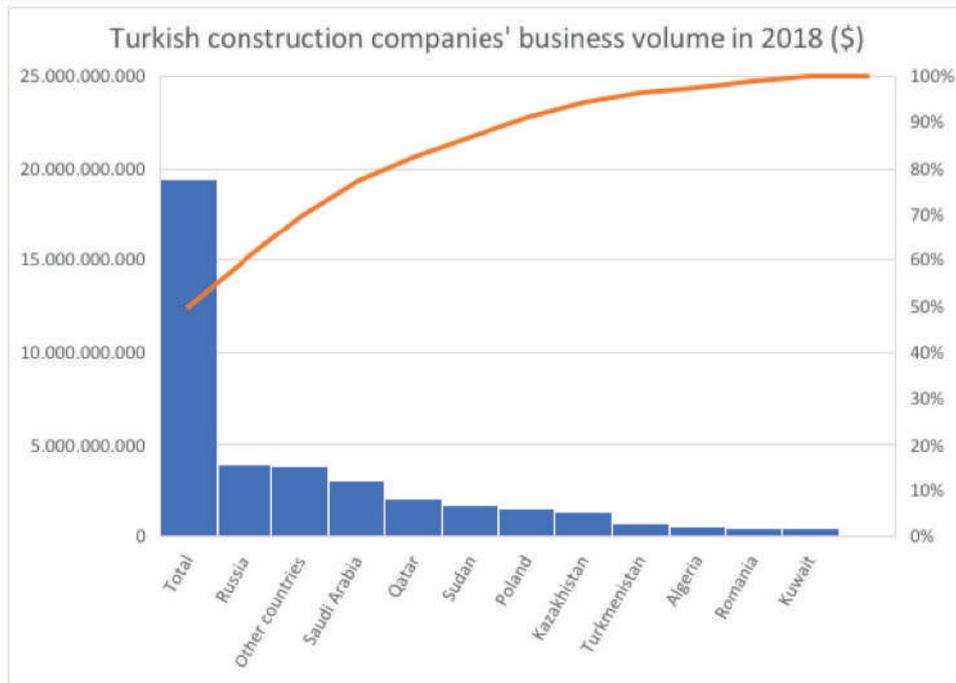
<sup>45</sup> Köstem, op. cit. p.16

<sup>46</sup> <http://moskova.be.mfa.gov.tr/Mission/ShowInfoNote/219659> (Accessed 18 June 2018).

<sup>47</sup> Köstem, op. cit. p.18

<sup>48</sup> Köstem, op. cit. p. 19

**Figure 5: Turkish construction companies' business volume in 2018 (\$)**



Source: Own elaboration based on calculations from TUIK data (2018).

**Figure 6: Total number of workers in Turkish construction companies in Russia (2015-2018)**

Years	Number of workers for each million \$	Total number of workers in Turkish construction companies in Russia	Total project value in Russia (\$)
<b>2015</b>	1,38	3152,8	2.284.638.224
<b>2016</b>	1,76	3117,7	1.771.474.376
<b>2017</b>	1,34	2302,7	1.718.493.353
<b>2018</b>	1,29	5037,01	3.904.661.116

Source: Own elaboration based on the data from the Republic of Turkey Ministry of Trade and the Turkish Employment Agency.

**Figure 7: Total number of workers in Turkish construction companies in Russia (2015-2018)**



Source: Own elaboration based on the data from the Republic of Turkey Ministry of Trade and the Turkish Employment Agency.

Turkish contractors have been very successful in penetrating markets globally since they started winning tenders in different parts of the world starting with the MENA region back in 1972. Turkish Contractors Association figures suggest that “1939 projects worth \$64.8 billion were carried out in the Russian Federation” (Figure 9).<sup>49</sup> As of 2016, \$9.9 billion worth of projects were under contract mainly to build airport terminals, roads, various businesses, shopping

centers, hospitals, residential complexes and business centers. Rönesans, Enka, AE arma, Ant Yapı, Limak, İçtaş are among the major contractors that do business in the Russian Federation. The activities of Turkish construction companies were curtailed significantly in the wake of the downing of the SU-24 in November 2015. Gradually the restrictions have been lifted.

**Figure 9: Business volume of Turkish construction companies in \$ (1972-2018)**



Source: Own elaboration based on the data from the Republic of Turkey Ministry of Trade.

Russian contractors have also been active in the Turkish Market. Besides the all-important Akkuyu nuclear power plant, Russian companies, in partnership with Turkish

companies, so far were engaged mainly in the construction of hydroelectric power plants, dams, and an underwater tunnel that was part of the Melen fresh water project.<sup>50</sup>

<sup>49</sup> RIAC, op. Cit., p. 18

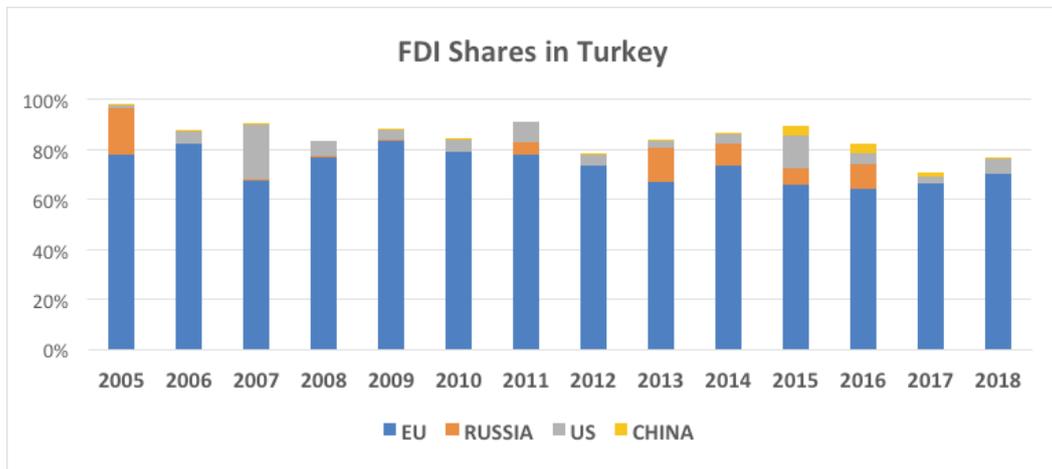
<sup>50</sup> ibid., pp. 18-19

## d) FDI flows

The Russian FDI flows to Turkey accelerated after 2011 and are more strategically oriented. The giant steel company Magnitogorsk Metal (MMK) jointly with Turkish steel company Atakaş built a steel mill in İskenderun which is currently the biggest in Turkey.<sup>51</sup> MMK also operates the privately owned Dörtyol Port, near İskenderun. Both of these facilities are also in close proximity to the nuclear power plant in Akkuyu that Russia will build, own and operate. After an amendment to the original contract, Rosatom will be able to use the surrounding areas for its own economic activities and will also be able to use port facilities in Mersin on the Mediterranean coast<sup>52</sup>. Until very recently, state owned

