PEASANTS, BANKERS AND THE STATE:
FORGING INSTITUTIONS IN NEOLIBERAL TURKEY

By

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ABSTRACT

The recent rediscovery of institutions in the study of international development has drawn considerable attention to macro arrangements, but sparked much less interest in mid-range, sectoral institutions and how they are reshaped under dynamic domestic and nondomestic constraints. This study joins the few examples of this latter research focus by offering a typology of sectoral institutional pathways in contemporary late developers. The typology incorporates four variables: pre-existing institutions, international norms, technocratic engineering, and coalition politics. It is argued that from careful pairings of these variables, for which the sectoral effects of internationalization and the intensity of domestic political competition are used as the main criteria, it is possible to deduce distinct ideal-typical pathways: insulated accommodation, insulated innovation, negotiated accommodation, and negotiated innovation.
The typology models the complexity of institutional trajectories, but it cannot predict concrete institutional profiles. Its value is in providing guidance for empirical analysis. The bulk of the study is devoted to applying this framework to the evolution of Turkey’s fiscal, financial and agricultural regimes of governance from 1980 to 2007. This comparative exercise unlocks several empirical mysteries at once: the failure of Turkish governments in the 1990s to readjust the novel fiscal and banking regimes to preempt the perils of democratic instability and rapid financial integration; the surprising persistence of populist-corporatist forms of market governance in agriculture despite the neoliberalism of the 1980s and 1990s; the stark divergence in reform outcomes across these regimes during the intense restructuring efforts of the 2000s; some odd instances of institutional complementarity; and the exotic twists in the fortunes of Turkish peasants and bankers throughout the entire period. A separate chapter extends the typology to four non-Turkish cases to gain comparative insight into the different types of reshaping: Chinese banking, South Korean corporate governance, Mexican agriculture, and Argentine labor markets. Among the main findings of the study are the need to get beyond dichotomous notions of institutional continuity and change, the problematicity of the quest for good institutions via externally-inspired reforms, and the value of mid-range institutional analysis for understanding shifts in collective fortunes and preferences under processes of macro-transformation.
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Ali Burak Güven

Toronto, Ontario
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<td>Adalet ve Kalkınma Partisi / Justice and Development Party</td>
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<tr>
<td>ANAP</td>
<td>Anavatan Partisi / Motherland Party</td>
</tr>
<tr>
<td>AP</td>
<td>Adalet Partisi / Justice Party</td>
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<tr>
<td>ARIP</td>
<td>Agricultural Reform Implementation Project</td>
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<td>BDDK</td>
<td>Bankacılık Düzenleme ve Denetleme Kurumu / Banking Regulation and Supervision Agency</td>
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<td>BIS</td>
<td>Bank for International Settlements</td>
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<td>CHP</td>
<td>Cumhuriyet Halk Partisi / Republican People’s Party</td>
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<td>DIE</td>
<td>Devlet İstatistik Enstitüsü / State Institute of Statistics (TÜİK after 2005)</td>
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<tr>
<td>DIS</td>
<td>direct income support</td>
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<tr>
<td>DP</td>
<td>Demokrat Parti / Democratic Party</td>
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<td>DPT</td>
<td>Devlet Planlama Teşkilatı / State Planning Organization</td>
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<tr>
<td>DSP</td>
<td>Demokratik Sol Parti / Democratic Left Party</td>
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<tr>
<td>DYP</td>
<td>Doğru Yol Partisi / True Path Party</td>
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<tr>
<td>EBF</td>
<td>extra-budgetary fund</td>
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<tr>
<td>EU</td>
<td>European Union</td>
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<tr>
<td>HM</td>
<td>Hazine Müsteşarlığı / Undersecretariat of Treasury; often referred to as “Treasury” (Between 1983 and 1994, HDTM: Hazine ve Dış Ticaret Müsteşarlığı / Undersecretariat of Treasury and Foreign Trade)</td>
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<tr>
<td>IFI</td>
<td>international financial institution</td>
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<td>IMF</td>
<td>International Monetary Fund</td>
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<td>ISI</td>
<td>import-substituting industrialization</td>
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<td>MHP</td>
<td>Milliyetçi Hareket Partisi / Nationalist Action Party</td>
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<td>MÜSİAD</td>
<td>Müstakil Sanayici ve İşadamları Derneği / Independent Industrialists and Businessmen Association</td>
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<td>Acronym</td>
<td>Full Form</td>
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<tr>
<td>OECD</td>
<td>Organisation for Economic Cooperation and Development</td>
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<td>PSBR</td>
<td>public sector borrowing requirement</td>
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<td>PSE</td>
<td>producer support estimate</td>
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<td>RP</td>
<td>Refah Partisi / Welfare Party</td>
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<td>SHP</td>
<td>Sosyal Demokrat Halkçı Parti / Social Democratic Populist Party</td>
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<tr>
<td>SOE</td>
<td>state-owned enterprise</td>
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<td>SPK</td>
<td>Sermaye Piyasası Kurulu / Capital Market Board</td>
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<tr>
<td>STB</td>
<td>Sanayi ve Ticaret Bakanlığı / Ministry of Industry and Commerce</td>
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<tr>
<td>TBB</td>
<td>Türkiye Bankalar Birliği / Turkish Banks’ Association</td>
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<tr>
<td>TCMB</td>
<td>Türkiye Cumhuriyet Merkez Bankası / Central Bank of the Republic of Turkey; often referred to as “Central Bank”</td>
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<td>Tarım ve Köyİşleri Bakanlığı / Ministry of Agriculture and Rural Affairs; often referred to as “Ministry of Agriculture”</td>
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<td>TMO</td>
<td>Toprak Mahsulleri Ofisi / Turkish Grain Board</td>
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<td>TMSF</td>
<td>Tasarruf Mevduat Sigorta Fonu / Savings Deposit Insurance Fund</td>
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<td>Türkiye Odalar ve Borsalar Birliği / Turkish Union of Chambers and Commodity Exchanges</td>
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<td>TSE</td>
<td>total support estimate</td>
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<td>TSK</td>
<td>Tarım Satış Kooperatifleri / Agricultural Sales Cooperatives</td>
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<td>Türkiye Ziraat Odaları Birliği / Turkish Union of Chambers of Agriculture</td>
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<tr>
<td>WTO</td>
<td>World Trade Organization</td>
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<tr>
<td>ZMO</td>
<td>Ziraat Mühendisleri Odası / Chamber of Agricultural Experts</td>
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CHAPTER ONE

INTRODUCTION

In late 2001, months after the collapse of the Turkish financial system precipitated the severest economic crisis in the country’s postwar history, numerous Turkish bankers were in jail. Their assets confiscated and their licenses revoked, these former bank owners and executives were now tried on charges of fraud and organized crime. While their fall from repute and subsequent incarceration triggered media frenzy, a similar story received scant attention. Of the nearly one million crisis-hit farmers across the country who had defaulted on their credit debts to Ziraat, the state agricultural bank, some two thousand from neighboring villages of the small town of Havran in Western Anatolia were facing short-term sentences due to some judicial technicality. But because Havran’s tiny penitentiary could accommodate only sixty inmates at a time, they were taking turns to pay their debt, almost literally, to society.¹

This was not the first of peasants’ and bankers’ shared experience. Oddly enough, the 1990s, otherwise known as Turkey’s lost decade, had been kind to both social groups. Turkey’s smallholders had benefited from generous price, input and credit subsidies as fragile coalition governments throughout the decade courted rural votes with old school populism. Bankers’ lot had improved more substantially. The financial revolution of the 1990s had seen the proliferation of domestic retail banks, whose profits soared at a juncture of international openness, high inflation, jumbo fiscal deficits, and lax

regulations. But now, as the ax fell on the economy, peasants and bankers were suddenly the most vulnerable economic actors.

For postcrisis reformers, these exotic twists in social fortunes were symptoms of the same anomaly that derailed Turkey’s market transition in the first place. During the 1980s and 1990s, the official postcrisis narrative insisted, Turkish governments had failed to build robust institutions that would serve as a suitable shell for the country’s persistent drive toward outward-oriented liberalization. In some sectors and policy areas, preliberal regimes were more or less preserved. In others, novel designs delivered poor coordination between social and policy actors. At the root of Turkey’s market failures was this disarray in its mechanisms of economic governance. Once the problem was identified in these terms, the solution looked straightforward: getting the institutions right. From this diagnosis followed an internationally supported recovery program, which introduced various elements of institutional reform.

This concern with institutional reform rested on a popular persuasion of our time—that poor economic performance and bad institutions go together. Today, mainstream development economics holds that the promises of domestic liberalization and international integration, the twin drivers of economic policy in late developers for the past thirty years, are unlocked only in the company of non-market arrangements that can simultaneously offer efficiency and competitiveness, cushion internal and external shocks, and mitigate social and distributive tensions—the so-called ‘good institutions.’ Certainly, there is wisdom in this view. Most late developers are afflicted with grave institutional deficiencies at all levels, which must in part account for their current economic maladies.
Yet in its normative emphasis on what is missing rather than what does indeed take place, this view also distances itself from the rich institutional histories of the past few decades. While pointing at the short supply of ‘good institutions’ in late developers, it overshoots the fact that institutional adventures are plenty. In actuality, rulers across the developing world make institutional choices of all kinds, without always claiming to seek after good or virtuous designs by this or that measure. They create brand new regimes, substantially transform existing configurations, engage in cosmetic surgeries, put old designs to new uses, or let arrangements drift and decay. At times these choices are reflected in overt reform programs; at other times they are implicit in the rough and tumble of everyday politics. Some choices bring countries closer to the sorts of arrangements contemporary economists hold in high regard; others push them farther away. In their efforts, executives are often constrained by the social forces with which they share the political landscape, but their actions always affect these forces profoundly.

It is this real world of institutions that I explore in this study. I draw on evidence primarily from Turkey by offering an in-depth analysis of institutional trajectories in two key sectors: finance and agriculture. Under the former, I focus on both the regime of public finance and the regulation of the banking sector, which, for reasons that will appear in due course, have come to be intricately linked. Under the latter, I trace the evolution of agricultural support schemes, the main instrument of market governance in the Turkish countryside.

Clearly, my focus is not on some macro-institutional conditions that receive the most attention in economic analysis, such as the regime of property rights or political accountability. Rather, I am concerned with institutions of sectoral governance—the
variety of mid-range and micro arrangements that govern particular economic sectors and policy domains. Such institutions are often legally and organizationally visible, although they might embody some informal features. Invariably, they represent clear social and strategic preferences, so they comprise important sites of political struggle. It is also meaningful to study them, for these are the most common objects of institutional reform.

The two sectors under scrutiny make good candidates for such an exploration in part because they offer a diverse range of possible scenarios. Accounting for this diversity constitutes the primary axis of my analysis. Under liberalization, Turkey’s fiscal and financial regimes displayed a considerable openness to change, with novel mechanisms emerging by the mid-1980s, to be subjected to continuous adjustments in the 1990s. In agriculture, by contrast, pre-existing arrangements largely persisted, although their effects oscillated in line with changing policy objectives. But despite their varied trajectories, these regimes proved equally detrimental to the Turkish economy, playing into its collapse in numerous ways. In turn, postcrisis reformers sought to remodel institutions in both sectors. Yet another divergence followed from these efforts. While new designs were quickly consolidated and would later prove resistant to subversion in finance, reforms were soon diluted in agriculture as pre-reform arrangements resurfaced to coexist with new ones in a hybrid institutional environment.

For students of institutions, these cases raise interesting questions. What explains such sharp variations in institutional trajectories? Why do novel designs seem more likely to emerge in some sectors than others? How do old arrangements persist in the face of macro-environmental changes? How is it possible for similarly dismal outcomes to follow from such dissimilar patterns of change? And why do some institutional reform
efforts succeed while others fail? All such questions, I believe, follow from and therefore can be more or less reduced to the broader question of how sectoral institutions are reshaped in late developers. Institutional pathways are the dependent variable of the study. I try to develop a framework that can account for the variations in sectoral institutional trajectories in an increasingly open and market-based economy.

One particular dimension of this process receives special attention throughout the study: its connections to collective interests. Regimes of sectoral governance are unique in that they rule over clearly identifiable societal interests. Here again, the cases point to a rich history. In Turkish agriculture we encounter a vast smallholder peasantry whose livelihood was initially severely challenged by neoliberal austerity, which would then recover during a long period of intense democratic competition, only to enter another phase of structural dislocation during postcrisis reform attempts. In finance, we see the waxing and waning of rentier interests amid rapid internationalization, as well as striking twists in relations with industry. Perhaps most surprisingly, in the peculiar context of the 1990s, we observe an accidental convergence of interests between peasants and bankers in support of unsustainable levels of fiscal expansion, securing synchronous transfers of income toward both groups—an oddity I have come to label ‘double redistribution’.

The way these shifts in collective fortunes overlap with shifts in sectoral regimes tells us something important about interests and institutions: that they can serve as symptoms of and vehicles for change in one another. With every major rupture in institutional configurations, Turkey’s financiers and rural producers found themselves in a different position vis-à-vis both the state and other classes. In turn, understanding the
roles these interests played in the forging of sectoral institutions at different points of that history holds the key to making sense of the politics of institutional stability and change.

This dual focus on sectoral institutions and attendant interests is inspired by the shortcomings of two major contemporary debates on late developers. On one side is what Peter Evans (2005) calls the “institutional turn” in development economics. Growing out of a widespread discontent with the neoclassical orthodoxy of the 1980s, yet quick to integrate into the dominant wisdom, this surge of interest in institutions found its most powerful expression in the refurbished policy recommendations of the IMF and the World Bank around the turn of the century as part of an expanded ‘Post-Washington Consensus.’ I shall call this mainstream variant of the institutional turn ‘neoliberal institutionalism’. It was this particular variant that gave rise to the aforementioned persuasion that derailed market transitions could be fixed via comprehensive institutional reforms. The problems with such blanket faith in the virtues of institution building, as I will discuss in the next chapter, were multifarious. As a result, it has come under heavy attack in recent years and has lost some of its allure, although it remains firmly planted at the messy center of development thinking.

I join with the critics of this position by stressing two interrelated themes on which neoliberal institutionalism remains tellingly silent, but that are nonetheless crucial to understand: the origins of ‘bad institutions’ and the variability of outcomes of institutional reform. How matrices of ineffective practices ‘stick’ on the long march to

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3 Not to be confused with ‘neoliberal institutionalism’ in international relations theory.
the market or why countries fail to arrive at prudent arrangements despite considerable institutional dynamism under lengthy episodes of restructuring remain mysteries to economic analysis. Likewise, we know little about the constellation of factors that affects institutional reform efforts so as to generate a wide range of outcomes. The evolution and postcrisis recasting of Turkey’s financial and agricultural regimes offer insight into both phenomena. My findings paint a complex picture in which voluntaristic solutions to deep-seated institutional problems are very hard to defend.

On the other side of the intellectual spectrum is a vast political science literature on market transitions, which owes its remarkable longevity to the seemingly never-ending complications that have engulfed this process. From early works on the politics of policy change to the more recent analyses of second and third generation reforms, most research in this literature has displayed a tendency toward an actor-strategic and policy-oriented perspective. Much attention has been focused upon the complexities of building reform coalitions, the effects of reform sequencing, and the role of policy networks. However, perhaps reflecting the enormity of the tasks involved in market transitions, institutional questions in this literature are invoked ordinarily at trans-sectoral and macro-political levels, and are often used to explain other phenomena. Surprisingly few studies have moved beyond the common question of institutional legacies to put forward substantive accounts of how sectoral institutions are remade during market transitions.

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A sectoral institutional focus thus also fills a gap in this diverse literature. Studying sectoral regimes opens up a scarcely explored analytical terrain with problems and relations that are not easily accessible through a policy-oriented outlook. What I propose here is not an analysis devoid of strategic action, however. The dense links between sectoral governance and collective interests prohibit that. Rather, I take the main challenge as one of historical specification—not why or whether actors’ strategies matter in the reshaping of institutions, but how and when they matter, especially given the structural constraints economic sectors face in an internationalizing economy.

1.1 The Argument

The past few decades have been a turbulent period for the developing world. Countries often experienced radical political-economic transformations at home while being exposed to dizzying sea changes abroad. Any analysis of institutional pathways in late developers will therefore encounter multiple and interacting factors. But precisely which factors are important, and what follows from their interaction? I identify four broad variables, and argue that from a careful reordering of them we can deduce distinct types of sectoral institutional reshaping. These variables are explored in greater detail in the next chapter. Here, I introduce them briefly.

(1) **Pre-Existing Institutions:** Institutionalists argue that pre-existing institutions often constrain policymakers’ choices as to future configurations: what already exists can shape what is to come. In some instances path dependence proves strong, rendering
arrangements resistant to change or favoring some designs over others. Institutional interaction or complementarity can also be a factor; the presence of an arrangement in one domain might influence institutional options in other domains.

(2) **International Norms:** Rulers also consider what is internationally acceptable at the time. In some sectors, strong, coherent norms about sectoral governance may encourage convergence upon ‘best practices’ through imitation or translation. In others, shifts in global wisdom may generate relatively diffuse, weaker norms, which may prove less inspiring. As important as the content of these norms are the channels through which they are transmitted, and the receptiveness of the domestic scene.

(3) **Coalition Politics:** This is the terrain most intensely explored by students of reform politics. It refers to a political space where rulers seek social allies to construct or broaden reform coalitions, intra-state factions clash over bureaucratic turf, and collective interests strike open and tacit bargains with incumbents and with one another to influence policy and institutional agendas. Political and organizational resources available to actors are an important factor in this process.

(4) **Technocratic Engineering:** In most late developers, market transitions coincided with the ascendance of liberal-minded, technocratic elites within state bureaucracies, who typically stand as ardent supporters of radical institutional reforms. The hallmark of technocratic engineering is the implementation of transformative blueprints with the least possible exposure to societal and other intra-state pressures.
All four of these factors regularly crop up in studies on contemporary late developers. And each, I believe, has something to contribute to institutional trajectories in any given context: they can be neither fully absent nor are they mutually exclusive. Nonetheless, they cannot be expected to apply to every context with equal force. In different sectors and at different times, some factors will naturally appear more salient in shaping institutions than others. If we can determine what renders a variable dominant or recessive, we will make important headway in accounting for institutional pathways.

I use two criteria to make this inescapably untidy determination: sectoral effects of internationalization and the intensity of domestic political competition. More formally, I am interested in two conditions: (1) whether dominant patterns of market and policy internationalization in an economy create stronger or weaker incentives for reorganization in a given sector; and (2) whether policymakers are exposed to higher or lower levels of political competition. These two conditions help sift through the four variables in the following way (Table 1.1).

A1 When country-wide patterns of internationalization create only weak incentives for reorganization of economic activity in a given sector, rulers are likely to employ a strategy of accommodation, whereby existing institutions will not be dismantled, but adapted to accommodate new policy goals. This will accord significance to pre-existing institutions.

A2 Conversely, when internationalization creates strong incentives for sectoral reorganization, rulers will be more inclined to abandon existing institutions and
search for new arrangements through *innovation*. In this quest, they will be more open to being guided by *international norms*.

**B1** Under low levels of domestic political competition, rulers may afford shaping institutions in relative *insulation* from collective actors. This will in turn facilitate *technocratic engineering*.

**B2** By contrast, high levels of political competition tend to open the policy regime to influences by contending interests and compel rulers to adopt a strategy of *negotiation* with collective actors in reshaping institutions. This will increase the significance of *coalition politics*.

![Table 1.1](A Typology of Sectoral Institutional Pathways)

<table>
<thead>
<tr>
<th>(B1) Low levels of domestic political competition</th>
<th>(A1) Weak international incentives for sectoral reorganization</th>
<th>(A2) Strong international incentives for sectoral reorganization</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>INSULATION</strong></td>
<td>ACCOMMODATION</td>
<td>INNOVATION</td>
</tr>
<tr>
<td>Pre-existing institutions</td>
<td>International norms</td>
<td></td>
</tr>
<tr>
<td>Technocratic engineering</td>
<td>Technocratic engineering</td>
<td></td>
</tr>
<tr>
<td>INSULATED ACCOMMODATION</td>
<td>INSULATED INNOVATION</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>(B2) High levels of domestic political competition</th>
<th>(A1) Weak international incentives for sectoral reorganization</th>
<th>(A2) Strong international incentives for sectoral reorganization</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>NEGOITIATION</strong></td>
<td>NEGOITIATED ACCOMMODATION</td>
<td>NEGOITIATED INNOVATION</td>
</tr>
<tr>
<td>Pre-existing institutions</td>
<td>International norms</td>
<td></td>
</tr>
<tr>
<td>Coalition politics</td>
<td>Technocratic engineering</td>
<td></td>
</tr>
</tbody>
</table>

| Pre-existing institutions                        | International norms                                      |
| Coalition politics                               | Coalition politics                                       |

11
The confluence of these variables reveals four basic ideal-typical pathways: In *insulated accommodation*, technocrats will try to adapt institutions on the ground to new policy objectives through modest adjustments and with limited input from attendant interests. In *insulated innovation* as well, technocrats’ preferences will weigh heavily, but this time they will aim at building new institutions or substantially reforming existing arrangements in the spirit of reigning international norms. In *negotiated accommodation*, incumbents will strike coalitions with social actors to redeploy pre-existing institutions in ways conducive to changing domestic priorities. In *negotiated innovation*, they will try to create new configurations by reconciling collective interests and international norms.

Of the four types, insulated accommodation is the least problematic one, for it requires minimal consultation with societal actors while saving technocrats the hassles of designing and implementing new regimes. Negotiated innovation, by contrast, is organizationally and politically the most troublesome, but also perhaps the most common of all four. Negotiated accommodation is likely to result in the least amount of institutional change, creating a synergy between pre-existing institutions and collective interests which would already normally have a stake in their persistence. Insulated innovation has the potential of leading to most substantial changes, with old institutions defenseless against reform-minded technocrats.

