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How the Iran Conflict Is Reshaping Turkey's Economy and Geopolitics

By

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Executive Summary

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Global and Regional Economic Risks

- ✦ The IMF warns that renewed conflict in the Middle East could raise commodity prices, disrupt supply chains, tighten financial conditions and fuel inflation, while increasing food insecurity and economic instability in vulnerable countries.
- ✦ The conflict has already affected economies representing nearly \$4 trillion in output. For Turkey, it creates higher energy and inflation risks but also opportunities to expand trade, logistics, investment and regional security partnerships.

Domestic Economic Pressures: Inflation, the Budget and the Current Account.

- ✦ Higher oil prices initially disrupted Turkey's disinflation process, although easing energy costs helped reduce annual inflation to 32.1% in June. Inflation nevertheless remains well above the central bank's 26% target.
- ✦ Lower inflation has strengthened expectations of an interest rate cut later this month, though policymakers are expected to remain cautious given persistent price pressures.
- ✦ Rising energy subsidies and fuel-tax cuts have weakened public finances, with the budget deficit reaching 1.06 trillion lira in the first five months of 2026 and interest payments rising by more than 50% year-on-year.
- ✦ Prolonged high oil prices could undermine the government's fiscal consolidation efforts and broader macroeconomic stabilisation programme.
- ✦ Turkey's external position has become more vulnerable as it imports over 90% of its crude oil and 96% of its natural gas, making the current account highly sensitive to higher energy prices.
- ✦ Analysts estimate that every \$10 increase in oil prices adds roughly \$4.5–5 billion to the current account deficit, while more than \$100 billion in short-term external debt leaves Turkey dependent on continued foreign capital inflows.

Strategic Opportunities: Defence Industry and Trade Routes

- ✦ Turkey's defence industry is benefiting from rising geopolitical tensions, with defence exports projected to exceed \$11 billion in 2026, up from \$1.67 billion in 2016. Turkish firms also secured \$8 billion in export agreements at the SAHA 2026 defence exhibition.
- ✦ Europe is increasingly viewing Turkey as an indispensable NATO partner, seeking closer defence cooperation as Ankara's military capabilities, strategic location and defence industry gain importance amid growing security challenges.
- ✦ The Hormuz crisis has renewed interest in alternative trade corridors, including the Middle Corridor and the Iraq Development Road, enhancing Turkey's role as a regional logistics and transit hub.
- ✦ Positioned at the intersection of Europe, Central Asia and the Gulf, Turkey is well placed to capture redirected trade, investment and supply-chain flows while strengthening its geopolitical influence.

Introduction

The IMF has warned that renewed conflict in the Middle East poses the most immediate risk to the global economy, with the potential to raise commodity prices, disrupt supply chains, tighten financial conditions and

fuel inflation. A prolonged conflict could also worsen food insecurity, increase social instability in vulnerable economies and intensify exchange-rate pressures.

For the Middle East and North Africa, the shock is already unusually broad. [According to analysis by Asharg Business with Bloomberg](#), the Iran conflict has affected economies worth nearly \$4 trillion, equivalent to around 70% of regional GDP and 3% of global output. Energy exports, trade routes, tourism, shipping and investment have all come under pressure, while recovery depends heavily on the reopening of the Strait of Hormuz, the restoration of energy exports and the prevention of renewed regional escalation.