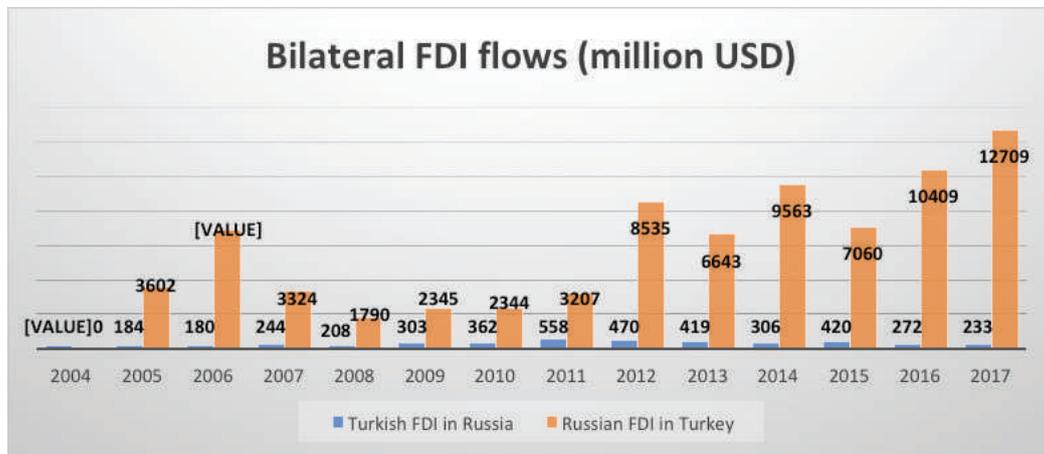
Russian bank Sberbank owned Denizbank which was sold to Dubai's NBD. Lukoil has a strong presence in the Turkish market after it bought off Akpet. Motor vehicles producer GAZ group also has a plant in Sakarya.<sup>53</sup> Although there is a rough equivalence in the amount of FDI each country's companies invested in the other there is an imbalance when it comes to the share of FDI each country has in the other's economy. Whereas in the decade between 2007-2016 "FDI originating from Russia has accounted for 2.8% of the total FDI inflow to the Turkish economy (Figure 8)...FDI originating from Turkey has accounted for only 0.3% of the total FDI in the Russian economy."<sup>54</sup>

**Figure 8: The total FDI inflow to the Turkish economy**



Source: Own elaboration based on calculations from the Turkish Central Bank data (2018).

**Figure 8: Bilateral FDI Flows (2004 – 2017)**



Source: Own elaboration based on calculations from the Central Bank of Turkey

<sup>51</sup> RIAC, op. cit. P. 8; Köstem, ibid. p.20

<sup>52</sup> [https://www.ticaretisicil.gov.tr/gosteryeni.php?ilan\\_yil=2019&sayi=9785&sayfa=853](https://www.ticaretisicil.gov.tr/gosteryeni.php?ilan_yil=2019&sayi=9785&sayfa=853)

<sup>53</sup> Köstem, ibid., p. 20

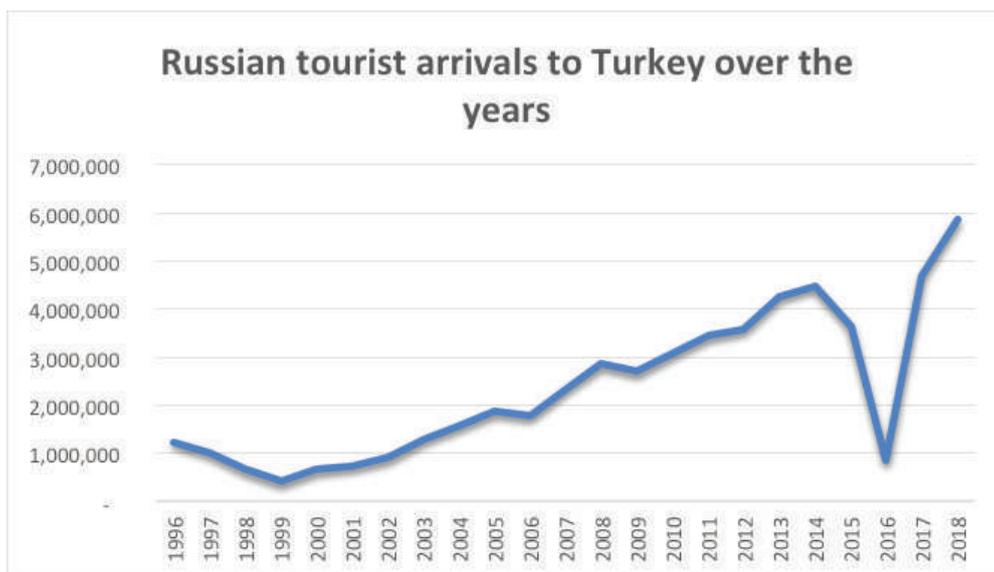
<sup>54</sup> ibid., p.21

## e) The ebb and flow of Tourism

Finally, tourism plays an important part in the economic relations between the two countries. For a long time, Turkey and particularly the Turkish Riviera have been a favorite destination of Russian tourists. Arguably, given the nature of the industry, tourism was the sector worst hit by the sanctions that President Putin put in place in retaliation for the downing of the SU-24. In fact, the ban on direct flights to the Southern city of Antalya on the Turkish Riviera had a devastating impact on the tourism industry. Antalya, itself was one of the main beneficiaries of this tourism. Many of the city's hotels specifically catered to Russian tourists and some were designed to appeal to that particular clientele.

The number of Russian tourists who came to Turkey went up from 700 thousand in 2000 to 4.5 million in 2014 (Figure 10). Admittedly, the sanctions imposed on Russia in the wake of Crimea's annexation and the slowdown in the Russian economy resulted in a decline in the number of tourists. Already in 2015, the number dropped to 3.7 million. Russia's sanctions resulted in a much sharper decline in the number of visitors to 900 thousand. Once relations ameliorated though, the numbers immediately picked up and reached 4.7 million in 2017 and nearly 6 million in 2018.<sup>55</sup> The refusal of the Russian government to lift the visa requirements on the other hand severely lowered the number of Turks traveling to Russia.

**Figure 10: The Russian tourist arrivals to Turkey in the period between 1996 to 2018**



Source: Own elaboration based on calculations from TUIK and TURSAB data (2018).

<sup>55</sup> Masumova, op. cit. P.46; <http://moskova.be.mfa.gov.tr/Mission/ShowInfoNote/219659>

### III. The Energy Axis

Energy is the mainstay of Turkish-Russian economic relations. It is the main cause of the asymmetric interdependence between the two countries. As such it is also the nexus of the growing strategic imbalance between Moscow and Ankara. Successive Turkish governments, imprudently in our opinion, took decisions that strengthened Russia's grip on the Turkish gas market. This dependency on Russia for energy was further consolidated when the construction of first ever nuclear power plant in Turkey was granted to Russia's state company Rosatom. Yet as the data in Figure 14 below shows, Turkey managed to diversify its gas sources in recent years and the share of Russia in Turkish gas consumption went down to 40% in 2018. This secular decline in the share of Russian gas in Turkey's consumption is a trend worth observing and in itself an interesting datum given how close the strategic cooperation between the two parties became in recent years.