Some clarifications are in order. First, real-world institutional trajectories do not seamlessly fit these ideal-types. They can only be approximations: some may come very close to the predicted type; others will display only a loose resemblance; yet many may fall somewhere in between different types. This is because the contrasts between the four main variables are always relative in the real world. Technocrats may have the upper
hand in decisionmaking, but even in the thickest of authoritarian repression they cannot fully disregard social interests. Implementation of new global norms may revolutionize a sector, but some components of the pre-existing institutional regime will still survive.

Second, the typology can predict institutional pathways by indicating propensity toward a certain type, but it cannot predict the real outcomes of these pathways, that is, concrete institutional profiles. The reason must be clear: although the typology points at the factors that distinguish one pathway from another, it says nothing about how these factors are manifested in a country context and which intervening dynamics might be at work in that process. Some pre-existing arrangements will have stronger self-reinforcing properties than others. Reigning international norms, even when rulers are prepared to adopt them, might prove more feasible in one sector than the next one. The effectiveness of technocratic engineering will heavily depend on bureaucratic capacity and reform legacies in a sector. Organizational prowess, formal and informal linkages to executive circles, and the conjunctural balance of social forces within the wider polity will influence collective actors’ ability to manipulate institutional trajectories under coalition politics. In the end, from the same type of reshaping, different institutional configurations might follow in different contexts. All the typology does, then, is to provide a vantage point for empirical analysis by drawing our attention to particular variables. Concrete institutional configurations can be accounted for only through detailed case studies that will explore the different values of these variables.

Third, the criteria I employ to rearrange the four variables make some assumptions that need to be exposed at the outset. In suggesting that the choice between innovation and accommodation will depend on patterns of internationalization, I assume
it is improbable (if not impossible) for domestic forces to serve as instigators of radical change in sectoral governance: the spark has to come from outside. While this is a big assumption, I believe it is generalizable. In a sector marked by complete autarky (unaffected by internationalization in other sectors as well), actors’ institutional preferences will change slowly, thus creating only evolutionary impulses, save for big contingencies such as revolution or war. The exception to this is what institutionalists call ‘threshold effects’, whereby slowly accumulating endogenous tensions reach a tipping point and are released suddenly to provoke major transformation (Pierson 2004, 83ff).

Yet in a typical late developer, which has been exposed in its recent history to such formidable international constraints as shifts in trade patterns, policy conditionalities imposed by international agencies, an unprecedented vulnerability to investor preferences, and requisites of membership in regional and supranational organizations etc., the likelihood of an undiluted tipping point to materialize fully independent from outside influences is minimal. Besides, developing countries are almost always at the periphery of global normative developments; novel ideas about sectoral governance tend to originate in advanced political economies. This does not mean, however, that domestic actors will remain passive spectators in the process of innovation. Once pre-existing arrangements are slated for change, fighting over the terms of innovation becomes fair game and will result in a domestic flavoring of new arrangements (e.g. Snyder 2001).

This brings us to the last caveat; that is, the extent to which collective interests can influence patterns of reshaping. At this level, the typology assumes a basic contrast between technocratic engineering and coalition politics, with the intensity of political competition separating the two. This may sound counterintuitive if one considers the
actor-oriented literature of the 1990s, which thoroughly studied how technocratic reformers establish coalitions with social actors to press for politically difficult reforms. Here, I am quite narrowly interested in a hypothetical continuum of political competition, at one extreme of which lies a unified, politically uncontested ruling elite, and at the other extreme a multitude of opposing factions vying for incumbency amid a political melee. The more the political context moves away from the former and toward the latter pole, the broader and more heterodox the ruling coalition, the smaller the leeway for insulated reformism, and the greater the influence of collective interests. In fact, the idea of ‘reform coalition’ is useful precisely because it tells us how in the ‘real world’ this tension is generally resolved. But more important for our purposes is this: high levels of political competition, and thus the resort to coalition politics, do not guarantee social actors to tip the (institutional) scales in their favor. In a policy context predisposed to societal negotiation, collective actors may still find it difficult to articulate their interests due to weaknesses in organizational capacity, the preferences of other social players, and even simple lack of information. Still, the contextual determinants of interest aggregation are more consequential for institutions when incumbents face strong competition, that is, when such aggregation has higher political purchase.

1.2 Research Design

As far as specific institutional configurations are concerned, the typology presented above provides only descriptive generalizations about the paths they take. Put differently, it leaves an explanatory gap between the types of reshaping and their real
world outcomes. This gap can only be overcome by detailed case studies. The empirical analysis presented in the forthcoming chapters thus serves a dual purpose. On the one hand, the diverse trajectories of Turkey’s fisco-financial and agricultural regimes help assess the validity of the main hypothesis behind the typology—whether different values of internationalization and political competition assign different weights to the four main explanatory variables, leading in turn to distinct types of reshaping. On the other hand, these cases also illustrate how these distinct types are put into action; that is, how pre-existing institutions, international norms, coalition politics, and technocratic engineering interact to reshape sectoral regimes of governance in a real world setting.

What precisely are the cases to be studied? I follow John Gerring’s useful distinction between populations, samples, units and cases. “A ‘population’ is comprised of a ‘sample’ (studied cases), as well as unstudied cases. A sample is comprised of several ‘units,’ and each unit is observed at discrete points in time, comprising ‘cases’” (2004, 342). Thus, within a vast population of mid-range institutions in contemporary late developers, I focus on a small sample from Turkey, which includes two units of analysis, that is, fiscal-financial and agricultural regimes. I observe these units across specific time frames that roughly correspond to higher and lower levels of political competition within Turkish polity and by paying special attention to the sectoral effects of the internationalization of the Turkish economy. This in turn generates eight distinct cases. Table 1.2 displays how these cases roughly fit the typology introduced earlier.

Obviously, Turkey itself is neither a case nor a unit of analysis in this research design. Yet because I derive my cases from this peculiar context, it is useful to reflect briefly on the kind of puzzle it poses in terms of institutional adjustment in late
developers. Both official and scholarly accounts of Turkish liberalization suggest that creating a ‘market-supporting’ institutional environment proved an insuperable challenge for Turkish policymakers, particularly in the 1980s and 1990s. Such misadventure is something of a mystery, though. From a comparative perspective, Turkey appeared in a favorable position to reorient the governance of its economy in line with its market transition. As in many countries, reform opening in Turkey initially empowered relatively autonomous, technocratic elites. But unlike postsocialist economies, Turkey had enjoyed a fairly long history of capitalist development, which in theory should have only strengthened the hand of the reformist elite. And unlike many Latin American polities that also had a capitalist pedigree, it encountered weaker and much less organized social opposition to neoliberalism. In stark contrast with some East Asian cases as well, Turkey’s liberal elites had no qualms about discarding the country’s long-standing state-induced model of development and the state-society relations that lay underneath.
Moreover, if the longevity of the reform process is a facilitating factor for the depth of institutional adjustment, Turkey’s reform push predates that of most other ‘emerging market economies’. If political will is the key, Turkish governments of all stripes were officially committed to liberalization. If it is international politics that counts, Turkey has been an important Western ally since the 1940s, receiving preferential treatment on multiple fronts to this day. If competitive politics facilitates a competitive, liberal economy, only a handful of non-Western countries spent more years under freely elected governments than Turkey in the latter half of the century. But if early stages of reform require unchallenged leadership, then one must be reminded that the first generation of Turkish reformers had the luxury of operating under the longest episode of authoritarian repression in the country’s postwar history. None of these circumstances helped reformers harmonize the way the Turkish economy was governed on the ground with their avowedly liberal goals. In terms of constructing market-enhancing institutions, Turkey should have succeeded; nevertheless, it seriously underachieved.

Explaining the Turkish puzzle in its entirety is not one of the tasks I set out for this study. Still, the trajectory of financial and agricultural regimes tells us something important about it. These arrangements are so different from each other and have evolved in such remarkably diverse ways that it is difficult to imagine a single route to ‘bad design’, as proponents of liberalization would see these institutions. Rather, it appears different causal mechanisms in different regimes of governance culminated in a similar outcome, that is, institutional profiles that complicated the country’s market transition.

But why finance and agriculture, and why these specific time periods? While these cases offer interesting patterns of institutional development, other sectors or policy
areas at other time periods would also make suitable candidates if one were to select simply on the outcome variable. Rather, I select on the explanatory variables of the typology. In much of the period under examination (throughout the 1980s and the 1990s), dominant patterns of internationalization created strong incentives for reorganization in Turkish finance, triggering innovative impulses along emergent international norms. By contrast, nondomestic incentives for reorganization were much weaker in agriculture, triggering accommodative impulses that reworked pre-existing institutions. Only in the aftermath of the 2000-2001 crisis did international constraints favor reorganization in both sectors. Likewise, the Turkish polity has been characterized by alternating episodes of relatively high and low levels of democratic competition since the early 1980s, which I use as the basis for dividing units of analysis into distinct cases for observation.

Turkish finance and agriculture are dissimilar in other ways as well. One major difference is in the organizational character of the regimes that govern these sectors. Historically, the tasks of governing state finances and regulating the banking sector depended upon fairly small, centralized agencies oriented toward a market composed of few actors. Agriculture, by contrast, exhibited a gigantic network of highly politicized state and parastatal organizations whose operation impacted the livelihood of almost half the total workforce. Second, social actors in these sectors differed sharply in their politics. Financial interests were quick to throw their weight behind market reforms. Agricultural interests, headed by the grain lobby representing the smallholders of Anatolian plains, remained skeptical of economic restructuring. Finally, an analogous divide characterized the public realm. The public agencies in which agricultural and financial regimes were embedded stood at opposite ends within the Turkish state in terms
of their organizational cultures, links to policymaking circles, profile of the bureaucratic staff, and attitudes toward the direction of the policy regime.

These dissimilarities are both a blessing and a curse for comparison. When financial and agricultural regimes take on different values of the dependent as well as explanatory variables, that is, in the 1980s and 1990s that generate half the cases, sectoral differences leave little common ground for a cross-unit ‘controlled comparison’. But in the postcrisis years, sectoral differences facilitate such comparison: strong international incentives for reorganization and identical levels of domestic political competition generated identical patterns of institutional reshaping (insulated innovation, followed by negotiated innovation) in both sectors despite their structural dissimilarities.

The bulk of my analysis employs “within-case” methods, whereby “hypotheses are evaluated by elucidating intervening processes and other observable implications of arguments” (Mahoney 2007, 131). In particular, I rely on the method of process-tracing, which “attempts to identify the intervening causal process…between an independent variable (or variables) and the outcome of the dependent variable” (George and Bennett, 2005, 206). This requires a comprehensive analysis of institutional development in both sectors. For this task, I rely on data collected from several sources: published and unpublished government documents; documents and reports from international agencies; reports from Turkish interest associations; personal interviews with Turkish government officials as well as representatives from autonomous and quasi-autonomous agencies; and numerous secondary sources including scholarly and journalistic publications.

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6 Controlled cross-case comparative methods require that the cases should either share the same values of the dependent and independent variables while they are unlike in all other respects, or differ in their dependent and independent variables while they are similar in all other respects. These conditions correspond to Mill’s *method of agreement* and *method of difference* (George and Bennett 2005, 153ff) and Przeworski and Teune’s (1982) *most different* and *most similar* research designs, respectively.
Process-tracing has two distinct advantages for this study. On the one hand, it effectively complements typological theorizing. Bennett and Elman (2006, 467), for instance, note that “[i]t is the combination of well-specified types and detailed study of a small number of cases that allows qualitative researchers to gain both inductive and deductive insights into higher-order interactions.” Put bluntly, the argument that wider patterns of internationalization and the intensity of political competition co-determine particular paths of sectoral institutional reshaping by altering the relative weights of some more imminent explanatory factors is meaningful only if we can unpack the distinct processes that lead to such an outcome in every single case.⁷ But an important problem is that for every cell in the typology there is not one explanatory factor to investigate but four potentially interacting factors, of which two are held to be dominant. This suggests a condition of complex causality and multiple interactions, which cannot be addressed without careful identification of the historical content of these factors. Here again, process-tracing proves to be an indispensable tool.⁸ For example, by looking at the dissimilar collective capabilities of peasants and bankers, we can discern different modalities of societal influence over institutional design during the intense coalition efforts of the 1990s. Likewise, only through an examination of the varied channels of international constraints over Turkish finance and agriculture and their varied impact on collective preferences after 1999 can we grasp the fundamental differences in the strength of recent innovative projects in these sectors.

⁷ As George and Bennett (2005, 255) put it, “[i]f the researcher has only identified the configuration of variables that defines the type but has not specified the interactions among them, process-tracing can help identify inductively the interactions that took place in cases of the specified type.”

⁸ George and Bennett (2005, 13) “recommend process-tracing as a means of examining complexity” and “suggest typological theorizing as a way to model complexity.”
On the other hand, process-tracing offers a methodological guard against underestimating the impact of left-out variables and thereby ignoring alternative explanations (George and Bennett 2005, 80-81; 223; 254). Could it be that the quality of democracy was more important than either the intensity of political competition or the intrigues of coalition politics for collective interests to take part in institutional reorganization? Was the crisis of 2000-2001 a catalyst for change in the governance of these sectors regardless of the preferences of social and policy actors? How can we be certain some of the variables predicted to be less significant in a certain type were really so (e.g. international norms for negotiated accommodation in Turkish agriculture during the 1990s)? These surely are important questions we cannot afford to dismiss. Following the processes that led to the specified institutional outcomes will force the analysis to confront such alternative variables and explanations. This could help refine the mode of explanation or even falsify some basic assumptions of the typological framework.

Case study researchers are routinely cautioned against the dangers of overgeneralization. Potential problems of case selection (Collier and Mahoney 1996, 63), tradeoffs between breadth and depth (Gerring 2004, 347ff), and complexities often inherent in causal mechanisms (George and Bennett 2005, 145ff) pose obstacles to extending findings from a small number of cases to a wider population. Given these difficulties, it is often suggested that detailed case studies are better suited to making descriptive (King, Keohane, and Verba 1994, 228) or contingent generalizations (George and Bennett 2005, 110-1; 119ff). Such generalizations apply only to a well-specified set of similar cases and under narrow scope conditions; thus, they are more useful to generate mid-range rather than general theories (George and Bennett 2005, 266). These
considerations are valid for the present analysis as well. My empirical findings from the eight Turkish cases, which spawn such issues as whether the institutional profiles that followed from the associated types prove desirable or undesirable from this or that viewpoint, which collective dilemmas they resolve or leave unattended, and their wider consequences for policymakers and social actors, are not easily generalizable.

But the typology itself has broader applicability, for it derives institutional pathways from some fundamental conditions that distinguish sectors and policy domains across contemporary late developers—the transformative content of international influences, the self-reinforcing capacity of existing arrangements, and the respective roles of technocrats and attendant intra-state and societal interests. Chapter 7 applies the typology to four widely studied non-Turkish cases: Chinese banking (1978-2003), South Korean corporate governance (1988-1997), Mexican agriculture (1988-2000), and Argentine labor markets (1989-2004). Each of these cases provides a plausible approximation of one type of reshaping, attesting to the comparative analytic value of the basic framework I offer. This exercise is useful in two additional ways. First, it further emphasizes the point that, even though the typology can predict the dominant type of reshaping in a mid-range institutional regime, this on its own is insufficient to account for concrete institutional profiles. As the manifestations of and interactions between the same explanatory variables differ from one context to another, so the configurational and social outcomes of the same type vary across cases. Second, accumulation of empirical evidence helps partially to compensate for this limitation. With an expanded comparative sample, it becomes possible to arrive at some limited generalizations about each of these four main types, mainly with respect to the potential scale of change, the extent of case-
specific variations in outcomes of the same type, and the impact on collective fortunes. In short, deductive typological theorizing offers valuable guidance for empirical analysis, which then supplies tangible improvements in our understanding of how mid-range institutions are reshaped in late developers and to what effect.

1.3 Peasants, Bankers and the State: An Overview

How did institutional trajectories in Turkish finance and agriculture embody these ideal-types? The application of the typological framework to the cases at hand reveals different sectoral scenarios in four distinct historical episodes (Table 1.3).

1980-1986

The early stage of liberalization in Turkey followed an insulated reform path, in which policies were designed and implemented by a technocratic change team that benefited from continued authoritarian constraints on electoral competition. Technocrats’ institutional preferences varied across sectors, however. In both public finance and the banking sector, reformers chose to break with pre-existing regimes and built novel mechanisms of governance. By contrast, existing arrangements were preserved in agriculture, yet they were set to serve ends that contravened their original functions.

In a domestic political context that constrained societal influences on policy, this difference in institutional pathways was a function of patterns of internationalization. Manufacturing export-led integration and continued problems of foreign indebtedness made existing fiscal and banking regimes unsuited for the new era. Reformers thus settled
on a path of innovation inspired by the neoliberal financial norms of the day, which were also enforced through World Bank projects and agreements with the International Monetary Fund (IMF). The outcome was the emergence of a semi-autonomous Treasury equipped with strong powers over government finances as well as a new legal-organizational framework for banking. Insulated innovation in finance brought about novel institutions that on the whole favored private financial interests.

In agriculture, falling world commodity prices and high international tariffs made the sector relatively irrelevant for Turkey’s newfound outward-orientation. Combined with the general sense of apathy international agencies displayed toward the governance of the sector, this gave technocrats little reason to alter the corporatist-interventionist support regime, which in the past had served as the primary mechanism of rural populism. Instead, reformers formulated the problem with support schemes as one of fiscal cost, that is, one of narrowly defined institutional effect rather than institutional design. They preserved the interventionist machine, but curtailed its populist effects by checking floor prices, input subsidies, and agricultural credits. Insulated accommodation in agriculture resulted in the conversion of the support regime from a mechanism of income transfer toward the countryside to one that repressed rural incomes.

1987-1999

In the late 1980s, the domestic context shifted radically. Redemocratization brought about higher levels of party competition, augmenting the leverage of distributive pressures. Technocratic engineering lost much of its appeal, and policymaking came to be dominated by everyday concerns of building and maintaining loose ruling coalitions.
Table 1.3  
*The Evolution of Turkey’s Agricultural and Fiscal-Financial Regimes of Governance (1980-2007)*

<table>
<thead>
<tr>
<th></th>
<th>International Incentives for Reorganization</th>
<th>Intensity of Domestic Political Competition</th>
<th>Dominant Forces Shaping Institutions</th>
<th>Dominant Type of Institutional Reshaping</th>
<th>Resultant Configuration</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture (1980-1986)</td>
<td>Weak</td>
<td>Low</td>
<td>Technocrats Pre-Existing Institutions</td>
<td>Insulated Accommodation</td>
<td>Conversion; Corporatist schemes of income transfer redeployed to check rural incomes</td>
</tr>
<tr>
<td>Finance (1980-1986)</td>
<td>Strong</td>
<td>Low</td>
<td>Technocrats International Norms</td>
<td>Insulated Innovation</td>
<td>Novel Institutions; The rise of semi-autonomous Treasury; new legal infrastructure in banking</td>
</tr>
<tr>
<td>Agriculture (1987-1999)</td>
<td>Weak</td>
<td>High</td>
<td>Coalition Politics Pre-Existing Institutions</td>
<td>Negotiated Accommodation</td>
<td>Restoration; Antiquated subsidy regime restored to its original function of populist redistribution</td>
</tr>
<tr>
<td>Finance (1987-1999)</td>
<td>Strong</td>
<td>High</td>
<td>Coalition Politics International Norms</td>
<td>Negotiated Innovation</td>
<td>Continuous Adjustments; Debt management refined; selective though feeble attempts at stronger banking regulation</td>
</tr>
<tr>
<td>Agriculture (2000-2002)</td>
<td>Strong</td>
<td>Low</td>
<td>Technocrats International Norms</td>
<td>Insulated Innovation</td>
<td>Novel Institutions; Pre-existing regime dismantled; agricultural reform brings in new, leaner subsidy schemes</td>
</tr>
<tr>
<td>Finance (2000-2002)</td>
<td>Strong</td>
<td>Low</td>
<td>Technocrats International Norms</td>
<td>Insulated Innovation</td>
<td>Novel Institutions; Debt management reformed; radical financial restructuring via new regulatory agency in banking</td>
</tr>
<tr>
<td>Agriculture (2003-2007)</td>
<td>Strong</td>
<td>High</td>
<td>Coalition Politics International Norms</td>
<td>Negotiated Innovation</td>
<td>Hybridization; Old support instruments resurface to co-exist with new ones; further innovation via new law</td>
</tr>
<tr>
<td>Finance (2003-2007)</td>
<td>Strong</td>
<td>High</td>
<td>Coalition Politics International Norms</td>
<td>Negotiated Innovation</td>
<td>Consolidation; Fiscal regime consolidated; new banking law reflects evolving international principles</td>
</tr>
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Still, the sectoral variance in institutional paths persisted. In finance, evolving international norms continued to dictate the spirit of restructuring efforts, even more so in the aftermath of capital account opening in 1989. The weak coalition governments of the 1990s held onto the arrangements built by their technocratic predecessors, making continuous adjustments along the way. None of these adjustments, however, was designed to pre-empt the grave dangers of rapid internationalization marked by increased exposure to short-term capital flows. Rather, negotiated innovation allowed for only limited changes. Most attempts at stronger prudential regulation after the 1994 shock succumbed to opposition from bankers and their allies within the political establishment, and refinements in fiscal debt management proved utterly ineffective.

In agriculture, the political quiescence of Turkey’s vast smallholder peasantry became indispensable for any ruling coalition of the 1990s. The outcome was the restoration of the populist-redistributive functions of the interventionist machine in a clear example of negotiated accommodation. The 1990s witnessed an explosion in older forms of side payments, ranging from excessive support purchases to subsidized credit and frequent debt write-offs. Distributive pressures from the countryside thus paid off remarkably, thanks to rapid fiscal expansion riding on financial internationalization.