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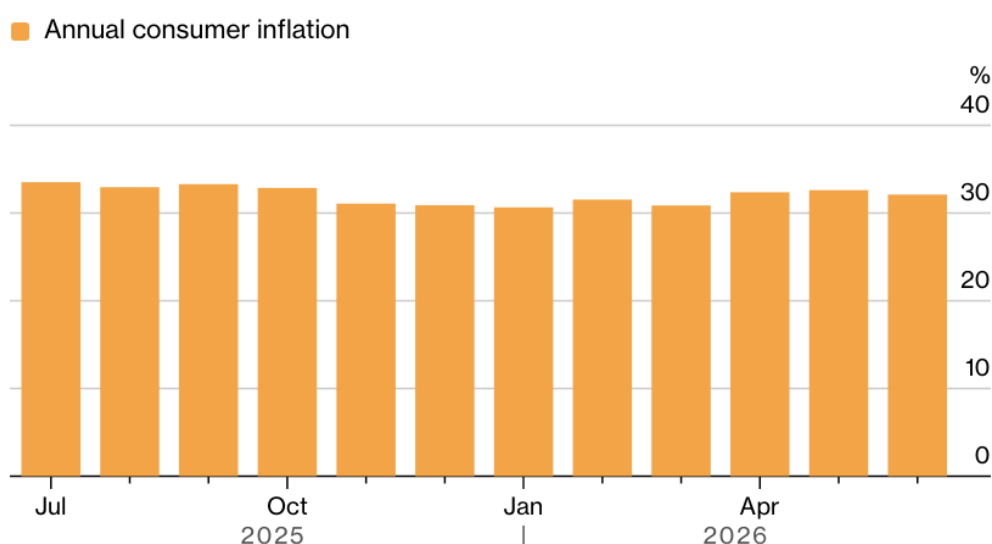
For Turkey, the conflict presents a complex mix of domestic economic pressures and strategic opportunities. As a major importer of oil and gas, Turkey is highly exposed to higher energy prices. The conflict has complicated the central bank's disinflation strategy, added pressure on public finances and widened external vulnerabilities. At the same time, disruptions across the Gulf may create opportunities for Turkey to capture redirected trade, logistics, investment and security partnerships.

The Economic Impact for Turkey

The economic impact is being transmitted through three main channels: inflation, the budget and the current account.

First, higher oil prices initially [disrupted Turkey's disinflation process](#), pushing monthly inflation above 4% in April and widening the gap between the central bank's inflation target and public expectations. However, easing energy prices helped slow monthly inflation to 0.99% in June, the weakest increase in six months, while annual inflation edged down to 32.1% from 32.6% in May, the first decline since the Iran conflict began. Despite the improvement, [inflation remains well above the central bank's 26% year-end target](#), with most economists expecting it to finish the year just below 30%. The moderation has fuelled expectations of a gradual easing in monetary policy later this month, although the central bank is likely to remain cautious given persistent inflation risks.

Figure 1: Annual Price Growth



Source: [Bloomberg](#)