Gareth Winrow identifies the aims of Turkey's energy policy as follows:

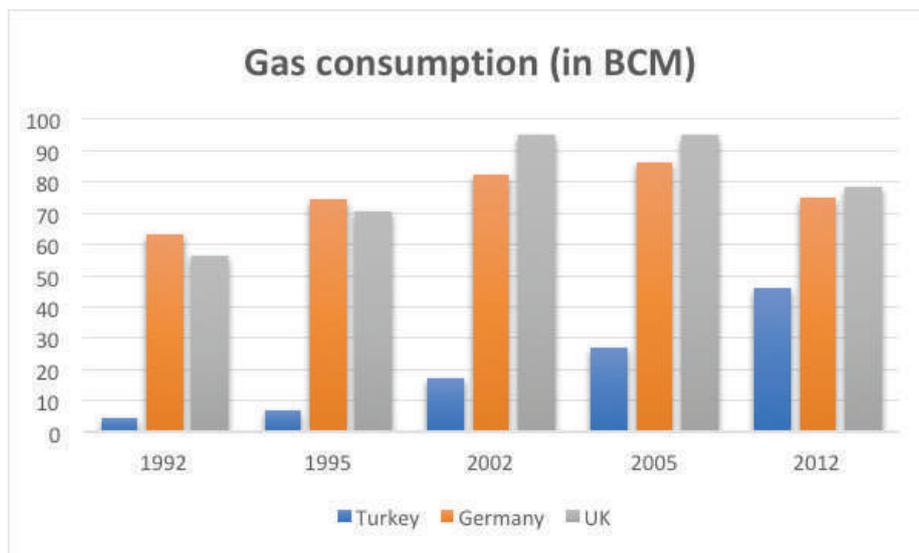
- the priority is to satisfy the energy demand of a growing economy.
- making Turkey an important energy transit state and a significant energy hub

- as such energy policy is closely interlinked with domestic politics and foreign policy concerns.<sup>56</sup>

Turkey is therefore an energy dependent country but wishes to use its geopolitical location as an asset to secure herself a place in energy related strategic developments. The country relies heavily on Russia for its supply of gas and to a lesser extent oil. This overdependence was compounded by the awarding of the Akkuyu nuclear power plant to Rosatom with concessions so significant and far reaching that some Turkish commentators likened these to the much dreaded "capitulations" granted to Western powers under the Ottoman Empire.

Emre Erşen registers that "Turkey imports 75% of its primary energy supply, which is composed of natural gas and oil. In the first half of 2017, the country's import dependency on oil was estimated to be more than 92% and...99% for natural gas."<sup>57</sup> Turkey is in constant need of finding reliable sources of energy at reasonable prices. As the world's second fastest growing market after China, Turkey's natural gas consumption has increased tenfold from 4.5bcm in 1992 to 46.3 bcm in 2012 (Figure 11).<sup>58</sup>

**Figure 11: Gas consumption (in billion cubic meters)**



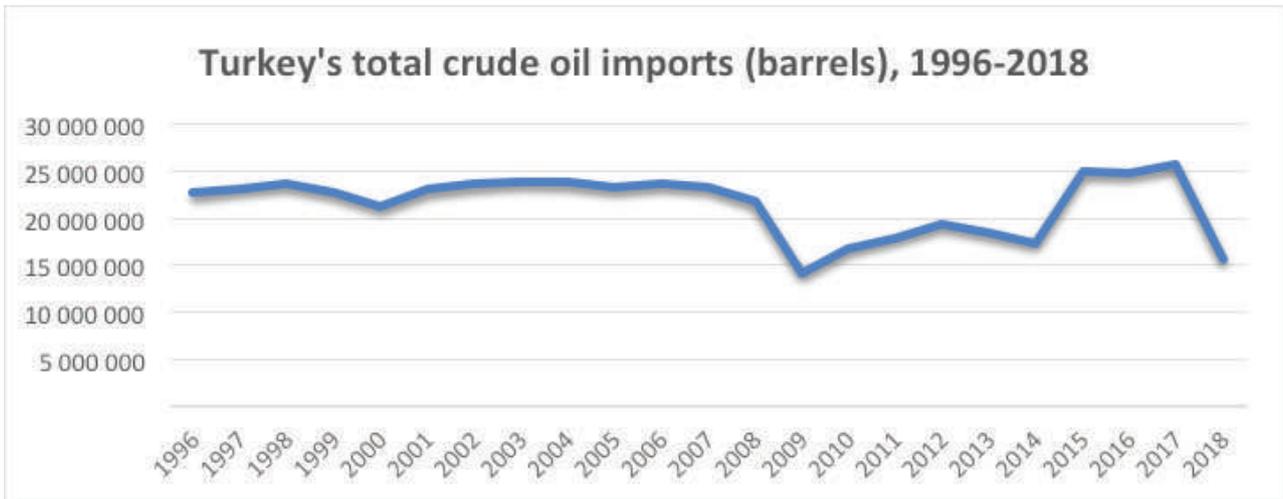
Source: Own elaboration based on the data from BP Statistical Review of World Energy, for various years.

<sup>56</sup> Gareth Winrow, "Realization of Turkey's Energy Aspirations: Pipe Dreams or Real Projects?," Brookings CUSE Turkey Project Policy Paper, No. 4, April 2014, p. 1

<sup>57</sup> Emre Erşen, "The Role of Energy in Turkish-Russian Relations: Converging and Diverging Interests" in Fyodor Lukyanov and Soli Özel, eds., Turkish-Russian relations: past and prospects, forthcoming, p.3

<sup>58</sup> Gareth Winrow, *ibid.*, p. 5.

**Figure 12: Turkey's total crude oil imports 1996 to 2018**

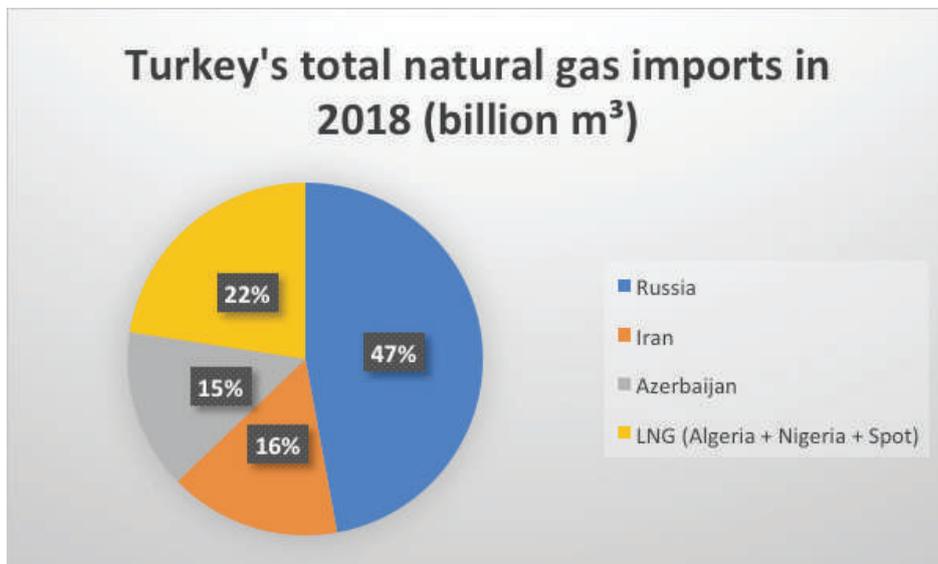


Source: Own elaboration based on calculations from TUIK data (2018).