Yet just as fiscal expansion via capital flows helped reinstate rural populism, so the allure of populism would make an end to growing public indebtedness politically unpalatable. A net result of this was the emergence of a second and eventually larger channel of income transfer, this time toward the financiers of the public debt via jumbo interest payments under high inflation. These twin transfers of income toward peasants and bankers I call ‘double redistribution’. This tacit, accidental social alliance led to a
fundamental intertwinement of existing fiscal-financial and agricultural regimes, which reinforced one another in an unusual example of institutional complementarity, neutralizing reform agendas in both spheres after mid-decade.

2000-2002

The crisis of 2000-2001 resulted in a brief resurgence of technocratic insulation under a weak and much discredited coalition government. This second episode of technocratic reformism, as different from the first one, would press for major institutional recasting not only in finance but in agriculture as well. In effect it displayed typical examples of insulated innovation, which generated novel institutions in both sectors.

In finance, the reformist drive followed the international policy consensus on the need for better financial governance as a reaction to the series of meltdowns in the semi-periphery. In the context of a comprehensive top-down reform program, which was also endorsed generously by the IMF and the World Bank, a new public authority in banking was established and mechanisms of public spending and debt refinancing refurbished. The new order emphasized much more stringent regulation of the banking sector and a more transparent, politically restrictive regime of public finance.

International normative pressures caught up with Turkish agriculture as well. Reforms in support policies in advanced economies that paralleled the growing preoccupation with domestic subsidy arrangements in international trade agreements left Turkey’s antiquated agricultural machine fully open to attack by technocratic reformers. Price supports and input subsidies were discontinued, and replaced by a US-style direct income support (DIS) system in the context of the World Bank’s Agricultural Reform
Implementation Project (ARIP). The project also advocated the divestiture of the remaining agricultural state enterprises and reform of corporatist farmers’ organizations.

2003-2007

The November 2002 elections brought collective interests and thereby coalition politics back into the domestic game, but they also paved the way for a strong single-party government for the first time in over a decade. Political competition in this period was thus not as intense as it had been during the previous decade when extreme party fragmentation had degenerated into constant skirmishes at an increasingly nebulous political center. Still, it forced the ruling Justice and Development Party (AKP) to construct a broader-based reform coalition. The events of this period show the complexities of negotiated innovation in its full.

The manifestation of this dynamic in finance was a counterreformist offensive by bankers, as well as elements from within the traditionalist bureaucracy. However, by skillfully exploiting the internal divisions among the banking community and having secured the unconditional support of both the dominant industrial bourgeoisie and international agencies, the AKP government managed to neutralize reform resistance and followed in the footsteps of the previous government to consolidate and further fiscal and banking reforms. In the process, Turkey’s nascent rentier class, represented by small and medium-sized banks that had benefited the most from fiscal expansionism of the 1990s, was destroyed through nationalizations, mergers, and domestic and foreign takeovers.

Agriculture offered a different story. The AKP’s attempts to stay the new path opened up under politically insulated technocrats (as it successfully did in finance) have
been complicated by the political weight of the Turkish peasantry. By 2004, and in the face of mounting opposition from farmers’ organizations, old support schemes resurfaced in the countryside, albeit in bits and pieces. Given continued international pressures for convergence on a different paradigm of support, however, ARIP and the DIS regime was kept alive. This trend toward a *hybrid* support regime was formalized in the Agricultural Law of 2006, which not only allowed new and old support instruments to operate side by side, but also introduced innovations beyond the original technocratic project.

### 1.4 Plan of the Study

The study is organized as follows. Chapter 2 explores the theoretical content of the proposed typology. Special attention is placed on the need for a synthetic approach to institutional development, and how insights from historical institutionalism, the literature on reform politics, and international political economy could be combined to this end. Chapters 3 through 6 present the empirical material on Turkey in chronological order. Chapter 3 gives a historical backdrop of financial and agricultural regimes in Turkey before liberalization. Chapter 4 discusses the emergence of discordant paths of institutional reshaping in Turkish finance and agriculture in the 1980s with special emphasis on the differential sectoral impact of wider patterns of internationalization. Chapter 5 examines how the intense coalition efforts of the 1990s affected institutional regimes in both sectors. The way these efforts tied collective interests together also provides some clues about thorny questions of institutional complementarity and coevolution. Chapter 6 offers a detailed account of postcrisis attempts at institutional
reform from above. Identical patterns of change in this period facilitate a broader cross-sector comparison. Chapter 7 extends the typology to two East Asian and two Latin American cases in an effort to flesh out its comparative usefulness and learn more about the different types of reshaping. Chapter 8 concludes with reflections on the wider findings of the study.
CHAPTER TWO

LIBERALIZATION AND THE RESHAPING OF INSTITUTIONS

Since the early 1990s, much emphasis has been placed on how institutions shape economic outcomes in late developers. The legacy of past arrangements, the shortcomings of existing institutions, and the promises of institution-building have become common themes in both policy narratives and scholarly studies on transformations in the developing and postsocialist world. But this increased interest has also produced disquieting realizations of how little we know about the way institutions themselves are shaped under liberalization: “our theories of how fundamental institutional change occurs are underdeveloped” (Evans 2004, 32); “institutional reform…is a field with much action and little theory” (Naim 2000, 515); “there is much to be learned still about what improving institutional quality means on the ground” (Rodrik, Subramanian, and Trebbi 2004, 158). It is difficult to find theoretically well-founded answers even to such basic questions as how market reformers end up with the institutions they possess, why some arrangements prove so resistant to change, or what explains the success or failure of institutional reform.

This chapter acknowledges this problem and searches for a remedy. But rather than call for a grand theory, it contends that insights can be derived from several existing literatures to illuminate institutional pathways in the developing world. Such a synthetic approach is not a convenience, but a necessity. The reshaping of sectoral institutions in
contemporary late developers is often such a multifaceted affair that it is unlikely to be fully comprehensible from a unitary theoretical position.

The discussion begins with a brief account of the ‘institutional turn’ in economic research and some problems associated with its recent policy extensions. The rest of the chapter fleshes out the explanatory variables that make up the typological framework offered earlier. The second section focuses on the impact of pre-existing institutions; here, historical institutionalism provides invaluable insight. The third section reflects on the contrast between technocratic engineering and coalition efforts for institutional trajectories in light of the vast literature on reform politics in the developing world. But while both historical institutionalism and the market reform literature contribute to our understanding of institutions in late developers in numerous ways, they also share an important affliction, that is, an inexplicably weak emphasis on nondomestic variables. Thus, the fourth section examines how international constraints can be systematically integrated into the study of sectoral institutions, emphasizing the link between the formative influence of international norms and the market and policy dimensions of internationalization. The chapter concludes with a brief note on some affinities between the four main variables.

2.1 The Institutional Turn and the Problems of Monocropping

In the face of the lackluster record of market reforms in much of the developing world, economists and international agencies have increasingly emphasized the importance of building and redesigning institutions as a means to achieve sustained
growth. This emphasis represents a strategic departure from the self-regulating market ideals of neoclassical orthodoxy, which guided mainstream development policy advice throughout the 1980s and in the better part of the 1990s. The logic behind this reorientation, variously labeled as “institutional turn” (Evans 2005) or “institutions fundamentalism” (Rodrik 2006), is simple: markets are not self-sustaining; they can facilitate high-quality growth only in the company of effective ancillary institutions. Developing countries should therefore complement policy change with the pursuit of market-supporting institutions. The discussion below presents the intellectual origins of this paradigm broadening and points to some problems with its recent policy extensions.

Much of the renewed interest in institutions in economic analysis can be traced to the growing popularity of new institutionalist economics (NIE) since the 1980s.¹ This approach emerged as a correction to neoclassical economic theory, particularly targeting its rationality assumptions. Institutions in this view are defined as “the rules of the game in a society or, more formally, the humanly devised constraints that shape human interaction” (North 1990, 3). They reduce uncertainty in social exchange and create incentive structures for individual as well as collective action. Bringing issues such as transaction costs, property rights, imperfect information and other production externalities to the attention of economic analysis, contemporary institutionalists explain cross-country variation in economic performance in terms of institutional efficiency over long periods of time.² Where institutions lack adaptive efficiency, suboptimal paths of development lock-in and economies lag behind. Yet it is not easy to escape from

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² See Alston, Eggertsson, and North (1996) for a classic collection of essays in this spirit. See also Harriss, Hunter, and Lewis (1995) for applications of NIE to some developing country cases.
inefficient institutions and acquire better ones. Rather, institutional change is often an incremental process that parallels the deep grooves of social change.³

In trying to explain the stark variations in economic performance across late developers, some recent large-\textit{n} analyses also build heavily on an NIE-inspired framework. Accordingly, endowments can account for variations in economic development only to the extent of their historical influence on institutional quality (Acemoglu, Johnson, and Robinson 2001). Likewise, neither policies (Easterly and Levine 2002) nor international integration (Rodrik, Subramanian, and Trebbi 2004) has a direct impact on incomes independent of institutions — “the quality of institutions trumps everything else” (ibid., 135). A growing awareness of institutions is shared by other prominent development economists as well. Sen’s (1999) emphasis on the value of participatory institutions, Bardhan’s (2004) work on the linkages between institutional change and collective action, and Stiglitz’s (2003) critique of the neoliberal orthodoxy all have institutionalist overtones.

This intellectual sea change has been well-received in the dominant centers of development thinking. In fact, the revision and repackaging of neoliberal policy advice around the turn of the century was heavily inspired by an institutional outlook. The troubled record of market reforms, particularly in Latin America and Sub-Saharan Africa, had exposed the fallacy of relying exclusively on a narrow set of macroeconomic policy measures, popularly known as the Washington Consensus (Gore 2000; Naim 2000). Adding institutions into the mix provided an attractive remedy, broadening the scope of policy advice while retaining its neoliberal core. It is in this context that I offer to term

³ North (1990, chapters 10-13). For a synoptic account, see North (1995, 23ff). See also Fiori (2002). Clearly, the gradualist tendencies of the NIE stand in marked contrast with recent policy emphases on fast-track institution-building.
the policy extension of the institutional turn as ‘neoliberal institutionalism’. Both Stiglitz’s (1998) early observations on an emerging *Post-Washington Consensus* and Rodrik’s (2006) useful discussion of the *Augmented Washington Consensus*, for example, describe a process of paradigm broadening in which the fortunes of neoliberal reforms are tied to the acquisition of an appropriate institutional environment (cf. Williamson 2004). The normative content of such an environment tightly overlaps with the evolving dominant ideas of sectoral policymaking. This includes strong institutions that would insure effective governance of industry, finance, and trade, while also offering some social protection to the losers of economic change through organizational reforms.

But how can liberalizing countries acquire such institutions? Domestic conditions in the developing world are not always conducive to the natural development of a market-enhancing environment. As Douglass North (2005, 46) points out, the changes necessary for acquiring good institutions are “frequently not in the feasible set”. Given this inherent difficulty, the attention of the international financial institutions (IFIs) has shifted toward the potentials of reforming the arrangements on the ground as a short-cut to appropriate institutions (Burki and Perry 1998; World Bank 2002a; 2003a). And where domestic actors might expectedly lack both the know-how and the political incentives for this difficult task, external guidance and compulsion is seen as a practical way of spearheading the much-needed change.

There are several problems with this reformist policy extension of the institutional turn. First, the agenda itself is too broad. The NIE starts from a concise definition of institutions, but in specifying which institutions matter for growth, economists draw up a very long list of items reminiscent of political development *à la* Western liberal
democracies. The elements of a market-sustaining institutional environment usually overlap with those of ‘good governance’, comprising such diverse parameters as the rule of law, political stability, government effectiveness, regulatory quality, accountability, and the control of corruption (Kaufmann, Kraay, and Zoido-Labatón 1999). Rodrik too casts a wide net in his description of institutions that assure long-term growth; such institutions “provide dependable property rights, manage conflict, maintain law and order, and align economic incentives with social costs and benefits” (2003, 10). Translated into policy advice, the acquisition of these ‘good institutions’ requires substantive reforms in a numerous sectors and policy areas, and involves building new regulatory agencies, refurbishing bureaucracies, and transforming deep-rooted arrangements. This snowballing of the institutional reform agenda has drawn criticism even from former advocates of the project.4

Second, reform proposals contain minimal insight into the origins, evolution and the workings of existing arrangements. How do institutions evolve as part of a wider sociopolitical sphere? Why do countries get locked into matrices of inefficient arrangements? These issues are typically left untouched. This leads to an overly “thin” view of institutions which often breeds a “false parsimony” (Chang and Evans 2005, 99). At the core of this thin view is a functionalist outlook. Functionalism views institutions from the standpoint of their effects on the environment in which they are embedded (Pierson 2000b; Mahoney 2000, 519ff; Pierson and Skocpol 2002, 708ff). In a similar fashion, most economists and policy advisors tend to judge existing institutions primarily against their utility for liberalizing reforms. Admittedly such a view offers a necessary

4 “[T]he obsession with comprehensive institutional reform leads to a policy agenda that is hopelessly ambitious and virtually impossible to fulfill.” (Rodrik 2006, 980). Cf. Grindle (2004).
standpoint for policy prescription. But strict adherence to functionalism also limits our understanding of institutions with its predisposition toward simplistic dichotomies. An institution can either sustain capitalist growth or it cannot. The latter type will either persist or will be reformed. That is, bad institutions are either made good or they remain bad. In this manner, a strict functionalist logic tends to reduce most institutional change under liberalization to outcomes of reformist action, while obscuring non-reformist change. In effect it pushes the analysis toward either of the two extreme situations of institutional existence—rapid intentional transformation or sticky automatic endurance. This hardly reflects the broad range of institutional trajectories in the developing world.

Third, and most important, strategies of institution building and reform usually involve the transplantation of institutional blueprints. As Peter Evans points out, such an effort “rests on…the general premise that institutional effectiveness does not depend on fit with the local sociocultural environment…and that idealized versions of Anglo-American institutions are optimal developmental instruments” (2004, 33). He terms this strategy institutional monocropping. Such belief in the transferability of institutions across different social contexts overlooks the basic question of endogeneity. In other words we have no way of knowing “whether one can stick any institutions into some particular conditions and expect that they would function in the same way as they have functioned elsewhere” (Przeworski 2004, 528). Transferability thus remains an unknown quantity, and renders large scale projects of institutional engineering an ultimately experimental enterprise.

The tension between endogeneity and transferability is not as straightforward as it may seem at first. For one thing, endogeneity does not necessarily entail indigenousness.
That arrangements do move across contexts, spreading from one setting to another, is a fact of social history—hence the basic idea of institutional diffusion (Campbell 2004, 77ff). Successful diffusion, however, is a complex affair which requires the outsider arrangement to establish sufficient feedback links with the pre-existing environment. In the institutionalist jargon this is called a mechanism of translation: “new [externally generated] ideas are combined with already existing institutional practices and, therefore, are translated into local practice in varying degrees” (ibid., 80, emphasis original). This certainly was the story of many arrangements that defined the governance of Turkish finance and agriculture by 1980. For example, neither credit rationing, nor producer cooperatives were indigenous to the Turkish scene. They had their origins elsewhere. Still, over decades, they had been successfully translated into the Turkish political economy and were accepted by social and policy actors as part and parcel of the natural order of things in these sectors. They were, in that sense, naturalized arrangements.

We may suspect this is what the World Bank expects to take place when it recommends that institution building should complement what already exists on the ground. But this is seldom the case. Even in the diffusion of macro- and meta-institutions, where convergence is comparatively slow, there is no guarantee for successful translation or naturalization. The challenges of diffusion are more obvious at

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5 In fact, the main question of comparative political economy since the mid-1990s has been the limits of institutional diffusion in the face of globalization, and in particular whether advanced industrial countries do or can retain their distinctive patterns of economic coordination despite pressures toward conversion. See Berger and Dore (1996) and Hall and Soskice (2001) for classic collections on this question.

6 The dynamic here is not too different from instances of ‘policy transfer’ or ‘policy diffusion’, as widely discussed in the comparative public policy literature. See, for instance, Dolowitz and Marsh (2000).

7 The first “lesson” for building market institutions is to “design them to complement what exists” (World Bank 2002a, 4).

8 Case in point is Bertrand Badie’s (2000) seminal account of how modern state practices have disseminated from the West to the rest of the world over the last two centuries. For Badie the diffusion of this political form involved exporters and importers, each following their own strategic interests.
the micro- and meso-levels, the subject of this study. In the simple scenario of an IFI-supervised reform project which has a life span of only a few years, the amount of structural change expected is so unrealistically high that countries are often hurried into dislodging well-established arrangements in favor of some new, untested ones. As a result, institutional diffusion by way of reform rarely takes the form of translation, but rather comes closer to rash transplantation, validating the ‘monocropping’ thesis.

These fundamental problems—too broad a reform agenda, based on a shallow understanding of the real world of institutions and a questionable assumption of transferability—have led some development scholars to denounce the institutional turn as a “sophisticated re-invention of earlier ‘modernisation’ theory” (Leftwich 2005, 590). In fairness, though, the problems discussed above do not always go unnoticed by economists. Indeed, the limitations of an undifferentiated approach toward institution-building are widely acknowledged even in the strongholds of ‘monocropping’. And yet transplantation via top-down reform remains a pervasive policy instrument, reflecting a disconnect between research, prescription, and application. One reason for this is the inherent ‘unfalsifiability’ of this sort of policy advice, which renders it a safe bet for the

Furthermore, the relations of the imported state to the ‘indigenous’ institutions and cultures have been remarkably complex, awkward, and often violent (cf. Scott 1998).

9 For example, Rodrik’s (2003) widely known collection of country studies emphasizes the diversity of successful institutions and the value of experimentation, while his recent work (2006; 2007) includes a stinging critique of ‘monocropping’. Meanwhile, some economists move toward developing ‘thick’ theories of institutions. Most notably, see Aoki’s (2001; 2007) work, which offers game-theoretic models of organizational co-evolution, institutional complementarity, and cross-country as well as cross-sectoral diversity.

10 The 2002 World Development Report, one of the founding texts of institutional engineering, rejects the idea of ‘best practice’ as a “flawed concept” (World Bank 2002a, 4). In fact, as criticism of monocropping intensified, “a more candid acknowledgement of the limited current understanding of the relationship between existing institutions, reform initiatives, and economic performance in the developing world has emerged even within official development circles” (Dunning and Pop-Eleches 2004, 5).
Another, and perhaps more important, reason is that convergence upon certain institutional designs, particularly in the governance of economic sectors, is imperative for the types of international integration preferred by dominant interests in the global economy. Monocropping is thus not simply a naively misguided policy advice, but inseparably linked to global power structures as well. Yet for now, the discussion will turn to another body of work that offers stronger tools for explaining institutional origination, stability and change.

### 2.2 Historical Institutionalism: How Pre-Existing Institutions Matter

The rediscovery of institutions was not a phenomenon confined to economic research. In sociology and political science as well, institutionalist analyses have gained prominence over the past two decades. It is generally held that this revival of interest in institutions stems from not one single research agenda, but three separate lines of scholarship: rational choice institutionalism, sociological/organizational institutionalism, and historical institutionalism. Despite a partial convergence of these three schools over time and occasional ‘border-crossings’ between them, important differences do remain.

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11 “So open-ended is the agenda that even the most ambitious institutional reform efforts can be faulted ex post for having left something out. (...) In the end, it is always the advisee who falls short, and never the advisor who is proved wrong” (Rodrik 2006, 980-1).

12 It is noteworthy that not all items in the Post- or Augmented Washington Consensus are *advised* with equal determination. Financial deregulation or industrial/agricultural subsidy regimes draw intense attention from policy circles and are typically enforced in the context of bilateral and multilateral arrangements, while issues such as social security or poverty alleviation are often left to softer, more dispensable World Bank projects. Economic sectors appear to be the primary battleground for institutional diffusion.

13 A classic comparison of the three approaches as it relates to political science can be found in Hall and Taylor (1996). DiMaggio (1998) offers a different typology: rational-action institutionalism, social-constructivist institutionalism and mediated-conflict institutionalism.

14 A concerted effort to find a common ground between these three approaches comes from Ellen Immergut, who traces the origins of institutionalist approaches as far back as Rousseau, Montesquieu and J.S. Mill: “All [three institutionalisms] are concerned with the difficulties of ascertaining what human
The main focus of the present discussion is historical institutionalism, which I believe provides the most useful tools for the present analysis, particularly in gauging the effects of pre-existing arrangements.

The core feature of historical institutionalism is an emphasis on concrete historical processes as the engine of institutional formation and change: “rather than conceiving of institutions as ‘holding together’ a particular pattern of politics, historical institutionalists are more likely to reverse the causal arrows and argue that institutions emerge from and are sustained by features of the broader political and social context” (Thelen, 1999: 384). As a reflection of this holistic approach to social change, historical institutionalists tend to address “big, substantive questions that are inherently of interest to broad publics as well as fellow scholars” (Pierson and Skocpol 2002, 695). They also launch from a broad definition of institutions, which “includes both formal organizations and informal rules and procedures that structure conduct” (Thelen and Steinmo 1992, 2).

This study adopts a similarly broad understanding of institutions. Terms such as ‘institutional framework’ or ‘institutional regime’ that are at times employed when the preferences expressed in politics are so radically affected by the institutional contexts in which these preferences are voiced. (...) The common research agenda is the study of institutional effects wherever, or however, they occur” (Immergut 1998, 25). On the other hand, Hay and Wincott (1998) strongly reject this optimism for collaboration and cross-fertilization on deeper ontological grounds. The idea of ‘border crossings’ between the three schools is suggested by Thelen (1999). See the collection by Campbell and Pedersen (2001), bringing together works from all three schools. See also Nielsen (2001).

Hence Immergut (1998, 22ff) points out that historical institutionalists employ ‘contextual logics of causality’ and emphasize ‘contingent relations between explanatory elements’ instead of unidirectional, deterministic explanations.