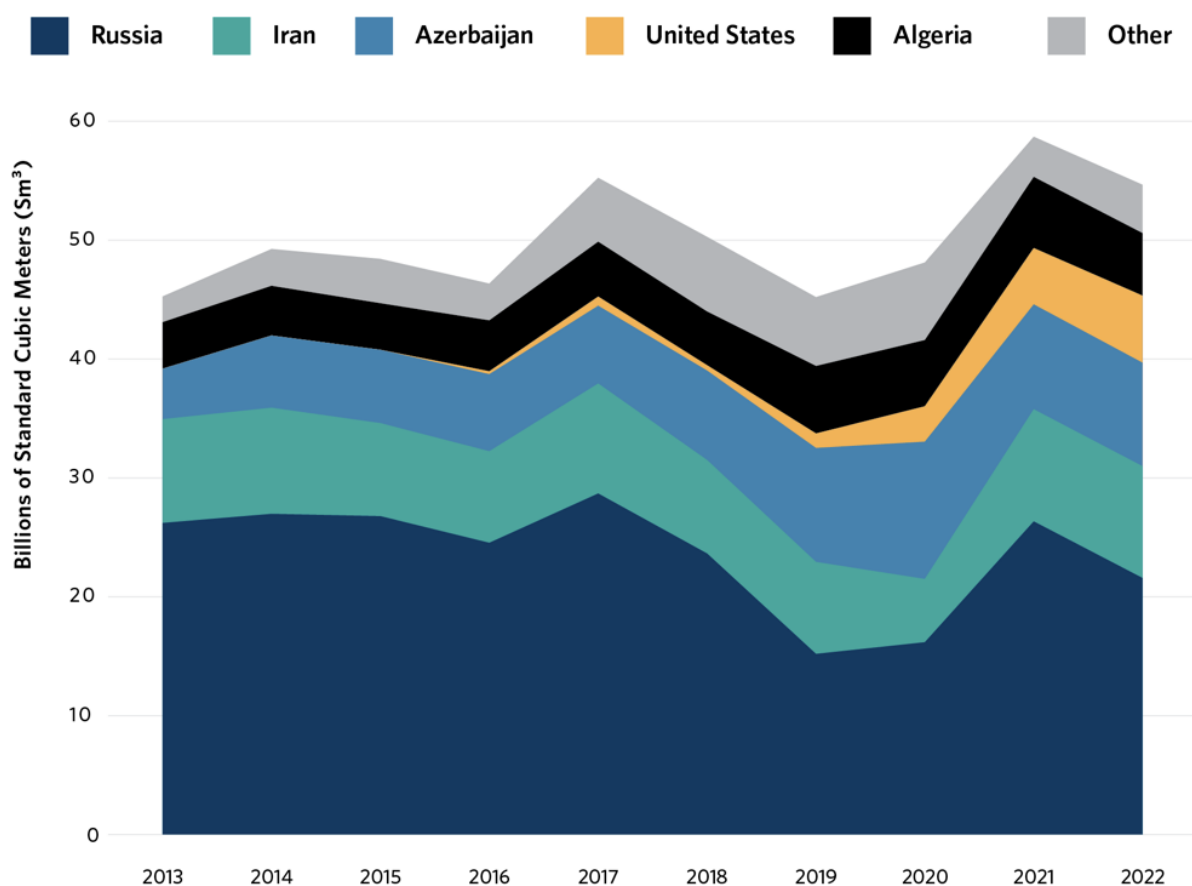
Second, at the fiscal level, fuel-tax cuts and rising energy subsidies are weakening the budget position and putting pressure on Mehmet Şimşek's stabilization programme. With rising interest costs and larger subsidy bills, analysts warn that prolonged high oil prices could undermine Turkey's fiscal consolidation efforts and weaken the credibility of its broader macroeconomic stabilisation programme. [The government posted a 298.2 billion](#)

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[lira \(\\$6.4 bn\) budget deficit in May](#), reversing a surplus a year earlier, as tax revenues declined and public spending increased. The cumulative budget deficit reached 1.06 trillion lira in the first five months of 2026, while interest payments surged by over 50% year-on-year, highlighting the growing cost of maintaining tight monetary policy. The weaker fiscal balance adds to concerns over Turkey's macroeconomic stability as policymakers continue to balance inflation control with slowing economic activity.

Third, Turkey's external position has also become more vulnerable. As the country imports over 90% of its crude oil and 96% of its natural gas, higher energy prices are expected to widen the current account deficit significantly. Analysts estimate that every \$10 increase in oil prices adds [\\$4.5-5 billion to the deficit](#), prompting forecasts of a \$45 billion current account deficit in 2026. At the same time, Turkey faces over \$100 billion in short-term external debt repayments, leaving the economy highly dependent on continued foreign investor confidence and sustained macroeconomic stability.