IN 2018, natural gas consumption reached 54bcm of which one third was for electricity generation.<sup>59</sup> Turkey purchases 52% of its natural gas from Russia, 17% from Iran and 12% from Azerbaijan (Figure 13). The remaining volume comes as

LNG from Algeria, Nigeria and Qatar. Back in 2005 Russia's share in gas imports was 66%.<sup>60</sup> In oil, Iran supplies 50% of Turkey's imports, Iraq 22% and Russia 10%<sup>61</sup>, 12% come from Saudi Arabia and Kuwait.

**Figure 13: Turkey's distribution of gas imports on a resource basis in 2018**



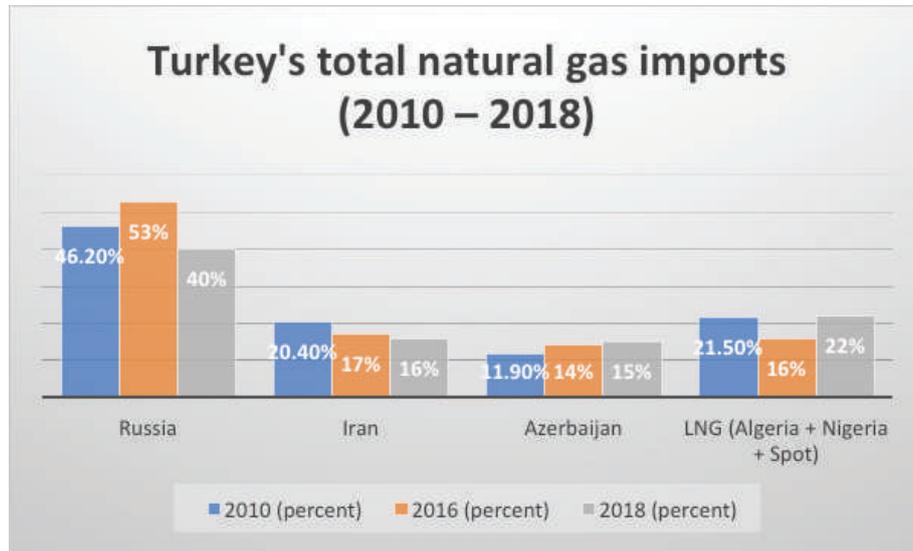
Source: Own elaboration based on calculations from Petform data (2018).

<sup>59</sup> Erşen, op. Cit., p.3

<sup>60</sup> Pinar İpek, "The Role of Energy Security in Turkish Foreign Policy", in Pinar Gözen Ercan, ed. Turkish Foreign Policy: International Relations, Legality and Global Reach, Palgrave-McMillan, 2017, p. 175

<sup>61</sup> Over the course of 1996-2018, Turkey has imported 22 million barrels of oils on average (Figure 12).

**Figure 14: Turkey's distribution of gas imports on a resource basis (2010 – 2018)**



Source: Own elaboration based on calculations from Petform data (2018).

Russia's economy depends on exports of energy and it needs stable markets. Petroleum, crude oil and natural gas accounted for 70% of all Russian exports in 2016.<sup>62</sup> Turkey is Russia's second largest natural gas market. This dynamic along with the geopolitics of gas and oil and the European Union's determination to reduce its dependence on Russian gas define the parameters of the relations between Russia and Turkey on matters concerning energy.

Both sides have their own strategic game plans, rely on one another but ultimately their interests beyond market relations do diverge considerably at times. The reasons as to why energy exports were not part of the sanctions regime President Putin imposed on Turkey in the wake of the SU-24 crisis was this interdependence; Russia's need for income and reliance on a stable market and finally the fear to appear as an unreliable supplier. The dependence of Turkey on Russia for its energy supply will be further increased when the new Turkish Stream pipeline becomes operational and the Russian firm Rosatom builds, owns and operates Turkey's first nuclear power plant in Akkuyu, in southern Turkey that is located in a "highly tectonic (spot) and open to landslides".<sup>63</sup>

Turkey is intent on using its geographical location and the advantages this location presents for her, commercially and strategically. These advantages derive from its proximity

to major energy reserves as well as its convenience as a transit route for this energy to move from various sources to Western consumer markets. Ultimately Ankara wishes to turn Turkey into an energy hub. The end of the Cold War and the opening of the Soviet space, brought the energy rich former Republics of the Soviet Union into the energy markets. Landbound as they are and relying on Russian outlets, the Western world was interested in reaching these countries' energy resources but at the same time looked for ways of by-passing Russia for transportation. IN fact the Baku-Tbilisi-Ceyhan pipeline that the Clinton administration pushed very hard to see through was the first example of this policy.

The Russians, on the other hand, have a major interest in maintaining their near monopoly power over European gas markets and block the access of the competition to these. Given the conflictual relations that Moscow has with Kiev, Russia is also interested in by-passing Ukraine after their pipeline agreement expires in 2019. The Turkish Stream that President Putin proposed in December 2014 and that replaced the South Stream Project, would serve that purpose. The European Union does not look favorably upon a pipeline that will use Turkey's EEZ and its territory to transport Russian gas since that would disrupt its plans to reduce Europe's overreliance on Russian gas. The goal of Brussels is to break member states' dependence on Russia

<sup>62</sup> Erşen, op. Cit., p. 3

<sup>63</sup> [http://www.tema.org.tr/web\\_14966-2\\_2/entitilfocus.aspx?primary\\_id=1341&target=categorial1&type=2](http://www.tema.org.tr/web_14966-2_2/entitilfocus.aspx?primary_id=1341&target=categorial1&type=2)

as a supplier and pipeline operator. Brussels has developed a Southern Gas Corridor (SGC) strategy just to be able to access non-Russian sources and transport them outside of Russia. The ill-fated and now defunct Nabucco project that was launched with great fanfare but could not secure the

requisite financing was one attempt to materialize that goal. These strategic positions provide the context within which Turkey tried to develop its energy policy and Russia pushed for hers.

## a) Supplies, market dominance, strategic aspirations

As has been a pattern even during the heyday of the Cold War, Turkey maintained its strategic identity within the Western Security system but managed to have mutually beneficial relations with Russia in the post-Cold War period notwithstanding the tit-for-tat support of one another's insurgent movements in the '90s. Other pieces of this report argue that the geopolitical and even economic balance of power between the two countries favored Turkey during the 1990s. In the 21<sup>st</sup> Century as their "asymmetric interdependence" grew and Russia regained its geopolitical posture, this has changed. Following the war in Georgia and the annexation of Crimea, Turkish naval supremacy in the Black Sea was by and large over, a fact that led President Erdoğan to warn NATO Secretary General Stoltenberg, during the period of tension and sanctions between Moscow and Ankara: "You are not visible in the Black Sea. Your invisibility in the Black Sea is turning the Black Sea virtually into a Russian lake."<sup>64</sup>

Despite these concerns though, "close energy ties between Russia and Turkey were maintained after Russia invaded Georgia in 2008 and annexed Crimea in 2014."<sup>65</sup> Even during the most serious crisis between the two countries in the wake of the downing of the Russian jet on 24 November 2015, Russia did not include cutting gas supplies in its sanctions regime and preparatory work on the Akkuyu nuclear power plant continued.