Note that the NIE calls for a clear separation between institutions and organizations: “If institutions are the rules of the game, organizations and their entrepreneurs are the players” (North 1996, 345). Such distinction is not always welcome, however: “[S]eparating institutions and organizations is not particularly useful. The tax bureaucracy of the central state, for example, is clearly an organization, but it embodies and defines a fundamental set of relationships between state and citizen which go beyond the workings of the actual organization” (Chaudhry 1997, 10n). This is quite true for my research as well. Especially in the realm of agricultural supports, ‘the rules of the game’ are not just ‘mental models’ that inspire general organizational forms, but they are directly and particularly embodied in a complementary network of public, quasi-public and private organizations. For the institutions that are studied here, rules alone would become irrelevant in the absence of specific organizational frameworks. Lately some institutional
interchangeably throughout the analysis refer to an ensemble of historically specific mechanisms that structure and regulate the ‘standard order of things’ in a particular political-economic sphere. At the sectoral level, this would include formal rules, informal norms, and organizational networks that are specifically created to coordinate economic activity in that sector, reflecting a specific *regime of governance.* 17 There is of course an important caveat here. Simply, sectoral governance is not a function exclusively of sectoral institutions. Macro institutions and sometimes arrangements in other sectors and policy domains will also influence actors’ incentives in a sector. Polity-wide patterns of interest intermediation will have implications for all sectors; any changes in the degree of credit activism will affect not only the financial sector but industry and agriculture as well, and so on. The study of sectoral governance thus cannot afford parochialism. A degree of holism and awareness of potential complementarities are indispensable.

In a similar vein, historical institutionalists often combine micro and macro levels of analysis. A most common approach is to emphasize the timing and sequencing of key events that lead to substantive outcomes later in the evolutionary path of societies. For example, in their seminal work on eight Latin American cases, Collier and Collier (1991) explore how different institutional forms of labor incorporation, themselves resulting from concrete political struggles, gave way to “contrasting trajectories of national political change” (ibid., 4). Similarly, Karl’s (1997) analysis of petro-states underlines economists also question the strict conceptual distinction between institutions and organizations. Aoki (2001, 95ff) treats organizations as ‘proto-institutions’. Hodgson (2005, 86) too defines an organization as a “special type of institution”.

17 Here I am interested in major economic sectors, i.e. agriculture, industry and finance, which in most countries are governed by distinct arrangements. At the same time, I believe the typology developed in the previous chapter can apply to some other mid-range institutions that govern specific policy areas such as social security, health care, and the labor market. As in economic sectors, in these policy areas too, deep-seated domestic legacies often come under pressure from emergent, more liberal international norms, and policymakers and attendant interests clash over the reshaping of governance arrangements.
how distributional conflicts are instituted within the political economies of oil-exporters via similar sequences of micro decisionmaking. In a well-known macro comparison including Turkey, Waldner (1999) argues that different levels of elite conflict at the critical moment of mass incorporation lead to divergent paths of state building. Historical institutionalism thus differs substantially from the NIE in its understanding of the nature of path dependence. The past does not extend itself into the present simply as a result of the ‘stickiness’ of institutional forms that were once adopted. Rather, societies are set to proceed along particular patterns of development through dynamic historical processes.

Kathleen Thelen identifies two distinct analytical claims to path dependence in historical institutionalism. One popular research agenda emphasizes critical junctures as “crucial founding moments of institutional formation” (1999, 387). While such an emphasis offers good insight into problems of institutional origination and change, it is much less useful for exploring institutional stability and reproduction. A second analytical avenue centers on ‘feedback effects’, through which institutional forms stabilize over long stretches of time (ibid., 392ff). Here, the principle of ‘increasing returns’, adapted from economic analysis, points to an important self-reinforcing mechanism: the longer an institution persists, the deeper societal and policy actors are invested in it, and the higher the costs of change (Pierson 2000a). Arguments based on feedback effects are therefore quite effective in addressing questions of institutional reproduction, yet they are comparatively less helpful for understanding change.

During the past decade, historical institutionalists have tried to reconcile these two poles of path dependence analysis. Paul Pierson (ibid., 263ff), for example, suggests that explaining inertia through increasing returns arguments cannot escape considering the
long-term effects of contingent choices at crucial times. Reading persistence backwards
will eventually lead us to moments of change. James Mahoney (2000) refines this line of
reasoning by emphasizing different types of path dependence. In his typology both ‘self-
reinforcing’ and ‘reactive’ sequences that reproduce institutions over time should be
started from contingent events that trigger changes in institutional design. Other scholars
call for exploring the middle ground between discontinuity and reproduction by focusing
on patterns of institutional evolution. A good example is a recent collection by Wolfgang
Streeck and Kathleen Thelen (2005), which brings together several country studies on
incremental but transformative change. Working around the familiar problematic of
liberalization, these studies identify distinct evolutionary paths that have characterized
the transition out of social market economies in the advanced industrial world.

How useful is historical institutionalism for exploring the remaking of sectoral
regimes in late developers? Given its broader understanding of institutions, its emphasis
on their historical and socio-political embeddedness, and its careful appreciation of
complexity in institutional continuity as well as discontinuity, historical institutionalism
is certainly more qualified for this task than the underdeveloped, ahistorical perspective
implicit in neoliberal institutionalism. And yet it remains rather underutilized by students
of institutional development in market reformers.

The ‘thick’ view of institutions characteristic of this research program is
particularly instructive for identifying the influence of pre-existing institutions over
subsequent institutional paths. It will be argued later in this chapter that the significance
of ‘what already exists’ for ‘what is to come’ in terms of sectoral governance under
liberalization rests on wider patterns of internationalization. For now, let us focus not on why and when pre-existing institutions matter, but how.

I shall cite three possible channels: persistence, evolution, and interaction. First, market reform may not constitute ‘as critical a juncture’ for some sectors and policy areas. In such a scenario, the basic historical institutionalist notions of continuity have broad applicability: If existing arrangements generate overly strong feedback effects or the reform impetus is comparatively weak, policy reorientation may not be sufficient to break through self-reinforcement. This could help account for islands of persistence in seas of change, and could even explain the re-surfacing of old arrangements. The restoration of populist corporatism in Turkish agriculture in the 1990s is an obvious example of this kind of path dependent influence, whereby intensified democratic competition from the late 1980s onwards reactivated the increasing returns from rural side-payments, not only in terms of securing electoral support from the countryside but also by reconstituting party linkages to rural elites and the agrobureaucracy.

Second, recent advances in the study of evolutionary change illustrate how pre-existing arrangements, even when they cannot persist as they are, can be reshaped without significant ruptures in design, and thus pave the way for different configurations. As such, an emphasis on institutional evolution helps explore the vast realm between undiluted persistence and revolutionary reconstruction. One important notion here is institutional conversion, which I employ to describe the transformation of Turkey’s agricultural support schemes in the early 1980s. Streeck and Thelen define institutional conversion as “redeployment of old institutions to new purposes” (2005, 31). Elsewhere, Thelen describes conversion as “institutions being functionally and politically turned on
their heads” (2003, 230). The guiding mechanism for such change is a reorientation of institutional objectives. This may result as much from new environmental challenges as shifts in the collective interests linked to that institution. In both circumstances structure and function are decoupled. Eventually, the same design is put in the service of formerly alien goals. In the case at hand, Turkey’s early neoliberal reformers preserved the pre-existing mechanisms of agricultural support, but managed to smother their redistributive effects under a conservative fiscal policy. When state procurement of important crops slowed down and agricultural credits and input subsidies dried out, the corporatist machine could no longer transfer resources to the countryside. Rather, it was effectively converted into a tool for checking rural incomes.

An equally important evolutionary concept that affords significance to pre-existing institutions is layering, defined as a process of “differential growth” (Streeck and Thelen 2005, 23). This corresponds to a “partial renegotiation of some elements of a given set of institutions while leaving others in place” (Thelen 2003, 225). Layering serves as a useful analogy to trace some patterns of change in Turkey’s fiscal-financial regime. Here, the steady proliferation of new rules, mechanisms, and organizations did not always displace old arrangements, but at times came as extensions of or revisions to pre-existing forms, particularly during the 1990s marked by ‘continuous adjustments’.\(^{18}\)

Another evolutionary pattern involves what I call the regrouping of preexisting arrangements: the Treasury was formed with personnel and resources from the Ministry

\(^{18}\) Note that according to the typology I offer, the main forces behind institutional change in Turkish finance during this period were international norms and coalition politics—due to strong international incentives for sectoral reorganization and high levels of domestic political competition, respectively. That pre-existing arrangements were part of this picture affirms my earlier caveat that variables other than those considered predominant could also have some bearings upon patterns of change. These, however, have little explanatory power compared to the primary explanatory variables. Layering in this example only describes how new arrangements were introduced, and cannot account for why they were introduced.
of Finance; the Capital Market Board (SPK) was the offspring primarily of the Central Bank; the Banking Sector Regulation Agency (BDDK) transferred elements from all four of these organizations, and so on. Some such attempts at regrouping, especially at the micro-institutional level, agree with what John Campbell calls *bricolage*: “actors often craft new institutional solutions by recombining elements in their repertoire through an innovative process of *bricolage* whereby new institutions differ from but resemble old ones” (2004, 69, emphasis original). A clear example is the proliferation of extra-budgetary funds (EBFs) in the fiscal regime, which was based on a reshuffling of existing principles and resources to find pragmatic solutions to new problems. In all these instances of evolutionary change (i.e. conversion, layering, regrouping/bricolage), pre-existing institutions inspire, enable, or constrain subsequent configurations. The point remains, however, that they are not necessarily among the main driving forces behind patterns of reshaping in every instance.

Apart from persistence and evolutionary change, a third way in which pre-existing institutions matter is through interaction and complementarity. Historical institutionalists seldom study a single arrangement. It is more common in this research program to focus on “configurations of policies, formal institutions, and organizational structures” as well as “intersections of organized practices” (Pierson and Skocpol 2002, 707-8). This is indeed something of an analytical necessity, for the institutions that govern modern economies are in a state of complex interaction at all times. The point is thus shared by students of institutions in other fields as well. In fact, perhaps the finest explanation of

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19 As Boyer and Hollingsworth (1997, 53) urge in their noted collection on the structures of contemporary capitalism, “[i]n the real world...any economy consists of a combination of institutional arrangements, all of which complement one another.” Indeed, institutional complementarity is one theme on which some
the connection between complementarity and institutional reshaping comes from a noted economist working in the game-theoretic tradition:

An institution prevailing in one domain constitutes an *institutional environment* for agents in other domains. (…) There can indeed be synchronic interdependencies among institutions emerging as equilibrium outcomes in each game domain. We explore this possibility…whereby one type of institution rather than another becomes viable in one domain when a fitting institution is present in another domain, and vice versa. We call this interdependence institutional complementarity. The presence of complementarity implies that a viable overall institutional arrangement, across different domains, constitutes a coherent whole and individual institutions therein may not easily be altered or designed in isolation (Aoki 2001, 225, emphasis original).

The unusual intertwining of Turkey’s fiscal-financial and agricultural regimes in the 1990s illustrates how complementarity might condition change. In this example, what made possible the reinstatement of rural populism was deficit financing via a highly internationalized, but insufficiently regulated banking system. The resulting fiscal expansion benefited both peasants as its recipients and bankers as its financiers, thereby creating strong incentives for the persistence of populist corporatism in agriculture as well as a relatively lax regulatory environment in banking. Eventually, this odd reciprocity, the two ends of which were connected by fiscal policy, came to work against reform agendas in both sectors. The stronger were the pressures for populist redistribution, the stronger was the need for fiscal expansion, and the weaker were the political incentives for financial reform. The more unruly was the banking sector, the greater were the fiscal opportunities for side-payments, and the weaker were the incentives for subsidy reform.

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groundbreaking research is being done by both economists and political scientists. See in particular Crouch et al. (2005), Aoki (2007) and Deeg (2007).
2.3 Reform Politics: Technocrats, Coalitions, Institutions

Never in history did so many countries simultaneously attempt to reorganize their economies along similar principles as during the rise of free market liberalism during the past quarter century. The political implications of this trend were enormous. In many countries outside the core of global capitalism, this purported move to the market coincided with tumultuous transformations in regime type, triggered the breakdown of long-established state-society relations, and inspired a fundamental reorientation of public bureaucracies. And in virtually all of these countries, both reformers and their adversaries encountered new collective problems they were ill-prepared to solve. A vast political science literature has emerged to analyze these complex issues.

What insights can we draw from this ever-expanding literature for exploring sectoral institutional pathways? The following discussion addresses this question in three parts. It first distinguishes between two modes of market reformism: one is politically insular and based on technocratic decisionmaking; the other involves negotiation and works through coalition politics. In actuality these two modes are often wedded together in various ways, but the distinction is nonetheless important because relative reliance upon one or the other has significant implications. The second part examines some interesting manifestations of technocratic engineering and coalition efforts by focusing on Latin American neopopulisms and public sector reforms in Asia. The discussion then turns to a few studies that share the same focus as the present project—how sectoral institutions are remade under difficult periods of economic transition.
The early literature on reform politics observed that in many countries policy change was spearheaded by small, cohesive groups of technocratic elites. But as scholars quickly recognized, the political sustainability of the reform process would eventually depend on securing support from various social groups by enticing them into reform coalitions. The logic of technocratic reformism and the imperatives of coalition building, however, are in obvious tension. One by definition has to exclude any consideration other than ‘technical’ ones; technocratic ‘change teams’ must be “protected from the pressures of interest groups and bureaucratic rivals,” and for this reason they tend to rely on “executive authority outside of normal institutional channels” (Haggard and Kaufman 1992, 23). The other, coalition building, is not only politically inclusive in principle, but requires some mastery of political tactics to be employed through the usual channels. “The key,” as Joan Nelson (1989, 13) puts it, “is to avoid alienating too many groups at once and to keep potential opposition groups isolated from each other.”

In almost every major ‘emerging market economy’, reform opening saw the rise to prominence of liberal-minded technocratic elites in the economic bureaucracy. Notable examples include Poland’s Balcerowicz Plan (Johnson and Kowalska 1994), Thailand under General Prem (Doner and Laothamatas 1994), Turkey during the first Özal government (Heper 1990a), and China under Jiang Zemin (Xiao 2003). But the influence of technocrats over the reform process is best documented in the Latin American context (Centeno and Silva 1998; Ratliff 1999). Chile, the region’s first market reformer, represents the height of such influence, with a group of US-trained economists, known as
the ‘Chicago Boys’, playing key roles in the country’s orthodox liberalization program under Pinochet’s military regime (Valdes 1995; Huneeus 2000). In Mexico and Argentina as well, “exclusionary technocratic decision-making styles” emerged as predominant by the 1990s, whereby “a very small number of technocratic policy makers insulated from both intra and extra state pressures” had extensive leverage over policy formulation (Teichman 1997, 32).

Technocratic reformism indicates a rather unique policy process. Whereas traditional bureaucratic authority relies on the principle of impersonality, technocrats operate through “narrow domestic personalistic support bases built on trust and personal loyalty” (Teichman 2001, 15). In many cases these personal connections would include close relations with chief executives and some elite factions within the state to culminate in an ‘inner circle’ of reform-minded elites; they might also extend to some prominent members of the private sector to form the basis of reformist ‘policy networks’ (ibid.). This feature of technocratic rule makes it difficult to push the insulation thesis to its extreme. Even in the Chilean case, technocrats established partnerships with other segments of the state elite (Huneus 2000) and proved attentive to, if not fully captured by, the policy demands of dominant industrial and agrarian interests (Silva 1993).²⁰

There are limits to how far (and sometimes, how long) reforms can be imposed from above through technocratic exclusivism. Regardless of regime type, fundamental policy changes cannot be sustained without a sufficient societal support base. Students of reform politics have long maintained that coalition building is the primary means by which market reformers garner such support (Nelson et al. 1989; Haggard and Webb

²⁰ That technocrats cannot indefinitely insulate themselves from everyday politics is perhaps best reflected in the popular 1990s’ notion of ‘technopols’—politically savvy technocratic leaders occupying high executive posts. See in particular Williamson (1994) and Dominguez (1997).
The goals of reform and the requisites of coalition maintenance do not always overlap, though. Striking political alliances entails compromises in resource allocation and is often riddled with collective action problems. Political inclusion exacts unforeseeable costs.

In many instances, early coalition efforts rested on a narrow convergence of interests aimed at neutralizing reform resistance. But as reforms went deeper and distributional costs became clearer, maintaining reform coalitions entailed more political footwork. For instance, ‘second-stage’ reforms, which involve complex institutional reorganization, have typically required “more coalition building, political maneuvering and managerial capacity than did the initial, stabilization-oriented, decree-driven stage” (Naim 1995, 39). Also, reforms create various opportunities for rent-seeking groups, who then may form into ‘distributional coalitions’ to influence the direction of policy and institutional change (Schamis 1999). As in the case of some postcommunist transitions, these rent-seeking groups may successfully block certain elements of reform to create a policy environment favorable to their own interests (Aslund 2002). In order to offset such challenges from losers as well as winners, central reformers may find it necessary to engage in complex alliances based on temporary compromises, such as in Russia (Shleifer and Treisman 2000). These ‘containment’ tactics may succeed in achieving specific policy objectives, as indicated by Brazilian and Argentine experiences with anti-inflationary stabilization (Treisman 2004). But reform coalitions may also undermine the interests of some partners in the long run, as was the case for Chilean and Mexican peasantry (Kurtz 2004). The general point is that coalition politics under liberalization is often characterized by an inherent volatility. After all, the political will to stay the course
may eventually crumble under pressure from competing interests, for which the Peruvian case provides a fitting example (Arce 2003).

In terms of the explanatory variables of this research, then, it is possible to associate technocratic engineering with a condition of insulation: the more insulated the executive authority from societal and intra-state pressures, the higher the political feasibility of technocratic reform agendas. By contrast, coalition politics would follow from a need for societal and intra-state negotiation: the stronger the voice of collective interests, the more urgent the need for deliberation and bargaining, and the more likely policymaking will rely on complex political alliances.

This leaves us but with one important question: Is it possible to find separate junctures of technocratic reformism and coalition politics under market reforms? If it is a tidy separation that we are after, the answer is a resounding ‘no’. Waterbury is right in warning that even authoritarian systems built on formal exclusion “will require careful management of the interests that constitute the regime’s basic support coalition” (1989, 55). And as the below discussion of Latin America’s neopopulisms will show, technocratic agendas may survive even under complex coalition dynamics.

While there is strong evidence for the constant interplay of these two basic modes of reform implementation, the contrasts between the logic of technocratic rule and that of coalition maintenance are still too sharp to ignore. Overreliance on one will certainly curtail the influence of the other over policy and institutional outcomes. In that sense one may argue that they are mutually delimiting, though not mutually exclusive. When technocrats appear to be unconstrained in dictating policy, reform coalitions are typically narrow or strongly skewed toward the preferences of some members. By the same token,
broad and volatile coalitions that require complex negotiation typically compromise technocrats’ hold over policy. It is not uncommon for the political context of reforms to pull in one or the other direction on a hypothetical continuum.

I shall suggest that, in many instances, the intensity of domestic political competition is a useful, if not perfect, criterion to determine whether technocratic insulation or coalitional negotiation will be more prominent in guiding policy. When competition is mild, reformers will be less concerned about losing their support base over to their rivals, and hence more open to technocratic projects unresponsive to societal pressures. By contrast, when competition gets stiff, reformers will be more concerned about expanding their support base, and hence more willing to strike bargains with collective actors at the expense of technocratic exclusivism. A good example is the link between authoritarian regimes and technocratic projects. Earlier literature may have overemphasized this connection while paying insufficient attention to the coalitional foundations of authoritarianism. Yet the general point is sound: more often than not, institutional limits on political contestation make technocratic policy choices easier to implement. The fact that coalition analyses in the 1990s were heavily inspired by earlier theories of democratic transition is quite telling in this regard. The ‘dual transitions’ literature was particularly instrumental in showing how the historic coincidence of democratization and market reforms in scores of developing and postsocialist countries complicated the implementation of unpopular policy measures characteristically

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21 The logic behind this argument parallels Waldner’s (1999) historical thesis that high levels of elite conflict during state building lead to broad, heterodox class coalitions, while lower levels of elite conflict generate narrow coalitions. At a different level, the notion of ‘electoral cycles’ also follows a similar logic. Tough policy choices that could alienate constituencies are more likely to be made during the early stages of political incumbency when direct competition for office is over for a while; but as elections near, politicians will grow more conscious of the consequences of their policy choices for the pending contest, and will gravitate toward more popular policies. Conflict and competition thus encourage political inclusion and coalition-building.
supported by technocrats. Economic crises too can impact the intensity of political competition. Crises typically shake the ruling coalition of interests, delegitimize some factions of the political establishment, and shift attention away from other issues over which political elites compete. As in Argentina in the late 1980s, some Asian countries after 1997, and Turkey after 2000-2001, this may invite bursts of foreign-assisted technocratic stabilization and reform, neutralizing effective contestation over economic policy in the immediate aftermath of the crisis. Yet these episodes are almost invariably followed by attempts to harness broader social support for the new wave of reforms, which may lead to the revival, revision, or replacement of the precrisis political coalition under intensified domestic competition.

Finally, it is important to note that the link between levels of political competition, and thereby different modes of reform implementation, on the one hand, and the outcomes of institutional reshaping for collective interests, on the other, is a complex one mediated by various intervening factors in any context. Even though technocratic insulation in principle precludes non-executive influences over policymaking, institutional reshaping may still benefit attendant interests. This was the case for Turkish bankers in the 1980s; they were unmistakably excluded from the top-down restructuring of the financial regime, but the new configuration, guided by the neoliberal norms of the day, was nonetheless conducive to their interests.

More important, in an open polity and under high levels of competition sensitive to societal negotiation, collective capabilities to manipulate institutional design will vary significantly across social groups: coalition politics is never an ‘equal opportunity’ game.