Figure 2: Origins of Turkey's Imported Natural Gas



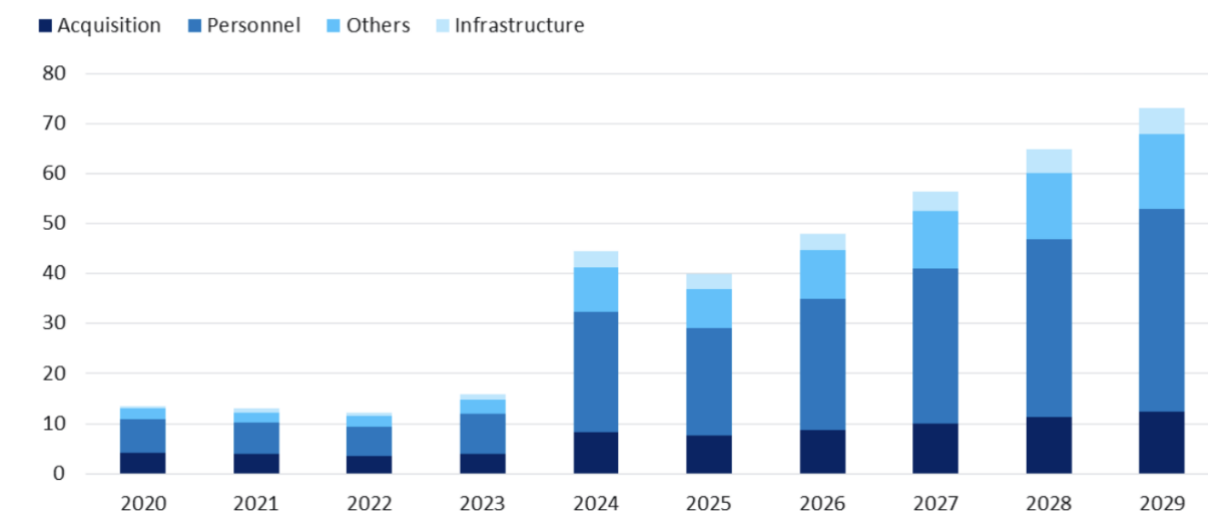
Source: [Carnegie Endowment](#)

Turkey's Defence Industry Drives Strategic Influence

Yet the conflict also creates strategic openings. Turkey's defence industry has emerged as one of the main beneficiaries of rising geopolitical tensions. [Defence exports are projected to exceed \\$11 billion in 2026](#), compared with \$1.67 billion in 2016, reflecting a decade of investment in domestic production. At the SAHA 2026 defence exhibition, Turkish firms signed \$8 billion worth of export agreements, highlighting growing international demand for Turkish military technology and strengthening the country's position in the global defence market.

Europe is reassessing its relationship with Turkey as rising geopolitical tensions, the wars in Ukraine and the Middle East, and uncertainty over the US security commitment elevate Ankara's strategic importance. Once viewed as an increasingly authoritarian and difficult ally, Turkey is now seen as an indispensable NATO partner, with its military capabilities, defence industry, and strategic location making it central to Europe's emerging security architecture. Ankara is leveraging this position to seek closer EU ties, greater defence cooperation, and expanded access to European technology, finance, and markets

Figure 3: Turkey's Defense Budget Breakdown (\$B), 2020-29



Source: [GlobalData](#)

Middle Corridor and Trade Routes

Turkey may also benefit from the redesign of regional trade routes. The Hormuz crisis has increased interest in alternative corridors, strengthening the relevance of projects such as the Middle Corridor and the Iraq Development Road. As Gulf states reassess supply chains and security partnerships, Turkey is well positioned to expand its role as a logistics, transit and investment hub.

For Europe in particular, the crisis has reinforced the need to diversify trade and energy routes away from Hormuz. This has renewed interest in overland connectivity projects, most notably the Middle Corridor (Trans-Caspian International Transport Route) linking China and Europe through Central Asia, the Caucasus and Turkey, as well as the Four Seas Initiative, which aims to connect the Persian Gulf with the Mediterranean and Black Sea via Iraq, Syria and Turkey.

Turkey is uniquely positioned to benefit from this shift. Situated at the intersection of both corridors, Ankara is strengthening its role as a strategic transit and logistics hub linking Europe, Central Asia and the Gulf. As businesses and governments seek alternatives to vulnerable maritime routes, Turkey stands to capture a larger share of regional trade, investment and supply-chain flows while reinforcing its geopolitical importance. The convergence of the Ukraine war, Red Sea disruptions and the Iran conflict is accelerating this process, making Turkey an increasingly indispensable gateway between Europe and Asia.

Conclusion

Overall, the Iran conflict is both a macroeconomic shock and a geopolitical opening for Turkey. In the short term, it raises inflationary, fiscal and external risks, making the stabilisation programme more difficult to maintain. In the longer term, however, it could strengthen Turkey's role in defence, regional connectivity and Gulf economic partnerships. Whether Ankara can convert disruption into strategic advantage will depend on how long the conflict lasts, whether energy markets stabilise and whether Turkey can preserve investor confidence while managing the domestic costs of the shock.