The 1984 agreement that allowed Turkey to pay with goods for the gas she bought from the Soviet Union led to the

construction of the first pipeline -the Western Line- that ran through Ukraine, Moldova, Rumania and had a capacity of 6bcm that was later expanded to 14bcm<sup>66</sup>. The dissolution of the Soviet Union presented a radically different geopolitical and energy picture. IN the new environment Turkey sought both to secure reliable supplies for its growing energy needs and to become first an energy corridor and then a hub for gas, at the same time protecting the straits from the perils of rising tanker traffic. The straits continue to be an important route for Russian tankers. Ersen quotes IEA figures pointing that an estimated 3 percent of the global oil supply was shipped through the Straits.<sup>67</sup>

With the second gas agreement Turkey signed with Russia on 10 December 1996 the terms for the payment of gas purchases changed from mainly barter to exclusively cash. This second agreement stipulated that Turkey would buy 8bcm/year from Russia and the agreement would remain in force for 23 years.<sup>68</sup> Next came the controversial Blue Stream project that the Russian authorities pushed very hard for and that replaced the plans for Turkey's purchase of Turkmenistan's gas directly from that country. This third gas agreement between Russia and Turkey significantly boosted Turkey's dependence on Russian gas and made her the second largest market after Germany once the pipeline became operational with a two year delay in construction in 2002. Half owned by ENI the Blue Stream would carry Russian oil underneath the Black Sea and would have a capacity of 16bcm of which Turkey would receive 2bcm.<sup>69</sup> Once Blue Stream opened in 2002 Turkey's gas imports from Russia

<sup>64</sup> Haberrus, "Erdoğan: Karadeniz adeta Rusya'nın bir gölü haline dönüşüyor", 11 May 2016  
<https://haberrus.com/politics/2016/05/11/erdogan-karadeniz-adeta-rusyanin-bir-golu-haline-donusuyor.html>

<sup>65</sup> Gareth Winrow, "Turkey and Russia: The Importance of Energy Ties", Insight Turkey, V.19, n.1, 2017, p.17

<sup>66</sup> Sinan Oğan, "MAVİ AKIM PROJESİ: Bir Enerji Stratejisi ve Stratejisizliği Örneği" (The Blue Stream Project: A case study of energy strategy and of the absence of one) Stradigma.com, August 2003, <http://www.emreozgur.com/Mavi.pdf>

<sup>67</sup> Ersen, op, cit., p.5

<sup>68</sup> Ibid.

<sup>69</sup> Assessing Turkey's energy strategies for the decade that covers 1992-2002 Oğan concludes that Turkey suffered the consequences of its own lack of coherent strategy that would better protect national strategic and economic interests: "In these three separate gas agreements signed with the Russian Federation enough attention has not been paid to the country's "energy security" and a dependence on Russian gas close to 60% of demand has been created; The trade balance favoring Russia has widened further; By not stipulating on at least partial barter arrangements Turkey's export potential has been restricted; Turkic Republics' already existing economic and political dependence on Russia has been exacerbated as their problems with transport trajectory and the absence of buyers in their vicinity forced them to sell their gas underpriced to one country; These agreements were economically expensive and cost Turkey billions of dollars." "MAVİ AKIM PROJESİ: Bir Enerji Stratejisi ve Stratejisizliği Örneği" (The Blue Stream Project: A case study of energy strategy and the absence of one) Stradigma.com, August 2003 (Our translation)

rose to 65 percent of the total but eventually declined. After these contracts were signed Turkey underwent liberalization of its gas market. In the wake of that development Turkish and non-Turkish private companies have assumed some of these contracts that were signed by BOTAŞ since 1986. Winrow notes that “by 2009 half of the gas contracted by the 1998 agreement (ie. 4 bcm/y) had been transferred to private firms. In 2012, the whole of the gas volume originally contracted in 1986 (i.e. 6 bcm/y) had been transferred to private companies. These businesses have accepted the BOTAŞ take-or-pay obligations, but have negotiated lower prices with Gazprom.”<sup>70</sup> The higher prices that BOTAŞ had to pay would later become a matter for lengthy litigation against Gazprom with limited results.

The authorities in Ankara then tried to convince Moscow to look favorably on an oil pipeline from the Black Sea city of Samsun to Ceyhan in the south in order to reduce the tanker traffic along the Straits that has been a major concern of Turkey’s since the beginning of the 1990s. Although doubtful of the feasibility of such a project Russian authorities seemingly went along and signed a framework agreement. This show of good will for a project that ultimately would be shelved because of its infeasibility allowed Russia to push for the South Stream Project. As Emre Erşen argues, this project was “launched by Russia in 2007 as a response to the EU’s Nabucco project.” Nabucco, which failed because it could not raise the necessary finances despite its ostentatious beginnings was a major move on the part of the EU, the centerpiece of its Southern Gas Corridor strategy that aimed to reduce Europe’s dependence on Russian gas and pipelines. “Although Turkey was one of the key participants of the Nabucco project, it also issued a permission to Russia in 2009 to build part of the South Stream pipeline on the Turkish exclusive economic zone (EEZ) in the Black Sea.”<sup>71</sup> The South Stream pipeline network was supposed to

deliver 63 bcm/y to Europe with four offshore lines. Winrow suggests that “this project threatened to disrupt the plans of the European Union to reduce Europe’s energy dependency on Russia by promoting the Southern Gas Corridor.”<sup>72</sup> The feasibility of this project became highly questionable though as the European Union opposed it “on the grounds that it violated the provisions of the EU’s Third Energy Package with regard to Gazprom’s ownership of the planned pipeline network and control over gas transmissions.”<sup>73</sup>

On December 1, 2014 during a visit to Ankara, Russian President Vladimir Putin surprised his hosts and the relevant public opinion when he announced that a new project dubbed Turkish Stream would replace the troubled Southern Stream. Originally planned to have four strands and then reduced to two because of European reluctance to buy gas from this project, Turkish Stream is to transport the gas via Turkey to Greece and Bulgaria. It would be in service by the end of 2019 but on a much reduced scale. The project ran into a lot of difficulties and negotiations were suspended prior to the downing of the Russian jet. When the reconciliation process started, work on Turkish Stream also accelerated. Turkish Stream is 2,100 kilometers shorter than the South Stream and therefore represents considerable savings for the Russian economy that is under the pressure of Western sanctions.<sup>74</sup>

The project consists of two pipelines with a capacity of 15.75 bcm/y each that will have maritime sea and land parts. The maritime stretch of the pipeline will be constructed by the Russian Federation and the pipelines on the land will be owned by a Turkish company.<sup>75</sup>