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Organizational and/or political resources available to collective interests are perhaps the most important determinant; well-organized interests with formidable electoral prowess and actors with strong organic links to executive circles will probably have a better chance to influence institutional pathways. This perhaps was the key factor in the partial defeat of the internationally-supported reform of the agricultural subsidy regime after 2002. Likewise, in the late 1990s, financial rentiers were able to block bureaucratic initiatives toward a tighter regulatory regime in collusion with segments of the political establishment. The balance of the preferences of other domestic actors as well as the content of nondomestic policy pressures could also impact collective capabilities. For instance, neither workers nor industrialists were particularly successful in securing institutional gains during the high competition period of the 1990s, even though they did take part, on and off, in ruling coalitions. In a similar vein, bankers during the more negotiative context of post-2002 politics failed to subvert the consolidation of a highly restrictive regulatory regime in the face of both intra-sectoral divisions and, more crucial, strong support for reforms from industrialists, the ruling party, and international agencies.

Distorted Coalitions, Constrained Technocrats

Coalition politics and technocratic engineering represent two contrasting modes of introducing policy and institutional changes under liberalization. But under different circumstances, these strategies are employed in different ways to different effects. The historical context matters. Below, I resort to two examples to illustrate this point: Latin American neopopulism and Asian administrative reforms. The former shows how in the
absence of a consolidated democracy mass mobilization can be put in the service of technocratic projects; the latter shows how institutional legacies can constrain insulated technocrats in their reformist ambitions.

Since the mid-1990s, students of Latin American politics have frequently pointed out the striking convergence of neoliberal economic restructuring and populist political projects in the region. In countries as diverse as Brazil, Argentina, Mexico, Peru and Venezuela, painful market transitions were often spearheaded by populist leaders who enjoyed considerable support from disorganized masses, but nonetheless relied on technocratic insulation for reform implementation. Leaders such as Fujimori, Menem and Collor “used political populism to impose economic liberalism, and in turn used economic liberalism to strengthen their populist leadership” (Weyland 1996, 9).

This apparent paradox is explained at two levels. First, the historic resilience of populism is traced to the institutional shortcomings of Latin American polities, rather than to any particular model of economic development: “[p]opulism is a perpetual tendency where political institutions are chronically weak” (Roberts 1995, 113); it “indicates a crisis of existing political institutions, and itself constitutes and extends a crisis of political and institutional mediation” (Cammack 2000, 154); “fully institutionalised democracy is an enemy of populism” (Philip 2000, 220). There is no reason, then, to associate personalist, plebiscitarian mobilization of mass support exclusively with state-led development. Second, not only populism can survive economic liberalism, but it thrives under it because of the affinities between the two. Weyland (1996; 1999; 2003), for instance, observes that both populism and neoliberalism have an anti-status quo orientation; they share an anti-establishment, anti-elite discourse; they are
both reluctant to embrace organized interests and collective identities; and surprisingly, both attempt to garner support from the same social strata: “neopopulist leaders appeal for support especially to the largely unorganised informal sector and the rural poor, and neoliberal reformers and the international financial institutions benefit these sectors with targeted social emergency and anti-poverty programmes” (Weyland 2003, 1098-9).

A series of empirical analyses reveals the connection between market reforms and populist politics more clearly. In his study on the Fujimori regime in Peru, Roberts (1995) not only explores how neoliberalism was implemented through political populism, but also draws attention to signs of economic populism at the micro level. Gibson (1997) discusses how Peronism in Argentina and the PRI regime in Mexico combined metropolitan-policy and rural-electoral coalitions in a populist political project in the course of market reforms. Leaman (1999) argues that Menem’s populist liberalism served as a dominant ideology during Argentina’s neoliberal restructuring. After showing that classical populism did not necessarily involve fiscal profligacy, Knight (1998) points out how Salinas successfully combined populism with economic liberalism in Mexico. Interestingly, in his institutionalist analysis, Philip (2000) maintains that opposition in Mexico as well was riding the populist train under Cardenas. Murillo (2000) problematizes the interactions between populist parties and labor unions during the implementation of neoliberal reforms in Mexico, Venezuela and Argentina. Ellner (2003) stresses both the successes and failures of neopopulism in Peru and Venezuela with special reference to the mobilization of support from the informal sector.

The literature on neoliberal populisms confirms a point that is frequently emphasized by students of Latin American politics—that pre-existing political
arrangements can be successfully redeployed in the service of market reforms.\textsuperscript{23} Perhaps more important for the present study, it also warns against a premature assumption of congruity between popular political mobilization and meaningful coalition politics. Evidence from Latin American neopopulisms supports the thesis that political competition does compel reformers to expand their social support base through coalition efforts. And yet it also strongly affirms the caveat that the effectiveness of collective action through coalition politics is contingent upon the wider historical-political context.

The recent experience of some Asian countries with administrative reforms offers a similar reality-check about technocratic reformism. Governance and public sector reform initiatives promoted by the IFIs since the mid-1990s illustrate classic attempts at institutional monocropping to be implemented by technocratic reformers. Little policy advice goes into ‘complementing’ the institutions that operate at the local scene when these very structures are considered potentially corrupt, inefficient, and thus detrimental to growth.\textsuperscript{24}

The idea of governance reform has heterodox intellectual origins. One obvious source of inspiration is the original NIE framework which portrays the early constitution of rule of law and a liberal regime of property rights as the main engine of capitalist growth in the West. Another one is the ‘second stage’ or ‘second generation’ reform arguments in the 1990s, which ran parallel to the IFIs’ acknowledgement of the need to expand the scope of their development policy advice from macroeconomic measures to

\textsuperscript{23} Likewise, Teichman (2004) argues that Chilean and Argentine leaders relied on the region’s specific form of patrimonial rule—\textit{caudillismo}—to instigate sweeping market reforms through technocratic rule. Levitsky (2001; 2003) suggests the informal and highly decentralized party organization of Peronism proved instrumental to mobilize support for reforms particularly from the informal sector.

\textsuperscript{24} For reforming \textit{public institutions}, the World Bank vocabulary shifts unmistakably away from the idea ‘complementing’ the institutions on the ground, which implies, albeit rhetorically, a possibility of translation. Instead, countries are recommended to “\textit{start} with what exists” and then “\textit{deepen} the Bank’s analytic work” (2003a, 1). This is akin to the crude idea of transplantation criticized by many.
other policy areas (e.g. Naim 1995). A third is the new public management (NPM) literature, which builds on evidence from bureaucratic reforms in some Anglophone countries (most notably, New Zealand) since the mid-1980s, and in turn offers a “shopping basket of different elements for reformers of public administration” (Christensen and Laegrid 2001, 19). It advocates productivity and effectiveness in bureaucracy, underlines the value of ‘customer service’ in government practice, and welcomes the neoliberal agenda of deregulation, decentralization, privatization and contracting out of public sector in search for leaner, flatter organizations (Lane 2005, 5ff). A fourth intellectual precursor to governance reform is the neo-Weberian, state-centric literature of the 1980s, which has been selectively incorporated into the official development discourse since the mid-1990s (e.g. World Bank 1997). In particular, sustained growth in Asia’s interventionist developmental states as opposed to the neoliberal debacles in Africa and Latin America challenged the orthodox idea of a minimalist state and shifted policy attention toward improving state capacity.26

25 For early examples in this literature, see, among others, Nordlinger (1981) and Evans, Rueschemeyer, and Skocpol (1985). Originally, the neo-Weberian overtones of the state-centric approach, especially its emphasis on the centrality of effective public intervention for achieving developmental goals, ran counter to the market orthodoxy of the 1980s. Its subsequent incorporation into mainstream development policy advice is quite problematic, too. First, state-centric research does not envision state capacity and effectiveness as qualities that can be obtained on command. Rather, state properties are a function of prevailing state-society relations on the ground (Migdal, Kohli, and Shue 1993; Evans 1995); state capacity, for example, develops through macro-social, historically specific processes, including colonial legacies (Migdal 1988; Kohli 1994). From that perspective the notion that state capacity can be improved via short-term interventions from outside and above is questionable. Second, while scholars in this literature insist on the growth-promoting effects of Weberian bureaucracies and call for their strengthening in the developing world (Rauch and Evans 1999; Evans and Rauch 2000), most public management reform ideas are rooted in a stingy critique of traditional, rational-legal bureaucracies that have characterized the Western scene for almost a century (Pollitt and Bouckaert 2000, 58ff). NPM, for example, directly challenges this Weberian model (Christensen and Laegrid 2001, 13).

26 See, for example, Geddes’ (1994) game-theoretic work on building state capacity in Latin America.
East and South East Asian cases offer useful comparative insight in this regard.\textsuperscript{27}

In the wake of the 1997 crisis, Asian public sectors came under much pressure. Liberal policy analysts and multilateral agencies associated Asia’s economic ills partly with some traditional characteristics of Asian public bureaucracies, which, according to this diagnosis, harbored corruption and inefficiency. In the face of the international policy pressures already in place and widespread public dissatisfaction at home, many Asian governments were compelled to try their hands at administrative reform. The story of these attempts is a familiar one of considerable variation between countries in terms of design, implementation and outcomes. Thailand, for example, was caught in a vicious reform cycle whereby successive unstable governments would potter around complex proposals with little progress (Bowornwathana 2001). South Korea, on the other hand, established a special agency to coordinate reform efforts (Government Reform Office) and embarked on an ambitious reform path in the context of a social compromise between the government, business and labor. Yet there might be an order to this variation, too. One comparative model, for instance, finds that in instrumental bureaucratic systems with strong central executives (e.g. Malaysia and Singapore) reforms are likely to conform to prevailing patterns of ‘continuous self-improvement’; in contrast, in more autonomous bureaucracies (e.g. Taiwan and Thailand) reform attempts tend to end in gridlock or require deeper political reform (Painter 2004). If there is one commonality between these diverse routes, it is the impact of individual bureaucratic traditions and power structures on reform outcomes, which in most cases have translated into a slow process of reform, shielding pre-existing regimes from abrupt destruction

\textsuperscript{27} See Bresser-Pereira (2004) and particularly Schneider and Heredia (2003) for insights from non-Asian cases of governance and administrative reform.
(Cheung 2005). Consequently, even in an issue area where institutional reform does not directly concern collective interests outside the state and where there are strong international incentives for convergence on similar principles, technocratic reformism could be seriously constrained by domestic legacies.

Reforming Sectoral Institutions

Many of the works cited from the wider literature on market reforms so far share a common foible. They often deal with institutional problems, and sometimes come close to offering institutional analyses, but seldom do they employ a coherent perspective on institutional pathways.\(^{28}\) And even fewer studies focus on the trajectory of sectoral arrangements. Below I take a quick look at some examples of such rare effort.\(^{29}\)

Juliet Johnson’s (2000; 2001) careful analysis of Russia’s disastrous financial affairs in the 1990s calls for a careful look at the problem of institutional legacy. Johnson criticizes the Western as well as Russian misperception that when the Soviet regime collapsed the Russian scene presented policymakers with an empty institutional space. Instead, “the Soviet system bequeathed Russia a dazzling array of institutional forms that refused to vanish on command” (2000, 20). Institutional legacies are therefore important. Yet Johnson’s analysis is also an important break from the standard applications of this notion in that it considers the effects of these legacies as “contingent upon the type of

\(^{28}\) The typical treatment institutions receive from students of reform politics is one of implicit, last resort independent or intervening variable. In that sense, the rediscovery of institutions in social science research has created an interesting comfort zone for reform analysis. When all other things are in flux it is handy to look in the direction of elements that seem to solemnly work in the background. Perhaps the most common instance of this is the frequent use of the notion of ‘institutional legacies’, which is often thrown into the mix of factors that could account for irregularities in the reform process.

\(^{29}\) Other notable examples include Luong and Wienthal (2004) and McDermott (2007a; 2007b).
policy choices made by state actors” (2001, 256). Institutional legacies are a lot more important when policy actors opt for passive institutional design schemes, which, rather than try to transform the existing arrangements, “introduce broad measures designed to alter the behaviour of institutional actors” (ibid., 257). Examples of this involve privatization, deregulation, and similar state withdrawal measures. Legacies are less important when state actors choose active institutional design schemes that directly transform existing arrangements or replace them with new ones. In the Russian case policymakers continually relied on passive schemes that amplified the legacy of an institutional framework that was already incompatible with the goals of reform. In turn, the convergence of bad policy with unfavorable legacies bore disaster. In the typology introduced earlier, Johnson’s analysis highlights the interactions between pre-existing institutions, technocratic reformism, and, to some extent, coalition politics. She calls this approach path contingency.

But what happens when the institutional space is truly empty? Timothy Frye’s Brokers and Bureaucrats (2000) deals with this scenario of building institutions from scratch. Frye investigates the emergence and performance of self-governance organizations (SGOs) in five currency, commodity, and corporate equity markets in Moscow. Some of these attempts at self-governance succeeded regardless of organizational disadvantages, whereas some others failed despite favorable circumstances. What explains this unlikely outcome? Frye’s political approach to the problem argues that variations in state policy across markets weighed heavily on the fortunes of these SGOs. By delegating governing authority to some SGOs but not to others, state agents created an uneven playing field. Interestingly, what lay underneath
this policy variation was not any rational organizational calculation but plain, simple
bureaucratic infighting: in a context of intense bureaucratic competition, state agents used
the weapon of authority delegation “as a strategy to entrench their position within the
state” (2000, 216). Frye’s book has several other implications for other fields of study, but for our purposes its message is clear: the state casts a very long shadow. Its influence
over evolving forms of governance is not limited with strategic policymaking.

Richard Snyder’s (1999a; 1999b; 2001) analysis of the rural institutions of market governance in Mexico engages a similar problematic, but this time from the standpoint of coalition analysis. Neoliberalism hit the Mexican countryside hard, destroying the historic arrangements of corporatist governance. Reforms transformed the property regime, dismantled public enterprises and eliminated subsidies. Deregulation did not pave the way to self-regulating rural markets, however. Instead it triggered “a complex landscape with different types of institutions for market governance that connect producer organizations, government actors and private actors in novel and often surprising ways” (1999a, 1). Snyder’s subsequent work (1999b; 2001) on the coffee sector details this complexity of institutional pathways. In some Mexican states (Oaxaca, Chiapas) attempts at reregulation yielded participatory institutions; in others (Guerrero, Puebla) this process ended up with the construction of exclusionary frameworks. Snyder accounts for this sub-national variation by employing a two-step approach, which “connects reregulation projects launched ‘from above’ by political incumbents to responses to these projects ‘from below’ by societal groups” (1999b, 174). In explaining why politicians settle on different projects and how societal actors respond to them, Snyder invokes variables as diverse as regime institutions, policy repertoires, social
mobilization strategies and traditional elite interests. Among the three authors under review, Snyder comes closest to offering a fully-fledged analytical framework for explaining institutional pathways, albeit only with regard to the emergence (and not evolution) of new arrangements.

These three pieces of scholarship underscore similar basic themes about patterns of institutional reshaping in contemporary late developers: forging institutions in reform settings is an exceptionally complex and unpredictable process; institutional legacies have differential, not uniform, effects; what goes on inside the state and outside of it are intricately linked; strategic behaviour of collective interests is integral to institutional change; both macro- and micro-level variables must be taken under consideration. Overall, these points confirm the basic contention of this chapter—that a monocausal approach is unlikely to offer sufficient insight into institutional pathways under liberalization. What we need is a synthetic perspective which can capture the interactions between several variables that contribute to this process.

2.4 Internationalization: The Missing Link

There is but one commonality between the numerous research avenues discussed so far—an overwhelming reliance on domestic-level explanations. The current economic wisdom agrees with historical institutionalism that existing institutions are primarily the long-term products of endogenous political-economic relations. The critiques of neoliberal institutionalism argue transplantation is a flawed idea precisely because of that. Various studies on reform politics pay considerable attention to international compulsion
in accounting for reform opening and implementation, but differences in reform paths and outcomes are usually explained via domestic variables—the domestic macro-institutional sphere, strategic policy choices, collective action, and so on. These are also the variables most emphasized in the few works on sectoral institutional change briefly introduced above.

This is an indefensible analytic proclivity given that liberalization everywhere is accompanied by increased economic and policy internationalization. At a most general level, market reforms in the periphery have entailed the replacement of inward-oriented development strategies, notably import-substituting industrialization (ISI), with outward-oriented ones, such as export-led growth (ELG). Integration with international markets and exposure to global policy pressures have been a central thread in the story of market transitions in the developing world. The influence of these nondomestic variables over the reshaping of sectoral institutions cannot be ignored.

In contrast with the domestic bias in most analyses of sectoral institutions in late developers, this study argues that, until recently, the principal explanatory difference between Turkey’s fisco-financial and agricultural regimes has been the respective positions of these sectors vis-à-vis economy-wide patterns of internationalization. Specifically, it contends that because the dynamics of market integration and policy exposure at the time of reform opening posed different challenges for Turkish finance and agriculture, Turkey’s early market reformers in the 1980s settled on different paths of institutional reshaping in these sectors. In finance, reformers had to come up with a new framework. The switch to export-orientation, the growing reliance on foreign credit, and policy compulsion from international agencies rendered it inescapable to build a liberal
financial environment in tune with the paradigm shift in the global policy wisdom in finance. Conversely, in agriculture, reformers had the freedom to make do with the existing framework: the sector did not have any significant comparative advantage; agricultural commodity prices were depressed around the globe; and there was no discernible nondomestic policy pressures concerning institutional design.

These divergent paths, one leaning toward innovation and the other toward accommodation, were broadly reinforced in the 1990s. Unchanged patterns of market integration and weak external policy pressures in agriculture shielded the support regime from the potentially transformative impact of shifting global norms in rural market governance. Meanwhile in finance, accelerated integration with international markets fostered a process of innovative convergence on global norms, especially earlier in the decade. These externally-generated incentives weighed heavily on domestic collective struggles over institutional design during the negotiative 1990s: in agriculture the fusion of accommodation and negotiation ensured the restoration of populist corporatism; in finance the combination of innovation and negotiation permitted only selective adjustments. In short, the general course of reshaping was dictated from outside in both sectors, although attendant interests, when given the chance, strived fiercely and at times successfully to manipulate the way Turkish governments navigated these sectoral courses. This game would be repeated, just as vibrantly, during the postcrisis period as well.

The literature on exogenous influences on domestic policy and institutional change is vast, reflecting the numerous channels and the complexity of this process. The most common approach is to focus on how exogenous phenomena could alter the
preferences of domestic collective and policy actors. Events as diverse as international economic crises (Gourevitch 1986), changes in relative prices (Rogowski 1989), the rise and decline of a hegemon (Loriaux 1991), and changes in levels of capital flows (Chaudhry 1997) could facilitate a reshuffling of collective interests and a reorientation of policy goals. This in turn will have far-reaching implications for domestic institutions. A more elaborate version of this basic pattern is offered by Garrett and Lange (1995). The model they propose also allows for ‘endogenous’ institutional change through feedback effects from existing socioeconomic and formal public institutions.

At this level, the principal question for sectoral institutional analysis is the extent to which domestic arrangements are reshaped along norms and principles that originate in other social contexts, that is, the scope of institutional convergence. This theme has triggered a voluminous comparative political economy literature that focuses on the experience of advanced economies (e.g. Berger and Dore 1996; Kitschelt et al. 1999; Hall and Soskice 2001; Morgan, Whitley, and Moen 2005). Here, evidence points to substantial sectoral differences. In some sectors, countries are inclined to converge on emergent international norms (e.g. Thatcher 2004). In others, policymakers have the luxury to work around the variations of pre-existing domestic institutional themes (e.g. Thelen 2001). What accounts for this differential impact of international norms, the examples of which also abound in the developing world? My position is that the sectoral effects of internationalization are an important part of this puzzle. In particular, I suggest that external norms and principles will matter considerably more when wider patterns of market and policy internationalization create strong incentives for reorganization of economic activity in a given sector, and considerably less when they do not.
Before I explicate this argument, a few words on internationalization: By the term ‘internationalization’ I try to capture two related but nonetheless different phenomena: increased exposure to transborder market forces and relations, and increased exposure to transborder policy pressures. A rather narrow understanding of the former dimension of internationalization would emphasize “processes generated by underlying shifts in transaction costs that produce observable flows of goods, services and capital” (Milner and Keohane 1996, 4). Internationalization in that sense refers to market integration, and denotes increased levels of market exchange between domestic and non-domestic actors based in principle on their price-driven preferences. Equally important is the policy context of this increased interaction. Internationalization in this second sense means that “policies within domestic jurisdiction face increased scrutiny, participation, or influence from transnational actors and international institutions” (Bernstein and Cashore 2000, 72). I take the wider pattern of internationalization of a country as a function of both these dimensions. Position in the international economy, perceived comparative advantage in certain goods and services, preferences of international market players, relative dependence on or freedom from the IFIs, and membership in regional, international, and supranational organizations will influence the extent and terms of nondomestic influences. Around these incentives and constraints, countries develop specific strategies of internationalization (Palan and Abbott 1996).

How do these different dimensions of internationalization play out at the sectoral level? Let us first look at internationalization as market integration. Here, focusing simply on the integration of the sector in question is not always a sufficient benchmark for tracing institutional trajectories. Rather, we need to maintain a holistic, economy-wide
perspective, for two reasons. On the one hand, inter-sectoral linkages might render the organization of economic activity in a sector—from which I understand the size, structure, ownership, and production profile of firms, prevailing linkages with other sectors, intra-sectoral distribution of resources, and overall levels of productivity and competitiveness—unfeasible for the country’s preferred mode of integration, even if the sector in question is not at the forefront of this effort. When a sector creates such a comparative disadvantage, rulers will be inclined to encourage reorganization by attempting to redraw the rules of the game, that is, the institutions governing that sector. As such, a sector might be a slow internationalizer, and yet its governance might need to be profoundly reshaped due to integration in other domains. This was the case for Turkish banking in the early 1980s, for which manufacturing export-orientation was an important catalyst for overall reorganization (due to an increased need for trade financing and foreign exchange operations), which was largely accomplished through institutional reforms that altered the incentive structures in the sector. On the other hand, if a sector is already endowed with features conducive, or at least not inimical, to the wider patterns of integration, there will be weaker incentives or even disincentives for reorganization, regardless of the intensity of market exposure in that sector. In this way, a leading internationalizing sector may well experience relative institutional stability. This roughly corresponds to the experience of Turkish manufacturing since the late 1980s, in which continued immersion in export markets has not provoked a comparably intense remodeling of sectoral governance. This is not to suggest that sectoral patterns of integration are unimportant; most of the time, as in the case of Turkish agriculture, they tell a crucial story. The point, rather, is that there is no necessary correlation between the
intensity of market integration and incentives for reorganization, and thereby the need for substantive institutional recasting, in a given sector. A ‘big picture’ approach yields more accurate conclusions.

Incentives for sectoral reorganization can follow not only from wider patterns of market integration but also from external policy pressures. In fact, the link between international constraints and sectoral institutions is often much more direct at this level, for the main instruments of external policy pressure, that is, international, regional, and supranational organizations and arrangements, are also the main agents of normative diffusion and may even serve as breeding grounds for new global norms.\(^{30}\) For this reason, countries’ level of exposure to such agencies and arrangements is in itself an important factor, since higher levels of exposure often augment the relative weight of international paradigms for institutional pathways. No wonder the most sweeping institutional reforms in Turkey were carried out during the two most intense episodes of IFI influence, in the early 1980s and the early 2000s.

But here again, there is room for nuance. First, there is considerable variation in the way policy pressures embody international norms. Part of this stems from the different capabilities of international policy actors and arrangements. In principle, organizations and arrangements have more clout if they govern domains in which emergent norms and the requisites of market integration intersect; the WTO, the NAFTA, and in part the EU are examples of this. By comparison, the OECD, for instance, which

\(^{30}\) For example, the World Bank has been instrumental in the growth and consolidation of global norms about corporate governance and fiscal and public management; the Organization for Economic Cooperation and Development (OECD) has long championed an anti-interventionist agenda in agriculture; the current norms on banking regulation can be traced directly to the efforts of the Bank for International Settlements (BIS) since the late 1980s; and regional and international agencies such as the World Trade Organization (WTO), the European Union (EU), and the North American Free Trade Agreement (NAFTA) have been at the forefront of the consolidation of the norms that underpin international trade.
operates largely as a think tank that produces policy advice on a wide range of topics, is less instrumental in pushing for institutional convergence. Perhaps more important, international agencies tend to concentrate on ‘problem sectors’ and policy domains where there is a greater perceived need for reorganization due to past market failures. The Asian Crisis of 1997 was followed by an explosion of international policy pressures for corporate governance, financial sector, and public management reforms in the region. In Turkey after 2000 as well, reform compliance in fiscal and banking regimes was a more pressing concern for the IMF and the World Bank than in social security or anticorruption. In short, incentives for sectoral reorganization due to external policy pressures depend not only on the level of exposure to international policy actors, but also on the capabilities and strategic preferences of these actors.

Second, just as pre-existing institutions vary in their self-reinforcing properties and some collective actors are better-equipped to advance their design preferences under coalition politics, so international norms display a remarkable variation in strength and coherence across different sectors and policy areas. This in turn impacts their effectiveness in inspiring new institutional configurations. For example, especially in finance, but in industry as well, neoliberal principles spread rapidly and forcefully, leading to a succession of rich interpretive frameworks that encouraged (if not ensured) institutional convergence along new norms. In agriculture, by contrast, policy debate in dominant centers has been deadlocked over issues of what Juliet Johnson (2001) calls “passive institutional design”, such as deregulation. As a result, until recently, global policy wisdom in agriculture offered relatively little in the way of new institutional designs, and remained more tolerant of versions of pre-existing arrangements. This
variation in the characteristics of global norms becomes a constraining factor when stronger incentives for reorganization arise. Diffuse and underdeveloped normative frameworks tend to curtail the efficacy of external policy pressures.

The hypothesis as to the link between patterns of internationalization and the significance of international norms for sectoral institutional pathways can now be more explicitly formulated. When wider patterns of market and policy internationalization entail substantive sectoral reorganization, rulers will be more inclined toward institutional innovation. In doing so, it is likely they will take reigning international norms about institutional design very seriously. The perceived inevitability of reorganization undermines the ideational legitimacy of and, through this, usually the societal support for pre-existing arrangements, and makes reformers much more receptive to alien design parameters that are often championed by multilateral agencies as well.

Conversely, weaker nondomestic incentives for sectoral reorganization will limit the significance of international norms for institutional pathways. Such sectors, even when enlisted for institutional reform, will be more likely to be characterized by weak reform compliance and slow convergence on international norms. In this second scenario, rulers will be less eager to face the uncertainties of building novel institutions. In turn, the dominant mode of reshaping will be one of accommodation, in which new policy challenges will be addressed, as much as possible, within the confines of arrangements already in place. Obviously, this will accord significance to pre-existing institutions. How existing designs could matter has been discussed earlier in this chapter: they may either assure relative stability or allow for only slow, limited adjustments. In the presence of
strong institutional interaction and complementarity, such evolutionary patterns can also impact regimes that govern other sectors and policy domains.

2.5 Some Affinities

This chapter has discussed the explanatory variables of the research, that is, pre-existing institutions, technocratic engineering, coalition politics, and international norms. Two conditions have been specified to gauge the relative significance of each of these variables for institutional pathways. First, the sectoral impact of economy-wide patterns of market and policy internationalization assigns different weights to pre-existing institutions and international norms. It does so by rendering innovation more attractive or less attractive for policy and collective actors. Second, the intensity of domestic political competition helps us determine whether technocratic engineering or coalition politics would carry more weight. What is at stake at this level is the degree of societal and bureaucratic influence over the policies that decide the fate of sectoral regimes. It must be reiterated that the argument I make here is about relative effects. At any given time one can reasonably expect all four variables to have some impact on resultant configurations. What I am suggesting is that only some (specifically, two) will have a decisive influence.

In closing, I reflect on some affinities across these variables. These are two: between technocratic engineering and international norms, and between coalition politics and pre-existing institutions. The co-existence of the first pair generates a type of reshaping I have specified as insulated innovation; the second pair leads to a different type, negotiated accommodation. I will argue below that the synergies between the
variables that underlie these two types produce more dramatic examples of institutional change and persistence.

Let us first look at the affinity between technocrats and international norms. In the previous section I have suggested that the urgency of sectoral reorganization would encourage innovations in regimes of governance, amplifying the significance of international norms in the process. Technocrats are particularly well-positioned to instigate such innovations. First, insofar as they can retain their autonomy from everyday political pressures, they may be immune to the feedback effects associated with pre-existing arrangements, catching social coalitions supporting these arrangements off guard. Waterbury’s (1993, ch. 5, 7) comparative analysis of public sector reform offers several examples of how technocratic teams can punch through old coalitions.31 Second, relative insulation from intra-state pressures may help technocrats overcome bureaucratic inertia. Williams (2002), for instance, shows how Mexican and Argentine technocrats served as agents of institutional innovation through rule-changing, instrument-creating and strategizing behavior. Third, at least partial autonomy from domestic struggles combined with the foreign training of most technocrats make them suitable catalysts for policy and institutional diffusion, especially as “interlocutors between the state and multilateral lending institutions” (Teichman 2001, 202). Thus, the policy dimension of internationalization can permeate the domestic scene much more effectively during periods of technocratic rule.

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31 Waterbury’s cases include Egypt, India, Mexico and Turkey. His conclusion as to the tension between technocratic teams and old coalitions is especially instructive: “[D]efense of the old pact arrangements is a collective good…and no single entitled interest would have any incentive to contribute to it. Rather, these interests have tried to defend their particular entitlements, allowing determined change teams at the highest political levels to pick them off one at a time” (Waterbury 1993, 264).
In order for technocratic engineering to work in tandem with international norms as dominant factors in the shaping of sectoral institutions, we need a context marked by low levels of political competition and strong international impulses for sectoral reorganization. This corresponds to insulated innovation. My research involves three cases of this type: finance (1980-1986); finance (2000-2002); and agriculture (2000-2002). Unsurprisingly, these cases also represent the most dramatic ruptures in the institutional trajectories of Turkish finance and agriculture, whereby entire regimes were uprooted and redrawn.

The second affinity is between coalition politics and pre-existing institutions. I shall cautiously argue that, just as there is a technocratic predisposition to innovation, so there is a coalitional predisposition to accommodation. The reason is simple. In principle, political bargaining augments the leverage of collective interests that stand to gain from prevailing arrangements even under policy shifts. Hence, coalition politics is more easily put in the service of defending pre-existing institutions. This connection probably lies at the heart of a great many stalled or subverted reform attempts in the developing world. Dismantling or substantively transforming an arrangement is not permissible if it is dear to some important members of a ruling political coalition; selective reorganization or pragmatic adaptation is a more opportune route. This affinity holds true when formulated from the internationalization side of the main argument as well. Weak international incentives for reorganization that convince rulers to stay within the confines of pre-existing arrangements will only make policymaking more susceptible to the preferences of collective and state actors that have a stake in the persistence of these arrangements.32

32 There are numerous reasons for caution in advancing this second argument. Organizational weaknesses on the part of collective actors may impede their ability to defend an arrangement even when they appear to
Coalition politics and preexisting institutions can serve as dominant factors only when domestic political competition is high and international incentives for sectoral reorganization are weak. This in turn generates a type I have called *negotiated accommodation*. Compared to its insulated variety led by technocrats, negotiated accommodation could be expected to produce less dramatic changes due to stronger influences by collective interests. My analysis includes a single example of this type: agriculture (1987-1999), which was marked by some adjustments in sectoral governance but, more importantly, a forceful resurrection of past designs. In the process, antiquated forms of rural populism resumed and corporatist channels of cooptation regained ground despite changing environmental realities.

Reformers can exploit coalition dynamics to isolate some sub-groups while rewarding others. Other variables, such as international constraints or economic crises, may trump collective preferences and sway the outcomes of political negotiation in the direction of innovation. Or collective interests may simply shift under long episodes of policy change and internationalization, diminishing the distributive gains from old arrangements. In all these scenarios, coalition politics will eventually contribute to institutional innovation. In fact, *negotiated innovation* is perhaps the most common route to institutional reorganization in today’s late developers. Nevertheless we can reasonably expect that, compared to technocratic engineering, the outcome of coalition politics will less likely reflect institutional blueprints originating from abroad, but rather involve significant compromises in design, especially when popular interests are at stake.
CHAPTER THREE

COMMON LEGACIES

This chapter examines the financial and agricultural regimes of governance inherited by Turkey’s neoliberal reformers. Its work is largely descriptive, focusing on over five decades of institutional development. Such an historical account is crucial for understanding both the background of the configurations enlisted for change under liberalization and the class and political dynamics that characterized Turkish finance and agriculture at the time of reform opening.

Formally, the arrangements that governed these sectors in the postwar decades could not be more different. The financial regime by today’s standards was quite lean and straightforward. It relied on a couple of large, universal public bodies, the Ministry of Finance and the Central Bank, which together enforced a strategy of financial repression. Conversely, agricultural governance depended on populist-corporatist support schemes embedded in a stupendous web of state and parastate organizations. Compared to its counterpart in finance, the regime that governed rural markets was much more decentralized and was inescapably open to everyday political influence.

But behind this formal variation there was a degree of functional uniformity. Especially after the institutionalization of development planning in the 1960s and in the context of a fairly coherent policy of import substitution, financial and agricultural regimes could not escape the exigencies of the wider developmental project. I will argue that these distinct patterns of governance ensured the successful incorporation of Turkish
peasants and bankers into a series of social compromises that upheld the country’s inward-oriented, state-led strategy of industrialization. That the Turkish state was not a mere regulator but by far the strongest and most cohesive economic player in both sectors rendered this link even stronger.

In essence, what we have here is a neutral trajectory accessible through standard historical institutionalist notions of origination, continuity, and change. Both regimes emerged during a long period of crisis and adaptation that can be perceived as a critical juncture; they then evolved in ways that often reflected the gradually shifting preferences of the social and political interests they embodied; and over time they got so deeply entrenched in the fabric of the Turkish political economy that substantive transformation became progressively difficult. What separates this evolutionary pattern from the way these institutions were to be reshaped under liberalization is the absence of discernible international constraints and powerful technocratic initiatives. In the postwar decades, institutional development in both sectors relied on a mixture of societal bargaining and self-reinforcement, which permitted only limited and highly deliberated modifications on a stable path. Seen through the typological framework I have proposed, these common trajectories exemplify one overly long episode of negotiated accommodation.

3.1 The State, ISI and Capitalist Development in Turkey

Let us begin by examining the legacies of state interventionism in Turkey and how they fit the inward-oriented industrialization strategy that preceded market reforms. When Turkey embarked on a path of import-substituting industrialization (ISI) in the
1950s and more openly in the 1960s, it was already endowed with a strong tradition of state intervention in the economy. At its height, the Ottoman Empire, founded upon the Byzantine legacy of a powerful central administration, was a bureaucratic giant relative to the absolutist state systems of sixteenth century Europe. Yet by the end of the eighteenth century, the bureaucratic kernel of the Ottoman state had been severely weakened, largely as a result of the diminished redistributive capacity of a steadily shrinking imperial order. In much of the nineteenth century, the country had little room for maneuver other than reluctantly to fall on a path of dependent incorporation into the world capitalist system. As crafts and proto-industries steadily declined, trade integration degenerated into a classic pattern of non-manufacturing exports, particularly from the Western provinces that saw a spread of commercialized agriculture (Owen 1981, 200ff; Pamuk 1987; Kasaba 1988). In the face of rising domestic commercial interests inside and European political and financial encroachment from outside, Ottoman rulers tried to restore the bureaucratic power of the center through a series of modernizing reforms. At the core of these efforts was the cultivation of a largely autonomous and reformist military-civilian bureaucratic elite (Karpat 1972; Findley 1980).

Although state restructuring failed to save the empire from its pending disintegration, it was elements from within this reformist bureaucracy that spearheaded a much more comprehensive modernization project under the new republic. This would not bring an immediate break with the prevailing pattern of economic dependency, however. The liberal 1920s continued the hallmarks of peripheral integration with world capitalism (Keyder 1981). Only in the extraordinary context of the 1930s did Turkey’s ‘revolutionaries from above’ (Trimberger 1978), organized within Kemal Atatürk’s
Republican People’s Party (CHP), renounce the economic legacy of the empire and turn decisively toward top-down, state-led industrialization. Several factors converged here. Abroad, the Soviet miracle, the successes of Italian corporatism, and the debunking of free markets as a reaction to the world depression that shook even the traditional strongholds of the “liberal creed” (Polanyi 1957) lent enormous credence to the idea of state intervention. Meanwhile at home it took several years for Kemalist bureaucrats to neutralize rival and socially better connected factions and build sufficient political capital for fundamental changes in economic policy. In addition they were obligated by the terms of the post-independence war treaty to honor the overly liberal Ottoman trade regime until 1929 (Keyder 1987, 91ff). It was this propitious fit between emergent economic norms outside and expanded policy freedom inside that enabled Turkey’s republican rulers to settle on a path of bureaucratic, interventionist developmentalism.

Three aspects of Turkey’s pre-ISI record of state economic involvement are crucial for our inquiry. The first is the emergence of a large public sector (Boratav 1982; Waterbury 1993, 35ff). There were some initiatives toward government control of a few subsectors in the 1920s, such as in sugar, tobacco, alcohol and petroleum, but the 1930s still constituted a radical break with these early attempts. ‘Statism’ was adopted as one of the founding principles of the ruling CHP in 1931, consolidated as official policy through the Soviet-advised Five-Year Plan in 1934, and finally carved into the constitution in 1938. The 1930s saw the surfacing of numerous large scale state enterprises with an emphasis on catering industrial raw materials and intermediate goods, such as coal, iron and steel, cement, paper, glass, textiles and chemicals. The burgeoning public sector was
not limited to industry. As will be examined further below, some key state and parastate organizations in finance and agriculture also originated in the 1930s.

The second is a restructuring of state-society relations, largely along corporatist lines. At the core of the Kemalist world view was an organic conception of the nation, which rejected the idea of conflicting class interests and in turn emphasized the functional complementarity of social groups in a modernizing economy marked by professional specialization (Parla and Davison 2004). This strong adherence to national solidarism among the early republican elites was compatible with state interventionism of all kinds (Richards and Waterbury 1996, 314ff). Out of this fusion of statism and solidarism followed a long-term policy of orchestrating economic interests through quasi-public associations that also provided circles of patronage. Corporatist co-optation was readily visible in agriculture and small business in which interest articulation would increasingly rely on an extensive network of involuntary organizations, based on the French example of professional ‘chambers’. Meanwhile, the nascent industrial bourgeoisie had to strategize around state investment decisions, and as the main beneficiary of state credits and government contracts, was forced to retain a close clientelistic relationship with the bureaucracy. This early interventionist phase would set the tone for interest group politics in Turkey for decades to come, which would decisively lean toward varieties of corporatism rather than pluralism (Bianchi 1984).

Third, state intervention proved resilient regardless of the political fortunes of the military-civilian bureaucratic elite. The transition to multi-party politics led to the defeat in the 1950 elections of the CHP at a time of growing public discontent with bureaucratic tutelage. The succeeding Democrat Party (DP), which ran on a populist platform of
commercial and rural interests, emphasized market values and even unveiled a privatization plan during the early years of its incumbency. But as economic conditions deteriorated and the party’s popularity eroded, the DP would discover the utility of protectionism and an overextended state sector for the co-optation of potential dissidents (Waterbury 1993, 42). The 1950s was therefore a critical period for the consolidation of a wide array of constituencies around a state that was, at least in the short run, perceived as capable of appeasing conflicting collective interests simultaneously. Import substitution would make this reconciliatory political logic feasible in the longer term and within a virtuous developmental framework.

This is an undoubtedly simplified account of Turkey’s pre-ISI politics of state intervention.\(^1\) The general point is nonetheless clear: import substitution was not in defiance of the hitherto evolution of Turkish political economy. Rather, it constituted a logical next step. It would comfortably tap into the prevailing institutional arrangements, of both interest representation and state intervention, for policy reorientation. It would also link bureaucratic reformism with a range of large collective interests around a coherent project that would deliver sustained growth throughout the 1960s and in much of the 1970s. In fact, it would be so successful in patching up otherwise disparate interests and would engraft the prevailing institutional framework so much deeper into the political-economic landscape that it would ossify as the only feasible policy and, in the end, fall victim to its own rigidity.

Import substitution had heterodox origins in the developing world. In his classic account of the Latin American experience, Albert Hirschman (1968) noted that the

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\(^1\) For a vivid analysis of the early consolidation of ‘statism’ in Turkish political economy in light of various case studies, see Tekeli and Ilkin (2003).
adoption of ISI as official development policy had been typically preceded or facilitated by factors such as balance of payments difficulties, wars, and the expansion of domestic markets. This certainly characterized the Turkish experience as well. After the liberal interlude of the early 1950s that ended in an import boom and foreign exchange shortages, the DP re-erected protectionist walls, behind which a frail manufacturing bourgeoisie concentrated its productive efforts on formerly imported simple consumer goods. But only in the wake of the 1960 coup did import substitution become the openly favored and deliberately pursued strategy of industrialization.

Central to this paradigm change was the “‘fit’ between bureaucratic reformism and the ascendancy of the industrial bourgeoisie” (Keyder 1987, 148). The main vehicle for such a fit was the newly established DPT, the State Planning Organization, which was accorded the responsibility of supervising industrialization efforts. The DPT’s five-year plans would form the contours of the development strategy in the medium run. The everyday operation of ISI, on the other hand, depended on a host of policy measures. The most important of these was an import regime that systematically favored industrialists over commercial importers. It did so by implementing a strict quota list that discriminated against consumer imports, by giving manufacturers priority over the allocation of foreign exchange, and by exerting high guarantee deposit rates on consumer imports. Other

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2 The DPT was first designed as a small advisory board, bringing together a group of idealist academics and reformist bureaucrats. But its radical stance on issues such as agricultural taxation, under advisement from British economist Nicholas Kaldor, would soon create a backlash from the political elite. After political rows and a wave of resignations in its first years, the organization was “reduced to what the conservative politicians had originally intended it to be: a bureau to plan government investment.” (Ahmad 1977, 275). Still, government investment decisions during the planned era, the general context of which would be unveiled in the regular Five-Year Development Plans, were aimed not merely at complementing the private sector but rather to guide it through a desired path of industrialization. See also Kansu (2004).

3 Under Turkey’s trade regime at the time, importers were obliged to deposit a certain percentage of the cost of imported goods at the Central Bank as a way to ensure that much too valuable foreign exchange was indeed used for its intended purpose of bringing goods into the country (thus making capital outflow via the
policy measures included an overvalued exchange rate regime, tax rebates for industrialists, and the imposition of often negative interest rates on commercial bank deposits so as to ensure the flow of cheap credit to manufacturing (Barkey 1990, 70-74).

These policy tools, taken in the context of the state monopoly over foreign exchange and a system of strict price regulations, amounted to a fairly closed, inward-oriented economy. Still, the Turkish experience with import substitution is always remembered with a certain fondness even among its liberal observers, and very rightly so given its macro outcomes. Between 1962 and 1976 the Turkish economy grew every single year at an average rate of over 6 percent (DİE 2003). Industry remained dependent on foreign inputs, but it did achieve some deepening and accumulated considerable capital. Most important, this was also a phase of relatively equitable growth, during which time wages and agricultural incomes made significant real gains.