According to Demirci who highlights the fact that the agreement does not stipulate lower prices for the gas that Turkey will import, the terms of the agreement are more

<sup>70</sup> Gareth Winrow, *Turkey’s Energy Aspirations*, op. cit., p. 6

<sup>71</sup> Erşen, op. cit., p.2

<sup>72</sup> Winrow, “Turkey and Russia: The Importance of Energy Ties”, p. 19

<sup>73</sup> *ibid.*, pp. 19-20

<sup>74</sup> So far the most comprehensive report on TurkStream is the one prepared by EDAM and authored by Sinan Ülgen, Gürkan Kumboğlu, Mitat Çelikpala, Ahmet K. Han and Zafer Öztürk. [http://edam.org.tr/wp-content/uploads/2017/11/turkstream\\_report\\_eng.pdf](http://edam.org.tr/wp-content/uploads/2017/11/turkstream_report_eng.pdf) “Turkey will be in need of additional sources of natural gas supply after 2020 that exceeds the supply capacity of TurkStream. By 2025, the shortfall – if potential supplies from TurkStream are to be excluded - will be around 16 bcm under the business as usual scenario and 37 bcm under the gas scarcity scenario. For 2035, the shortfall will have reached 24 bcm under the business as usual scenario and more than 40 bcm for the gas scarcity scenario. It is clear that under these circumstances, Turkey will greatly benefit from the 15.75 bcm to be supplied from TurkStream. Turkey may even want to augment its purchasing commitments from TurkStream in the years following 2025.” P. 8

<sup>75</sup> Mehmet Cem Demirci, “Türk Akımı mı? Rus Akımı mı? Boru hattı en çok kime yarıyor?”, euronews, 28 January 2019, <https://tr.euronews.com/2019/01/28/turk-akimi-mi-rus-akimi-mi-dogal-gaz-boru-hatti-en-cok-kime-yariyor>

favorable to Russia. “Commercial terms identical to the ones that obtain for the Western Pipeline will still be valid. In this case, Russia will not pay the transit fees that it pays to Ukraine for the Western line and will collect higher profits from a direct transaction... In addition to this Russia guards the right to unilaterally cancel Maritime-2 and land-2 pipelines that will be used for export to Europe... Furthermore, Gazprom is under no obligation to obtain permission, consent or license from Turkey for the transit of gas to third countries...” The economic assessment of the project prepared by the Centre of Economics and Foreign Policy Studies (EDAM), shows that a the Turk Stream project will contribute around an additional \$546 million to Turkey’s GDP<sup>76</sup>. Considering the fact that 37% of Turkey’s current account deficit is caused by energy demand.<sup>77</sup> Demirci’s assessment is more pessimistic in terms of the relative benefits accrued to the two parties: “(IN short), Moscow managed to put in place a wise project that bypasses Ukraine and increases Turkey’s dependence on gas supplies from Russia with a cost cutting project, by using Turkey’s own EEZ”.<sup>78</sup>

One can add that by successfully pushing for Turkish Stream, Russia also wanted to protect its dominance over European gas markets. In this context Turkey does not have similar interests with Russia. Turkey’s interest is in diversification of supply lines for the lucrative and big European markets

and use this to enhance its own energy security and lessen her dependence on Russia. Recently, Ankara began to buy larger amounts of American and Egyptian LPG and reduce the share of Russian gas in its energy import bill. The quest for diversification received strong backing from Western countries as well. Early on, “both the Baku-Tbilisi-Ceyhan (BTC) oil pipeline and Baku-Tbilisi-Erzurum (BTE) natural gas pipeline which became operational in the 2006-2007 period received strong backing from Western leaders mainly because they were perceived as key geopolitical instruments in limiting the traditionally strong Russian influence in the Caspian region.”<sup>79</sup>

In addition to the unsuccessful Nabucco that was meant to be the centerpiece of the EU’s SGC, Turkey cooperated with Azerbaijan on the TANAP (Transanatolian Pipeline) project. The pipeline that will transport the gas from the Şahdeniz-2 field of Azerbaijan is 1850 km long and will have an initial capacity of 16bcm/y of which 6 bcm will be for Turkey’s domestic use and 10 bcm for European markets. With additional investments the capacity can be raised to first 24 bcm/y and then to 31 bcm/y.<sup>80</sup> The 10 bcm designated for Europe will be transferred to Europe through the TAP (Trans Adriatic Pipeline) that is being constructed and will traverse Greece, Albania and Italy.

<sup>76</sup> [http://edam.org.tr/wp-content/uploads/2017/11/turkstream\\_report\\_eng.pdf](http://edam.org.tr/wp-content/uploads/2017/11/turkstream_report_eng.pdf) “In addition to the contributions that TurkStream is set to provide for Turkey’s energy supply security, it should be underlined that the project will also generate other economic benefits, during its construction and operation phase, for the Turkish economy. This study analyzed the economic impact of the on shore construction part of the project. It was demonstrated that based on an investment expenditure of around \$ 1 bn, this task will generate close to 13500 direct, indirect and induced jobs, around \$100 million of additional household income and a contribution to Turkey’s GDP of around \$ 546 million. These positive economic impacts are due to be augmented by the yearly economic benefits derived from the operation of the pipeline”

<sup>77</sup> <https://www.tcmb.gov.tr/wps/wcm/connect/TR/TCMB+TR/Main+Menu/Istatistikler/Odemeler+Dengesi+ve+Ilgili+Istatistikler/Odemeler+Dengesi+Istatistikleri/>

<sup>78</sup> İbid., “Anlaşmada Türkiye’ye satılacak doğal gazda indirim yapılacağına dair herhangi bir hüküm bulunmamaktadır. Aksine, anlaşmanın uygun bulunduğu kanunun gerekçesine göre Batı Hattı için geçerli olan ticari koşullar aynen geçerliliğini korumaya devam edecektir. Bu durumda Türk Akımı ile Rusya, Batı Hattı için Ukrayna’ya ödeyeceği doğal gaz transit ücretini ödemediği Türkiye’ye doğal gaz satacağı için daha fazla kar elde edecektir... Rusya Avrupa’ya ihraç için kullanılacak Deniz-2 ve Kara-2 boru hatlarını tek tarafı olarak iptal etme hakkına sahiptir. Ayrıca, anlaşmada ismi açık bir şekilde Deniz-2 ve Kara-2 boru hatlarının iştiraki olarak zikredilen Gazprom Şirketi, bu hatlar üzerinden üçüncü ülkelere yapılacak gaz transitini için Türkiye’den herhangi bir izin, onay veya lisans almaya ihtiyaç duymayacaktır. Rusya Ukrayna’yı baypas ederek, Türkiye’yi doğal gaz tedarikinde, daha ucuza mal ettiği bir proje ile daha fazla kendisine bağlayarak ve karşılığında büyük bir taviz vermeden Türk Münhasır Ekonomik Bölgesini kullanarak akıllıca bir projeyi hayata geçirmiştir.”