This last point requires elaboration. The Turkish ISI relied on a grand social compromise that joined together the interests of four crucial actors: the bureaucrats, the industrial bourgeoisie, organized labor, and the peasantry. As in a proverbial fantasy tale, these actors had different “powers” at their disposal—the state, private capital, social activism, and numbers, respectively. It must be quite clear by now that this particular strategy of development would appeal to the modernist-reformist bureaucratic elites in its continuation, systematization and in some ways expansion of the pre-existing norms of state intervention. Import substitution would help quell the fears of this stratum about the potentially debilitating effects of electoral democracy over its long-standing omnipresence in Turkish society (cf. Heper 1976a). ISI was obviously a good bargain for private sector improbable). This percentage rate was set differently for commercial importers of consumer goods and industrial importers of capital and intermediate goods.
the industrialists as well, as it not only offered long-term protection from foreign competitors, but came with bonus incentives such as tax rebates and guaranteed access to foreign exchange.

Still, in an open polity, the fit between these two elite groups could not work without the consent of the wider society. Herein lay the significance of taking aboard organized labor and the peasantry. The case of the peasantry will be detailed later in our discussion, but it should be noted here that the cost of gaining the acquiescence of rural producers would mainly fall on the state and therefore the taxpayers. Organized labor, on the other hand, was concentrated almost exclusively in large private and public sector enterprises, and would fully benefit from the liberal political atmosphere ushered in by the progressive 1961 constitution. As a result, from 1963 to 1976, real wages in manufacturing more than doubled (Boratav 2003, 137)—a development that must be fully credited to increased unionization and militant class struggle.4 This was an acceptable price to pay for the big industrial bourgeoisie given the virtues of the system. And obviously, higher popular incomes, in cities as well as in the countryside, meant an ever expanding domestic market for the manufacturers of consumer goods.5

To be sure, ISI had its losers as well, but they did not constitute a qualitative majority either among the elites or the populace. One such group was the petit

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4 Keyder (1987, 161) notes that “wage levels in Turkish manufacturing…were considerably higher than warranted by the relative level of GNP per capita. For example, in 1977 the average daily wage in Turkey was $11.14; this compared with $11.72 in Greece, $20.44 in France and $23.56 in Britain. Per capita incomes in these countries were two and a half, six and four times the Turkish levels respectively. (…) [I]n 1974 Turkish manufacturing wages were three times the level of Korean wages. In 1977 they were double, and in 1979, despite very rapid increases in Korea, still 50 per cent higher.”

5 This is not to say that relations between the state and these social groups were free from problems. Rather, policymaking involved the strategic accommodation of the grievances of these groups that often took the form of open conflict. Here, workers were not the only class driving a hard bargain. The 1970 stabilization measures, which included a devaluation of the Turkish lira and imposed several new taxes especially on industry, for instance, were fiercely criticized by big manufacturers and dealt a serious blow to the state-industrialists alliance until they were watered down in subsequent years (Barkey 1990, 154ff).
bourgeoisie, comprising artisans, shopkeepers and other self-employed groups, which the state sought to co-opt via quasi-public professional associations. Another was commercial importers, who could not compete against the oligopolistic manufacturing bourgeoisie at the national scale. Perhaps the biggest losers were to be found in some segments of small industry, either on the labor or the capital side of the class divide. In subsectors where there was little niche to complement the big industry, competition was fierce and wages were abysmally low: “Small capitalists extracted high levels of surplus value from their workers, which they lost to big capitalists through the market system” (Keyder 1987, 176-7). But even these disadvantaged factions had a stake in the game. Deeper state penetration and the burgeoning of an urban middle class, fast economic growth and an increased sense of social justice in a brand new democracy, all worked in favor of the emergence of a sizeable welfare state for a semi-peripheral country, providing near-universal health care, free higher education and a stable social security regime. The politics of import substitution had intimately linked the four main actors of the compromise mentioned above at the expense of other societal interests, but it also had the grace to offer some compensation to those who were excluded.

The problem with import substitution was its utter vulnerability to foreign exchange shortages. The industry was dependent on the import of investment and especially intermediate goods, but it was not easy to secure a steady flow of foreign exchange for imports when overvalued exchange rates hampered export capacity. Here, agriculture continued to pull more than its weight. Agricultural exports, despite their declining share, still made up over 60 percent of total exports throughout the 1970s (DİE 2003). By contrast, the industry’s drive toward export orientation was quite slow. In order
to offset this chronic problem, Turkish governments continually relied on outside sources of financing: foreign aid in much of the 1960s, workers’ remittances from Europe from the late 1960s up until the mid 1970s, and short-term international borrowing at increasingly unfavorable rates in the latter half of the 1970s.

Eventually this last move toward foreign indebtedness became the string that unraveled Turkey’s import substitution. In 1977 Turkey ran out of foreign reserves and international creditors refused to roll over credits. The government agreed to an IMF austerity plan in exchange for partial debt rescheduling, but stabilization efforts failed in the face of policy stalemate. Turkey’s comparatively early debt crisis deepened in 1978-1979 as foreign exchange shortages grounded domestic industry and quickly translated into shortages of basic commodities. Meanwhile a prolonged political crisis, expressed in widespread civic unrest and street violence between supporters of the extreme right and the left, made impossible the formation of a broad-based policy coalition to tackle the economic crisis. In 1980, these twin crises would be confronted via radical measures by the two wings of the bureaucracy: In January, a faction within the civilian bureaucracy devised a master plan to ditch statist import substitution and move toward neoliberal export orientation. In September, the military bureaucracy stepped in, dissolving the parliament and thus effectively clearing the political clog. It was only behind this

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Different analyses emphasize different dimensions of this ossification of import substituting policies that led to policy stasis in the late 1970s. In his extensive study of the Turkish ISI, Henri Barkey (1990) focuses on private sector cleavages between the industrial and commercial bourgeoisie. Accordingly the roots of the policy paralysis must be sought in the conflicting demands of these two groups, to which weak coalition governments of the late 1970s, much like those throughout the 1990s, surrendered until the system of rent distribution finally collapsed. Korkut Boratav (2003, 139ff), on the other hand, emphasizes the impossibility of retreating from a well-established pattern of populist redistribution toward labor and the peasantry in a context of open class warfare. Çağlar Keyder (1987, 194ff) credits the availability of external funds, especially of workers’ remittances, for the Turkish governments’ ability to insulate the economy from the potentially debilitating effects of the first oil shock, leading to a popular illusion in the remainder of the decade about the sustainability of inward-oriented industrialization regardless of its contradictions.
authoritarian shield provided by the generals that technocratic policy elites could engage in a fundamental reorientation of the Turkish economy in the 1980s. For now, however, we need to go back one step and take a look at the prevailing regimes of financial and agricultural governance to be inherited by neoliberal reformers.

### 3.2 Bankers and Bureaucrats: A Recipe for Financial Repression

It is difficult to speak of a strong and independent financial interest in Turkey before the 1980s. Until then, the Turkish financial system was largely subjugated to the requisites of state-directed industrial development and the constraints it posed on the public as well as the private sector. The outcome was an oligopolistic market structure with growing interpenetration between financial, commercial, and industrial capital. Financial governance in turn was strict and single-handed, but only partially effective.

As in most other sectors, the 1930s and the immediate aftermath of the Second World War appear to be the crucial juncture for the remolding of the Turkish financial landscape. To comprehend the real extent of that break, we shall first glance at the pre-existing financial structure. The empire had bequeathed the young republic some 35 banks, many of which were foreign initiatives set up to oversee European commercial interests. In the latter half of the nineteenth century, the British and the French had made impressive inroads into the Ottoman financial scene (Kazgan 1995). The centerpiece of this effort was the Ottoman Bank, which was founded as a commercial enterprise by

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7 The pinnacle of European financial encroachment was the Public Debt Administration, set up in 1881, following Ottoman bankruptcy in the mid-1870s to ensure the servicing of its foreign debt. The administration effectively took over the public finance regime, and soon started mediating between European investors and the Ottoman bureaucracy. See Owen (1981, 191ff) and Keyder (1987, 39ff).
British capital in 1856 but slid largely under French influence in the 1860s. This joint venture was contracted out by the Ottoman state to serve as the equivalent of a national bank with a monopoly over the issuance of paper money. The bank would continue its public functions during the early years of the republic in addition to its private commercial activities. By the mid-1920s the Ottoman Bank still accounted for more than half the country’s total deposits. The rest was about evenly split between Turkish and the remaining foreign banks, led particularly by German banks (Keyder 1981, 100ff).

Germans were latecomers into the European scramble for exploiting the spoils of the ailing empire, but they had quickly caught up with the rest by winning the favor of the last generation of Ottoman modernizers. As opposed to their British and French rivals, the interests of German financiers went beyond simple trade financing and milking the Ottoman public debt; they were significantly more involved in productive investments, such as in mining and railways (Pamuk 1987). This would not only gain the sympathy of the bureaucratic elite and help expand German influence, but also prove inspirational for the early republican rulers. After all, it was after the German model of industrial banking that the Kemalist modernizers would shape their policies of industrial development. The German legacy of fusing productive and banking capital would also be emulated by the private sector in the wake of the Second World War, paving the way for an oligopolistic market structure in banking (Henry 1996, 98ff).

Shortly after the promulgation of the new republic in 1923, the bureaucratic elite engaged in projects of cultivating national banking. The most significant of these was

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8 The most important Turkish bank inherited from the empire was the Bank of Agriculture, or Ziraat, which in the following decades would become the country’s largest commercial bank with its ever expanding network in the countryside. Yet it was severely undercapitalized at the time, and obviously was not designed to meet wider commercial and industrial needs. Another was the National Credit Bank (İtibar-
the semi-official İş Bankası (Business Bank), established in 1924 specifically with Deutsche Bank in mind, to bring together on a credit platform the reformist bureaucracy, the domestic merchant capital and the fledgling private industry. A second was the official Sanayi ve Maadin Bankası (Bank of Industry and Mines), founded in 1925 to extend credit to the emergent state-owned industry, and a third was the Emlak ve Eytam Bankası (Realty and Orphans’ Bank) of 1926 to meet the financing needs of public construction works (Keyder 1981, 105-6). Still, these early attempts at national banking in the 1920s were far from decisively breaking with the Ottoman legacy of a credit regime which serviced the interests of trade financing and merchant capital (ibid., 124-5).

The 1930s represented a formative juncture for the emergence of a new financial environment in three important respects. The first of these was the creation of the Central Bank in 1930, which would fully take over the official functions of the Ottoman Bank by the middle of the decade (Tekeli and İlkin 1981). The second was the large scale exit of foreign banks from the Turkish economy. This was perhaps more the result of the Great Depression and the drying up of foreign trade behind protectionist walls than the development of national banking. Between 1928 and 1936, the number of foreign banks would be halved, from 18 to 9 (Yüzgün 1982, 18). The third was the dramatic growth of public banking around specific tasks in line with the paradigm shift toward state-led development in the 1930s. Ziraat Bankası (The Bank of Agriculture), which lay somewhat dormant throughout much of the 1920s, was rejuvenated in the face of the price crisis in agriculture. İller Bankası (The Bank of Provinces; est.1933) catered to local administrations; Halk Bankası (People’s Bank; est.1938) was aimed at artisans, Milli), which was not well-liked by the Kemalist elite as it was also wedded to the vestiges of the Ottoman bureaucracy. The rest of the nationally-owned banks were small, local merchant initiatives.
shopkeepers and other small business; and Denizcilik Bankası (the Maritime Bank; est. 1938) helped fund the merchant navy and the construction and maintenance of ports and docks. Yet the most important public banks of the period were Etibank (est. 1935) and Sümerbank (est. 1933), which succeeded the Bank of Industry and Mines, but unmistakably followed the German example of combined financial-industrial conglomerates. Etibank greatly expanded the state’s involvement in mining and energy, while the much larger Sümerbank would form the main driving force behind Turkish industrialization by providing a single roof for public investments in textiles, sugar, leather, paper, iron and steel, cement and so on. Meanwhile the semi-official İş Bankası would support the industrial drive through joint ventures in chemicals and especially in the glass industry (Kazgan et al. 1999, 151ff).

With the state’s overwhelming presence in banking, privately owned Turkish banks remained small and localized throughout the 1930s, although their numbers grew rapidly. At the same time, opportunities presented by chronic commodity shortages during the war, not to mention lucrative government contracts, facilitated the accumulation of considerable commercial capital in private hands. Toward the end of the war large commercial capitalists and would-be industrialists could no longer be confined to small local banks, nor did they always find it attractive to depend on state credit. Thus, from the mid-1940s on, larger private commercial banks started entering the system. One such bank was the Yapı ve Kredi Bankası, established in 1944 by a former state enterprise executive. Another was Akbank, founded in 1948 by a rich group of central-southern Anatolian merchants and proto-industrialists (Toprak 1998).9

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9 Another important private bank established in that period was Garanti Bankası (est. 1946). This trend toward larger private commercial banks would continue in the 1950s, with examples such as Demirbank
By the time import substitution emerged as the openly preferred development strategy, the Turkish financial system featured two major characteristics. First, the Turkish state was there to stay as the largest actor. The pattern of public industrial-financial conglomerates would gradually weaken, but public banks would remain crucial not only for the implementation of statist economic policies, but for political patronage and corporatist interest articulation as well. At the center of public banking, therefore, were preferential credit mechanisms through which bureaucrats and politicians juggled the contradictory tasks of long-term economic developmental and short-term political gain. The epitomes of such dual functionality were Ziraat and Halk, which to this day remain the main sources of credit for farmers and small business, respectively. In a similar vein the old Emlak ve Eytam Bankası was succeeded in 1946 by Emlak Kredi Bankası (Realty Credit Bank), whose functions were reoriented from financing public works toward mass housing projects in an era of rapid urbanization, while Vakıflar Bankası (the Bank of Foundations; est. 1954) managed the accounts of charitable foundations and some civic associations. All of these public banks were also ordinary commercial banks involved in deposit taking and credit allocation; what made them special was that each was strategically positioned to address the banking needs of different clienteles, and in doing so offered channels of patronage between central politicians and various constituencies.

The second major characteristic of the postwar Turkish financial system was the growing integration of private commercial banking and large manufacturing interests. The Turkish industry was credit-dependent in a strictly bank-based financial system (Zysman 1983). A contingent outcome of this pattern was the private sector’s mimicking...
of the government formula of fusing banking and non-banking capital. By the 1970s, all
major private commercial banks were either owned by or affiliated with Turkey’s
industrial conglomerates, typically organized as family holding companies. The semi-
official İş Bankası was itself an industrial conglomerate. Akbank was taken over by the
Sabancı Group, the second largest conglomerate, while the ownership of Yapı ve Kredi
fell to the Çukurova Holding of the Karamehmet family. There was, however, no single
formula of industrial-financial relations in the private sector. The experiences of the three
largest family holdings attest to this. The largest industrial conglomerate of the country,
the Koç Group, was economically so sound and politically so well-connected that it did
not initially make it a priority to have its own bank. 10 Sabancı’s Akbank, on the other
hand, was not itself a source of cheap credit for group companies, but was used to corner
the market on behalf of wider Sabancı interests: “the strategy was to squeeze other banks
into granting cheap credit…to the Sabancı Group” (Henry 1996, 114). 11 Only the
Çukurova Group did what some could reasonably expect of a developing country
industrialist, and increasingly resorted to its own banking capital in Yapı ve Kredi and
Pamukbank to finance the group’s industrial operations. Yet many other smaller groups
would follow in Çukurova’s footsteps in the 1980s and particularly the 1990s. The
smaller the industrial capital, the bigger was the dependence on external finance, and
naturally the more pronounced was the tendency to exploit the group bank.

10 Later, in the late 1970s, its foray into the sector via Garanti Bankası foundered at a time of economic
crisis and rapid policy shift. Only in the late 1980s would Koç return to the banking sector, and via the
much less ambitious Koçbank as a joint venture with American Express.
11 Ironically the biggest recipient of Akbank credits was the Koç Group. It was, in fact, a tidy little
arrangement between Koç, the largest conglomerate, and others (especially Sabancı) that in return for not
aggressively pursuing entry into the financial sector Koç received preferential treatment from other private
commercial banks. It was also good business for these banks as Koç companies were renowned for their
sound financial structures.
Having outlined the evolution and some important features of the Turkish financial system prior to liberalization, we can now turn to the institutional governance of the sector. The organizing principle here was financial repression, enforced in a heavy-handed manner through highly politicized central agencies. Turkish markets displayed all the hallmarks of financial repression typical of inward-oriented, state-induced industrialization throughout the developing world: the state kept interest rates artificially low, and addressed the ensuing excess demand for cheap funds through discretionary mechanisms of credit allocation (Haggard and Lee 1993: 5ff). As in most other cases, the main agent of government intervention in the Turkish credit markets was the Central Bank, which in turn was subordinated to the Ministry of Finance. Just as private industry had to strategize around the DPT’s investment plans as part of market competition, so did private commercial banks have to vie for Central Bank credits that formed an increasingly large portion of their sources of financing. Thus, as Ayşe Buğra (1994, 199) notes, “the ownership of a group bank [did] not…reduce the financial dependence of Turkish holding companies on the state.” Rather it engendered a new umbilical cord between the bureaucracy and big business.

The Central Bank’s powers went noticeably beyond simple credit allocation, though. It already had the monopoly over all foreign exchange operations. With a 1970 law, the bank was also given a renewed and wider authority to impose commercial bank interest rate ceilings for both deposits and lending. In addition, it was accorded a broadly defined autonomy over its discount rates, and for setting reserve and liquidity ratios. The Central Bank’s use of these instruments coincided with the objectives of state-led industrialization. In keeping with the model of financial repression, interest rates were
typically set below the rate of inflation so as to ensure the flow of cheap credit to industry; reserve and liquidity ratios were often unrealistically high; and the distribution of credit favored import-substituting industrialists and rural producers. As a result, until the mid-1980s, banking remained a low-profitability activity in Turkey.\(^{12}\)

This strict attitude of the Central Bank toward commercial banking was in stark contrast with its softer approach toward the public sector. Its decisions could make or break particular financial and thereby commercial interests, yet it had virtually no operational autonomy vis-à-vis demands from the political authority. In fact, by the 1970s, the bank had turned into the main vehicle for deficit financing (Kepenek and Yentürk 2004, 154ff). In the final analysis, this was a manifestation of the built-in imbalances of Turkish public finance. The political limitations of the ISI did not allow the Turkish state to grow too strong an extractive arm. Industrialists enjoyed tax breaks, farmers were virtually exempt from taxation, and the self-employed could not be effectively taxed. Taxation fed on areas in which the state was a clear intermediary, such as wages and salaries, financial incomes, and customs fees. Despite the structural limitations on tax income, public expenditures kept increasing, but not due to high levels of public investment. Rather, current expenditures steadily rose as a result of an expanded civil service, escalating welfare spending, and in particular below-cost pricing of the state-owned enterprise (SOE) output (Ibid.). In such a context, Central Bank credits and advances to the public sector were used to cushion off growing domestic and foreign

\(^{12}\) During the late 1970s, the reserve ratio for both time and non-time deposits was set at 35 percent (Yüzgün 1982, 79). While inflation exceeded 50 percent in 1978 and 60 percent in 1979, interest rates on one-year savings deposit were fixed at 12 percent and 20 percent, respectively (ibid., 116-117). Given this severe cap on interests, the majority of the bank clientele kept their savings in non-time deposits for everyday access, which comprised over 60 percent of individual accounts throughout the 1970s (ibid., 182-3). In 1980, the return on assets of the top ten banks was around one percent (Henry 1996, 119).
debt. Yet this fiscal expansion came only at the expense of unrestrained monetary expansion, putting the Central Bank in a position of juggling the two utterly undesirable scenarios of high inflation and state bankruptcy. In the end, neither could be prevented.

Nor could it be argued that such governance of the sector brought about effective regulatory oversight of either private or public banks. The extensive powers of the Central Bank were driven by policy and exercised from afar. But the state capacity to actively monitor individual banks was limited. The main agent of everyday public monitoring and supervision of banks was a tiny group of sworn auditors operating under the Ministry of Finance: as late as 1981, there were only 43 sworn auditors responsible for a total of 44 banks with over 6,000 branches nation-wide (Yüzgün 1982, 379). As a result, both public and private banks were left to rely on their own internal control mechanisms. The same held true for the expenditure side of public finance as well. The Turkish Treasury was organized as a general directorate under the Ministry of Finance, lacking formal insulation from ministerial offices whose interests depended on maximizing their share of public funds. Continually caught in the middle of bureaucratic infighting for the allocation of public income, it was not party to any system of checks and balances that could help arbitrate the intra-state competition rationally.

Two points need to be emphasized about the financial regime: its links to societal interests and its self-reinforcing character. First, despite the absence of a strong and independent collective interest in the sector, the regime itself was not insulated from the fine balance of power underlying Turkish industrialization. Rather, it was a direct manifestation of it. In the long run, financial repression created an environment in which only the most powerful could survive, leading to a high degree of concentration in
banking.\textsuperscript{13} By 1982, the top ten banks retained more than 90 percent of all deposits. The ownership structure of these banks was a clear expression of the state-manufacturers’ alliance. Four of the top ten were public banks, five were associated with industrial conglomerates, and one (İş) was itself a holding company (Barkey 1990, 124-5). This concentration was in fact an effective oligopoly given the immense weight of Ziraat, İş, Akbank and Yapı ve Kredi (the “Big Four”) in the system. In 1980 these banks accounted for 64 percent of total deposits and extended 63 percent of credits (Yüzgün 1982, 91; 235). But whereas three of the Big Four, with the obvious exception of Ziraat, were organically connected to industrial groups, the share of industrial firms in bank credits remained quite low, at around 4-5 percent of total credits in much of the 1970s (Kepenek and Yentürk 2004, 160). Instead, given negative real interest rates and low profitability, banks habitually preferred commercial credits which were considered more reliable and had faster turnaround times. Still, there is good reason to believe that a considerable portion of mercantile credits was finding its way into the largest manufacturers’ pockets, given high levels of interpenetration between commercial and industrial capital through complementary group firms, not to mention that import-substituting industrialists were at the same time big importers of intermediate goods, for which they extensively relied on bank credits. If there was any discrimination against industry, it hurt primarily small and medium manufacturers. Seen this way, the continuity of credit activism, thanks also to the growing powers of the Central Bank after 1970, cannot be explained without the political acquiescence of both large manufacturers and the commercial bourgeoisie.