<sup>79</sup> Erşen, op. cit., p.6

<sup>80</sup> <http://www.socar.com.tr/kurumsal-iletisim/haberler/2019-haberler/2019/03/12/tanap-azerbaycan-dan-gelen-gazi-avrupa-sinirina-tasimaya-hazirlaniyor>

## b) The Nuclear Deal

Under normal circumstances it would have been unadvisable for a country so dependent on Russian gas for its energy needs to further raise this dependency. By choosing Rosatom to build and own (build-own-operate) its first ever nuclear power plant in Akkuyu, Turkey did exactly that. What some commentators consider a deepening of the cooperation on energy matters between the two countries is actually a step to further tighten Moscow's grip on Turkey's energy supplies. This particular contract was therefore heavily criticized and the Union of Chambers of Turkish Architects and Engineers went to court raising issues about location and price setting mechanisms. Ultimately the government cancelled the bidding and granted the concession through an intergovernmental process. Mitat Çelikpala argues that despite the validity of the arguments concerning the nature of the deal, the price of the project and the all-important issue of energy dependency, the fact is that the Russian bid was the only one extended at the time.<sup>81</sup>

The agreement for the construction of the Akkuyu NPP was signed on 12 May 2010. The estimated cost of the project is \$20 billion<sup>82</sup>. The plant is composed of four 1200-megawatt reactors that was expected to produce close to 10 percent of Turkey's electricity needs as of 2010 once it is fully operational. By 2030 it is estimated that 6% of Turkey's energy needs will be provided by Akkuyu. Although the ground breaking ceremony already took place and the Turkish government extended further concessions to Rosatom, including the building of a port facility<sup>83</sup>, there are still outstanding security and financial matters.

In their 2016 report, EDAM raised questions about Akkuyu's

potential safety and security risks; the construction of the plant is estimated to take five years and its technical life is expected to be 60 years. During the first 25 years of the plant's existence Rosatom will *own* the plant. This setup requires a stable relationship with Russia until 2080. It is important to remember that Rosatom had stopped the preparations for construction work as relations between Moscow and Ankara worsened after the downing of a Russian jet<sup>84</sup>. The fact that the project is located in a hazardous zone both geologically and geopolitically highlight the relevance and importance of security concerns<sup>85</sup>.

Rosatom is responsible to provide 51% of the seed investment of \$11-13 billion<sup>86</sup>. A consortium of three Turkish companies were supposed to invest the remaining 49% but recently they opted out of the project. In 2017 the Russian side asked and received a particular status, not stipulated in the original contract, called Strategic Status. Accordingly they received on top of the original cost-free provision of the plot over which the plant will be built, tax exemptions and further incentives. The plant is supposed to have an economic life of 60 years. For 15 years there is a purchasing guarantee for 70% of the electricity produced by the reactors at an average price overtime of 12.35 cent/kWh. At the end of the 15 year period prices will be determined by the market.

In addition to environmental concerns and the fact that Akkuyu is situated on a Faultline, there were objections in Turkey to the building of Akkuyu because of the ownership structure. That a Russian company would fully own the plant was considered too big a concession. Two further developments, both of which not stipulated in the original

<sup>81</sup> Mitat Çelikpala, "Rusya Gazı Keser mi?": Son Gelişmeler Işığında Türkiye-Rusya Enerji İlişkilerine Bakmak, Kuşku ile Komşuluk, Evren Balta, Gencer Özcan, Burç Beşgül, eds., p 213

<sup>82</sup> There could be a cost overrun by about 34% from the initially planned cost of \$18.7 billion to \$ 25 billion – EDAM Akkuyu

<sup>83</sup> Akkuyu Nükleer Santralin Limanı Haziran Ayında Açılacak (The Port of Akkuyu NPP will start operations in June), Borsa Zamanı, <https://www.borsazamani.com/ekonomi/akkuyu-nukleer-santralin-limani-haziran-ayinda-acilacak-h7165.html>; the most important journalistic piece on the matter was by Turkey's foremost investigative financial columnist Çiğdem Toker, "Rusya'nın Akkuyu'da Liman Planı" (Russia's Plan for a Port in Akkuyu), 27 March 2019, <https://www.sozcu.com.tr/2019/yazarlar/cigdem-toker/rusyanin-akkuyuda-liman-planı-4142795/>

<sup>84</sup> <https://www.reuters.com/article/mideast-crisis-turkey-russia-nuclear-idUSL8N13Y31G20151209>

<sup>85</sup> "Turkey, is a country in a dangerous neighbourhood and continues to face internal and external threats emanating from both state and non-state actors. The nation's prospective NPP may be attractive targets for its rivals in the region, their proxy terror organizations, or other terrorist and militant groups aiming to harm Turkey or access the sensitive materials and information that the NPP contains." Ergun, D., & Kasapoglu, C. (2015). "Securing Turkey's Prospective Nuclear Energy Program: A Strategic Nuclear Security Risk Analysis" in Sinan Ülgen, ed. Nuclear Security: A Turkish Perspective, (EDAM: İstanbul 2015), p.39 [http://edam.org.tr/wp-content/uploads/2015/01/edam\\_nucphysec2015\\_full.pdf](http://edam.org.tr/wp-content/uploads/2015/01/edam_nucphysec2015_full.pdf)

<sup>86</sup> The information in this section is from Küresel Gündem: Akkuyu'da Türkiye Rusya'ya liman mı Verdi? <https://www.gazeteduvar.com.tr/video/2019/04/08/kuresel-gundem-erdogannin-cantasinda-suriye-ve-akkuyu-var/>

contract raised further concerns. The first one was the change of contractor that would build the reactors. The original contractor [JSC Atomstroyexport](#), a government controlled contractor was replaced by [titan2.ru](#) that is a private company, a clear violation of the original contract's stipulation. The second major problem as alluded earlier is the changes made on the contract on March 28, 2019. Aydın Sezer argues<sup>87</sup> that the building of a port for activities related to the functioning of the reactor is normal practice. However the changed relevant articles of the contract indicate that the activities including maritime ones that the port would be allowed to conduct would turn it into a full-fledged commercial port.

## Concluding Remarks

As befits a medium power Turkey has been consistently careful to have reasonably good relations with its historical nemesis and Cold War rival Soviet Union and then with the Russian Federation in the post-Cold War period. The two young regimes' solidarity and economic cooperation in the first half of the 20<sup>th</sup> Century despite regime and ideological differences was both exemplary and pragmatic. Even during the Cold War, economic cooperation thrived despite strategic competition and rivalry. The situation since the turn of the Century from an economic perspective is qualitatively different than the previous periods. Turkey's dependence on Russian energy, its inability to dominate any market segment in Russia with the possible exception of construction, its vulnerability to Russian sanctions and the oscillations in the fortunes of Russia render the economic relations between the two very uneven. What most of those who write about these economic relations prefer to call cooperation strike us as dependency induced as much by Turkey's insatiable appetite for energy as by strategically deficient thinking and behavior on the part of successive Turkish governments in managing these relations.

How vulnerable the Turkish economy is in this bilateral relation became all too evident when Russian President Vladimir Putin imposed harsh sanctions against Turkey after the downing of the Russian SU-24. "Russia's economic sanctions against Turkey included the abolishment of the visa-free regime which had been in effect since 2011, restrictions on Turkish investments and labor in Russia,

From a Russian perspective the Akkuyu project bears many advantages. Akkuyu is the first example for Russia to produce electricity in another country with the ability to sell that electricity from Turkey to third parties. Çelikpala suggests that the goal of the Russian Federation is to be able to market its nuclear technology globally. Akkuyu provides Russia with a perfect showcase.<sup>88</sup> What Turkey gets out of this deal or whether or not Turkey gets out of this deal as much as it should commercially or strategically, beyond the realization of its 60 year-old dream of having a nuclear power plant will be matters for debate for many years to come.

restrictions on Turkish goods exported to the Russian market, and the abolishment of charter flights to Turkey."<sup>89</sup> These sanctions highlighted how so manifestly asymmetric the "asymmetric interdependence" between Russia and Turkey was. Turkish economic interests could easily be harmed by adverse changes in Russian policy. Köstem identifies three reasons that exacerbated Turkey's vulnerability when faced with Russian sanctions: "Firstly, it was harder for Turkish exporters to find an alternative market that could replace Russia. Turkey's exports to Russia fell from US\$ 5.9 billion in 2014 to US\$ 3.6 billion in 2015, and to US\$ 1.7 billion in 2016, and recovered to US\$ 2.7 billion in 2017. Secondly, it was very difficult to substitute Russian tourists...Finally, it was almost impossible to do without natural gas imports from Russia and immediately find alternative sources of energy. Russia supplied almost 55% of Turkey's gas needs." Of these three vulnerabilities only one has been partially addressed. As we have shown the ratio of Russian gas in Turkey's gas imports dropped to 40% in 2018.

This picture suggests that Turkey cannot rely on its trade with Russia and on the Russian market, particularly given the composition of its export bill, for economic growth. In the near future that composition or Russian demand for Turkey's industrial goods are highly unlikely to change much either. Therefore, Russia's market by itself is too small to substitute for Turkey's major markets in Europe. After all, even after the great leap forward in diversifying Turkey's economic relations and her markets during the first decade of the

<sup>87</sup> *ibid.*

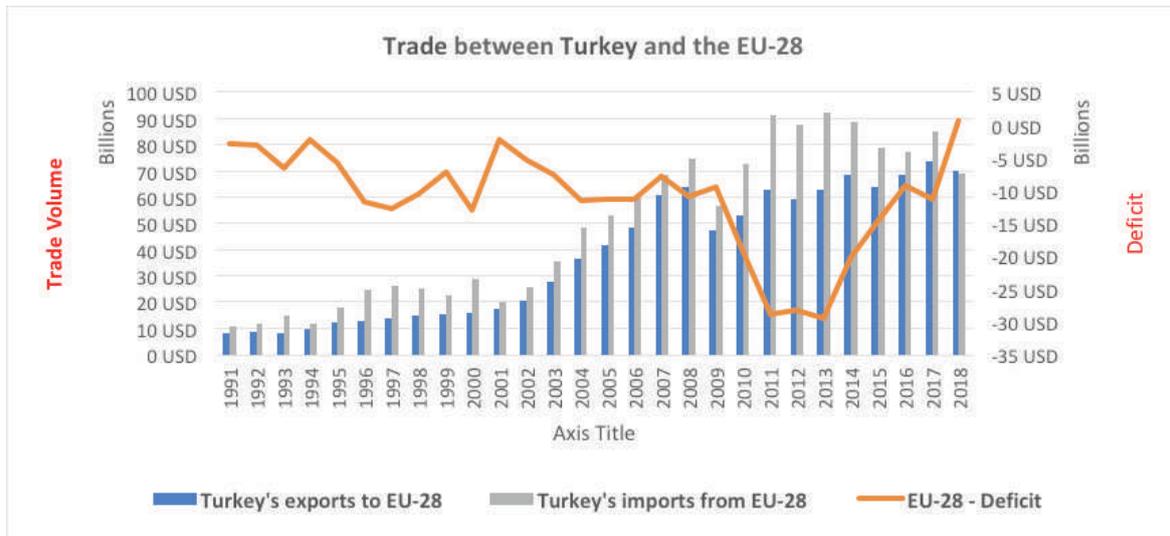
<sup>88</sup> Çelikpala, *op. cit.*, p. 212

<sup>89</sup> Köstem, *op. cit.*, p. 13

21<sup>st</sup> Century, the EU still accounts for 50% of the country's overall trade volume. Turkey exported nearly \$70 billion to the EU in 2018 and imported nearly as much. The trade

balance between Turkey and the EU-28 is therefore not just manageable but currently looks favorable for Turkey.

**Figure 15: Trade between Turkey and the EU**



Source: Own elaboration based on calculations from TUIK data (2018).

Although portrayed as big investments, the new gas pipelines and Akkuyu Nuclear project are not sufficient enough to bring vast economic resources for Turkey to consider Russia as an alternative market or a source of investment to the EU. All in all Turkey's well established economic ties both in trade and FDI to major European countries will be dominating its economic development perspective for a long time to come. Furthermore, Turkey's ties to the Western world financially and economically as well as its comatose but still relevant candidacy for membership in the EU or its institutional links to European institutions as well as NATO combine to cushion it from economic crises. They provide reassurance to investors that once Turkey's domestic political problems and rule of law deficit are overcome the country will be an attractive market as well as a target for investment.

It is in this context that one must assess the current strategic rapprochement between Turkey and Russia. As analyzed in detail in other articles of this report, Turkey's relations with its Western allies have deteriorated considerably since the botched coup of 2016. The outstanding issues with the United States in particular such as the residence of the alleged mastermind of the coup Fethullah Gülen in the USA and the problems with his extradition, the US alignment with and arming of the PYD/YPG (Syrian extensions of Turkey's nemesis the PKK) in Northeastern Syria, the diversion of views and policies towards Syria, Iran and Israel are

weighing heavily on the relations. The imminent delivery of S-400 missiles and the declared American response to such a delivery -the termination of Turkey's participation in the F-35 production network; the non-delivery of F-35s and the US Congress' resolution to subject Turkey to CAATSA sanctions- all point to a major crisis in Turkey's strategic identity and its posture in the Transatlantic Alliance. The economic fallout from such a development would be too great for Russia to even contemplate bailing Turkey out.

Given this reality, the debates over Turkey's likely attempts to form new economic partnerships to replace the one it has with the West appears to stand artificial. A comparison between changes in the volume of Turkey's trade with Russia and its other trade partners could prove the point, as it makes commercially harder for Turkey to further distance itself from the West. As the EU and the US still remain important markets and sources of FDI as well as portfolio investment for Turkish companies and the country, replacing Turkey's traditional trade partnerships with Russia and Moscow-led organizations does not seem a promising option.

That is as much part of the reality of Turkey-Russia economic relations as the "asymmetric interdependence" that defines these and set the limits to Turkey's search for alternative economic havens that can help her in its quest for sustainable development.



Foreign Policy & Security 2019/10

July 2019

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# THE ECONOMICS OF TURKEY-RUSSIA RELATIONS

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