\textsuperscript{13} It must be noted that this was a concentration of national banks. The exit of foreign banks from the Turkish system, which had started during the Great Depression, steadily continued in the postwar decades as well, with the remaining four foreign banks accounting for only about 2-4 percent of deposits in the 1970s (Yüzgün 1982, 92).
Second, equally important as the accommodation of interests was the self-reinforcing nature of the regime. One source of this was political, and followed directly from the above point: because financial repression did not permit the emergence of a powerful independent financier class, and because its main losers were either partly compensated for through public banks or co-opted within quasi-public interest associations, the financial regime automatically pre-empted its opposition. In fact, the banking community itself was co-opted within a compulsory interest association (TBB, the Turkish Banks’ Association), which was strictly controlled by the alliance between public and large conglomerate banks, and framed sectoral preferences accordingly. The second source of self-reinforcement was the product of an unintended feedback effect, and concerned the entanglement of fiscal and financial regimes. Namely, the weight of large, politically motivated, and bureaucratically administered public banks in the system made the governance of commercial banking an increasingly important concern for the bottom line of the state. Moreover, fiscal deterioration of the 1970s coincided with the growing powers of a non-independent Central Bank over the sector, rendering credit activism as an indispensable policy tool. This intense fusion of public finance with commercial banking, along with the oligopolistic market structure in the sector, would have decisive implications for the transition out of financial repression in the 1980s.

3.3 Peasants and Politicians: The Political Economy of Populist Corporatism

On the eve of the neoliberal reform push, Turkish agriculture was characterized by populist-corporatist forms of market governance, the main instrument of which was a
colossal support regime. The support regime was populist in that it embodied “an appeal to ‘the people’ against…the established structure of power and the dominant ideas and values of the society” (Canovan 1999, 3). Support schemes symbolized Turkish politicians’ acknowledgement of the structurally disadvantaged position of rural producers in the face of rapid capitalist industrialization led by urban elites; they were used, most effectively by right-wing parties and neopatrimonial leaders, to solicit mass support in return for ameliorating this systemic disparity via regularized interventions in agricultural markets. This populist promise was carried out within a squarely corporatist framework which linked “organized interests…with the decisional structures of the state” (Schmitter 1974, 86). Rural interests were functionally organized into compulsory, non-competitive, state-funded and -supervised regional/national associations that aided, in varying capacities, government agencies in the execution of support policies.

Since the Great Depression, two interrelated factors had contributed to this outcome. On the populism side, deep-seated state-peasant relations evolved in the way of reinforcing the dependence of the majority of peripheral producers on the political centre while rendering that centre itself highly sensitive to redistributive demands from the periphery. On the corporatism side, these relations were enveloped in a stupendous web of state and parastatal organizations and political arrangements that made intense state intervention a default component of agricultural activity.

Relations with the periphery had long been a thorn in the side of central authority in what is now modern Turkey (Mardin 1973). Against the feudalizing tendencies of provincial notables, both Byzantine and Ottoman rulers strived to preserve an agrarian structure based on free peasantry. Even after Ottoman lands were opened to European
commercial interests in the nineteenth century, this concern with preserving the power of the center precluded the development of large-scale capitalist agriculture (Keyder and Tabak 1991). Instead, bureaucratic modernizers both in the old empire and the new republic intervened at crucial moments of the country’s capitalist development on the side of smallholder peasantry (Keyder 1983; 1993; Arıcanlı,1986).

The historic predominance of petty commodity production would have unique consequences in modern times. From the 1930s on, the shift from liberal to statist policies under the crippling conditions of depression and war forced the centrist bureaucratic elites to seek political alliances first with middle farmers and then with small peasantry (Birtek and Keyder 1975). But the advent of the multi-party regime after the war would reveal the futility of this project (Jacoby 2006). As the significance of rural interests within the Turkish polity magnified, the centrist forces found themselves at a political disadvantage. The first successful opposition movement, the DP, came to power in 1950 by forging a broad rural and entrepreneurial front against the urban-statist bias of the republican elite (Kasaba 1993). This would pave the way for the strengthening of institutional mechanisms that placed a more or less unified agrarian interest at the center of Turkey’s competitive politics. This in fact was one of the main differences between financial and agricultural regimes of governance. Whereas financial repression and credit activism took advantage of and further reinforced private sector cleavages, agricultural support schemes led to a convergence of previously contending agrarian interests. Consequently, it is easier to observe the crucial role collective preferences and everyday politics played in the evolution of the support regime.
Two events during the early period of multi-party politics, concerning land reform and agricultural taxation, acted as important catalysts in bringing together diverse agrarian interests. In the 1930s and the early 1940s, the statist wing of the ruling CHP lobbied for a sweeping land reform, which met with tough resistance from the landed provincial elites within the party. This was an odd proposition because landlessness was not an acute problem in the Turkish countryside. Large holdings were few and far between, and were concentrated typically in the Kurdish regions where there was a history of semi-feudal arrangements on low fertility land. Rather, the proposition reflected a last ditch attempt on the part of the bureaucracy to appeal to peasant masses on the eve of the transition to competitive politics (Keyder 1987, 126). After prolonged debate, the parliament passed a watered down reform act in 1945, which aimed more at allocating property rights on already cultivated state land than expropriating property from large holders (Aktan 1966). But in subsequent years, reform implementation was unexpectedly slow. Ironically, it was the DP leaders, in sharp contrast with their ferocious opposition to any mention of land reform a few years ago, who embraced the new legislation as the centerpiece of the party’s commitment to agricultural development. Land distribution to landless peasants and smallholders from public land accelerated in the 1950s. Extensive land reclamations, riding on rapid mechanization in the context of the Marshall Plan, further improved the fortunes of the peasantry. These developments would seal the final consolidation of small peasant ownership in an increasingly commercialized countryside. In short, the bureaucratic tactic to win the favor of the peasantry via radical land reform was thwarted by landed elites and their commercial

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14 “Between 1948 and 1955 land under-cultivation increased by 50 per cent”, and “[t]he number of owner-occupied farms increased from 2.3m in 1950 to 2.5m in 1952 and to 3.1m in 1963” (Keyder 1983, 142-3).
allies through an overall expansion of the agrarian interest around which all sections of the rural society could unite.

This unified agrarian interest would be put to test in 1961, when the DPT’s idealist planners tried to insert a proposal for agricultural taxation into the first Five-Year Development Plan. But the project generated fierce criticism from the conservative elements within the post-1960 coup coalition, in which the CHP was the larger partner. A political crisis ensued and the proposal was subsequently dropped, triggering a wave of high profile resignations from the DPT, including the head of the organization (Kansu 2004, 110ff). This bureaucratic debacle at the dawn of the planned era would prove such a bitter testimony to the veto power of rural interests that the idea of agricultural taxation would be scrubbed for good for decades to come.

The privileges earned by agrarian interests during their political incorporation had the effect of foreclosing one potential developmental pathway: systemic extraction of surplus from agriculture could never become a viable political option for Turkish industrialization, and along with it foundered the possibility of a strong tax base at early stages of industrial development as well. Instead, industrialization had to work its way around the rural constraint. In that task politicians would rely on an ever-expanding set of populist support schemes that firmly bound together the political and economic logics of governance toward the periphery. One side of this story was simply about numbers. Sheer demographics in an open polity made it unimaginable for political projects to ignore agrarian interests. Despite rapid urbanization, rural population still hovered around 70 per

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15 Back in 1925, the first republican government had abolished the agricultural tithe inherited from the empire, relinquishing the state’s historically much abused extractive grip on the countryside. But in doing so, it had also given up a considerable source of public income. The alternatives to the tithe remained symbolic and were eventually phased out (Önder 1988). In consequence, during its postwar boom, agriculture was exempted from any meaningful taxation.
cent in 1960 and 60 per cent in 1970 (DİE 2003). Due to such a high concentration of voters in the countryside as smallholder peasants, rural populism took the form of what David Waldner (1999) calls *constituency clientelism* at a massive scale, cutting across the standard right-left divide. “All elected governments,” as Ergüder notes (1991, 72), “had to take into account the grievances against a State that in the past had treated the ‘peasant’ heavy-handedly”. With populism rapidly becoming the only game in the village, domestic terms of trade for agriculture dramatically improved in the 1960s and 1970s (Somel 1986, 111ff). On the other side, and as already noted, income transfer to the countryside formed an integral part of a series of social compromises which kept in partial balance the otherwise conflicting interests of industrialists, workers, and the peasantry under Turkey’s import substitution. Steady gains in the income of this largest class segment provided a progressively stable domestic consumer base for the manufacturing bourgeoisie. Furthermore, increased productivity and decent world agricultural prices in the postwar decades ensured that, despite heavy subsidization, agricultural exports continued to supply the bulk of much needed foreign exchange earnings in a relatively closed economy. In this way, the political exigency of rural populism snugly fit the wider developmental equilibrium.

The task of supporting a sector as large and diverse as Turkish agriculture was a complicated one that hinged on a unique institutional framework. The well-oiled support machine to be inherited by Turkey’s neoliberal reformers in the 1980s was the culmination of half a century of institutional development. The origins of the system dated back quite precisely to the procurement of wheat in 1932 as an emergency reaction to the collapse of world prices. Spread of procurement to other cereals and, later, forced
purchases during wartime shortages (Pamuk 1991) consolidated direct state involvement in the livelihood of wide segments of the rural society. In the following decades price supports were expanded from cereals to cash crops and livestock products. At the same time policy was diversified with the introduction of extensive input subsidies and credit opportunities. This exponential growth in policy objectives entailed a complex institutional structure. A massive network of state and parastate organizations followed, displaying a three-tiered structure (Somel 1986; Kasnakoğlu 1986; Kip 1988).

In the first tier were a number of state enterprises and regional corporatist associations engaged in support purchasing. By far the largest of these was the Turkish Grain Board (TMO), specializing in cereals and pulses. In sugar beets, the state-owned Sugar Factories held a monopsony, and so did Tekel in tobacco and Çaykur in tea. There were a couple of large agencies in livestock products and fish: Meat and Fish Organization (EBK) and the Milk Industry (SEK). Finally, numerous regional, state-funded Agricultural Sales Cooperative Unions (TSKs) largely controlled a variety of cash and export crops including cotton (Çukobirlik), hazelnuts (Fiskobirlik), sunflowers (Trakyabirlik), olives and figs (Tariş), pistachios (Güneydoğanbirlik) and so on. These producer cooperatives were the epitome of rural corporatism. Membership was voluntary, but in most crops they offered the only meaningful gateway to the market. More

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16 Support purchasing is the backbone of the market price support system. Its precondition is the existence of import limitations, mostly through high tariffs and to some extent by a quota regime. Close to the harvesting season of a supported crop, the government announces a “base price” for purchasing. With this base price it declares that it is ready to purchase the entire marketable produce at that price, so producers should not hesitate selling to other agents, in this case private traders, if the latter is willing to beat the floor price. The “private market” seldom produces better prices, however, because of an idiosyncratic and for the government a convenient problem in the system: throughout its history state procurement has been prone to frequent delays in state payments. Typically, the government would purchase the crop now, but make the payment several months down the road, sometimes in installments. Even a few months’ delay, especially under the typically high inflation scenario since the 1970s, is intolerable for the peasant, who needs the money right away to pay his debts and get the supplies for next year’s crop. Under these circumstances it was, and it still is, common for smaller farmers having to sell their crop to merchants for 10-20 percent below the government’s base price in order just to have access to cash upfront.
important, cooperatives implemented the annual government price policy in these crops by relying on government credits to finance their operational costs and cover their perennial losses. A similar relationship existed between the agricultural state enterprises and the Central Bank. All of these organizations were also actively involved in the processing as well as the domestic and international marketing of these products. Most agricultural enterprises were brand names and some even had their own retail network. Cooperatives, on the other hand, were mostly specialized in the exportation of cash crops.

A second tier of organizations regulated the allocation of agricultural inputs. The sale and distribution of subsidized physical inputs fell under the responsibility of the state-run Agricultural Supply Organization (TZDK), but were sometimes contracted out to local cooperatives. These included fertilizers, pesticides, seeds and animal feed, produced predominantly by large public sector companies. On the credit front, meanwhile, the heart of the network was the colossal, state-owned Ziraat. The bank supported not only sales cooperatives but individual farmers as well. In this task it was assisted by a network of district-level Agricultural Credit Cooperatives (TKKs) which specifically targeted small farmers. In 1930 there were less than two hundred such cooperatives with about twenty thousand members; by 1970 their numbers exceeded two thousand, joining together over 1.3 million members (Yüzgün 1982, 37). During the same period the share of agricultural credits in agricultural GDP grew from 5 percent to close to 30 percent (ibid., 284-5). As in the case of state enterprises and sales cooperatives, Ziraat frequently suffered “duty losses” as a result of its generous credit policy. The Central Bank would foot the bill through inflationary deficit financing.
Finally, a parallel network of state-controlled or otherwise politically well-connected professional and interest group associations closed the circle of corporatist market governance. Here the most important organization was the Turkish Union of Chambers of Agriculture (TZOB) with branches in every district. TZOB was a quasi-public entity and membership in the local chamber was mandatory. And given its vast member base in the countryside, it was structurally inclined to voice the concerns of small and middle farmers. This forced governments to keep a close eye on the union’s activities, often through direct patronage. Over time, TZOB took on a diverse set of formal and informal functions, ranging from farmers’ education and preparation of annual product reports for support pricing to lobbying for higher prices and even partisan support at election time. Another professional organization was the Chambers of Agricultural Experts (ZMO), which worked in tandem with agricultural chambers and sometimes with local cooperatives in technical matters. About the only independent interest association was the Turkish Federation of Farmers, representing the few large holders. Its main cause was to tenaciously guard the built-in rural bias in the Turkish polity against occasional calls for reform and change.

At the macro-political level, the support regime featured some idiosyncratic arrangements between various state organs. Price policy was the legal prerogative, interestingly, of the Ministry of Commerce, partly because it had nominal control over

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17 The first agricultural chambers were established in the 1880s, their numbers reaching around 100 by the turn of the century. In the following decades of war, revolution and economic crises, however, the idea of unifying mass agrarian interests through a countrywide network of peasant associations fell out of favor. Chambers were neglected by early republican governments, and when the state decided to actively govern market relations in agriculture, that is, by the 1930s, they had mostly atrophied. To invoke Streeck and Thelen’s (2005, 24ff) terminology, they had been victims of a process called “institutional drift.” In the 1940s and the 1950s, paralleling the strains in state-peasant relations at a time of increased political inclusion, there were some hesitant attempts to rejuvenate the chambers. But only in the mid-1960s did chambers fully resume their operations and spread across the countryside as an instrument of centrally-guided interest intermediation.
the sales cooperatives. But actual decision-making for prices lay with the Council of Ministers under consultation with the Ministry of Finance and the DPT (Ergüder 1980, 173). Likewise, the Ministry of Agriculture, although on paper isolated from price policy and reduced very much to a technical agency, wielded some political influence via its interpenetration with farmers’ organizations. And needless to say, both price policy and the annual fate of input schemes were matters of intense political struggle. Every year, just before government prices were announced, representatives from the country would flock to Ankara for lobbying, and the wheels of the clientelistic machine would start turning faster. Unsurprisingly, better prices and increased credit were more likely in election years (Gürkan and Kasnakoğlu 1991).

Consequently, the support regime represented a formula of rural populism entrenched in corporatist market regulation. Most observers of Turkish politics thus view it as an elaborate system of side-payments designed to woo rural votes (e.g. Waterbury 1992). This, however, is a fairly narrow interpretation. For one, a crucial factor behind the attractiveness of rural populism was its long-term consequences for both inter- and intra-sectoral distribution of income. Generous price supports particularly from the mid-1950s onwards led to dramatic improvements in the domestic terms of trade for agriculture (Somel 1986, 111ff). And while the regime unavoidably favored big landowners due to higher levels of marketable output in larger estates (Mann 1980), it also shielded small farmers, with the notable exception perhaps of semi-feudal sharecroppers in the south-east, from the destructive potential of rapid commercialization. As a result, high growth rates in the 1960s and 1970s did not lead to a projected worsening of the intra-sectoral distribution of income (Ulusan 1980). In the face of fast
industrialization, support schemes ensured a defensive redistribution of resources toward the entire sector without aggravating the pre-existing class cleavages in the countryside.

The resilience of corporatist interventionism, meanwhile, stemmed from its ability to resolve fundamental problems of market coordination in agriculture (Somel 1986, 118). In fact, far more than being constitutive of markets in the Polanyian fashion, under agrarian corporatism the Turkish state was the market, the price-maker, the visible hand. By the 1970s, production decisions in all major crops came to depend largely on material incentives emanating from the political center, and a great deal of market exchange had to go through state and parastate organizations even in non-monopoly crops. This in turn had broader feedback effects, as over time the regime had developed strong backward and forward linkages with state-owned as well as private industry. A sharp retreat from this path would not only drive rural market relations into abyss, but require costly adjustments in multiple industrial subsectors (e.g. machinery, fertilizers, textiles).

In short, the distributive consequences of rural populism and the market engendering properties of corporatist intervention created strong, although different, disincentives to alter the support regime. But together, populism and corporatism also produced a set of intense and unanticipated linkages between the center and the periphery that could not be reduced to the everyday functions of either. At the center, the diversity of policy tools and the scope of resources available for allocation gave central politicians new client bases and a constant foothold in the countryside. At the periphery, meanwhile, these very same structures ensured a reciprocal voice within the polity (cf. Alexander 2002). It is important to note that this voice did not come in the form of mass mobilization, but rather mass incorporation, as Waldner (1999) also correctly observes.
Decisive in that process was a significant shift in the country’s elite profile, as reflected in the growing salience of localism in national politics and the rise of the agro-bureaucracy. Deputies representing their birth provinces, for instance, constituted a mere 34 percent of the parliament after the 1935 elections; by 1969 this figure would climb to over 70 percent (Frey 1975, 59-60). Moreover, officials in state enterprises and farmers’ organizations comprised an increasingly influential segment of the administrative elite, which until then had been dominated by urban modernizers. In time, the continuity of populist redistribution through corporatist intervention became vital for these bureaucratic and political elites to retain their clientelistic hold over local constituencies and their power in Ankara. Unforeseen at the time of its creation, the support regime evolved to form the basis of an effective pattern of center-periphery politics that reflected but also sustained the transformation of Turkey’s elite structure. To put it in institutionalist terms, this was the primary source of its locking-in by the 1970s.

The general point is that populist corporatism was far more than an opportunistic tool for ensuring peasants’ allegiance in a broad-based network of social bargains. Its not so visible effects—long-term distributive consequences, market engendering, partial traversing of the center-periphery cleavage, and piggybacking on but also articulating changing elite configurations—gave it remarkable resilience over decades. The advent of neoliberalism would undermine many of these factors that had upheld the support regime under import substitution, and thus challenge its foundations.
3.4 Institutional Trajectories Reconsidered

Taken together, the regimes that governed Turkish finance and agriculture before market opening could be considered functionally complementary. Negative real interest rates were indispensable for credit access in agriculture. Both agricultural state enterprises and sales cooperatives counted on the government’s ability to tap Central Bank resources in a lax system of public finance. At the same time, a foreign exchange-earning agricultural sector was essential for the continuity of import activity, which also ensured a steady demand for commercial bank credits. Deficit financing via monetary expansion, precipitated by populist policies, was good for the banks as well, for it made interest costs that much cheaper. At the center of these interlocking arrangements was Ziraat, with its feet in both regimes. As the top commercial bank in the system and the largest client of the Central Bank, it was the symbol of the banking oligopoly. And supplying over 99% of agricultural credits, its commercial operations were deeply embroiled in the politics of rural populism.

Taken individually, these arrangements were hardly conducive to the development of the sectors they governed. Populist corporatism passively shielded rural producers from the vagaries of commercialization, yet at the price of rendering them structurally dependent on the political center and thus vulnerable to the slightest policy change. And while support instruments (particularly input supports) did facilitate the spread of new technologies, productivity levels in Turkish agriculture continued to lag far behind those in advanced economies. In a similar vein, financial repression hampered any financial deepening that could have taken place in a fast industrializing economy. Over
time, the extent of credit activism became just as big an excuse for sticking with an unsound fiscal regime as the requisites of import substitution. In short, the significance of these regimes should not be sought in their merits for the sectors they oversaw, but in the way they reflected the spirit of Turkey’s inward-oriented industrialization. Financial and agricultural regimes before liberalization were imperfect pieces of an imperfect puzzle, which nonetheless delivered acceptably fast and fairly equitable growth for about a quarter century.

The developmental trajectories of these sectoral institutions display a common and relatively neutral pattern of origination and evolution, the story of which can be told from a standard historical institutionalist angle:

(1) In both regimes, the depression years of the 1930s and the immediate aftermath of the Second World War appear to be formative periods. These two periods could be treated as one long critical juncture, marking the emergence of a state project before the war and the eruption of respondent societal interests after. It is crucially important to note that many of the principles behind the institutional configurations that surfaced during that early period were not native to Turkey. Both bureaucrats and social forces were deeply inspired by international norms and practices: Soviet planning, German industrial banking, the French system of interest articulation, and Italian corporatism. But in the absence of corresponding external policy pressures, they were not bound by any design schematic as today’s institutional reformers are, so they pragmatically picked and chose from among feasible options. Sometimes they simply emulated a design that looked promising because it worked elsewhere under perceptibly similar conditions, as in the case of industrial banking. At other times they attempted to
rejuvenate arrangements that had been introduced a long time ago, but had since drifted and regressed, as in the case of agricultural chambers. Every step of this process of institution building saw open (agriculture) and tacit (finance) negotiations between contending political and economic factions.

(2) In both sectors, the emergence of some skeletal regime of governance was followed by a period of modification which extended well into the 1950s. This was a time when bureaucrats and societal interests had the equivalent of a ‘test drive’ with these institutions. In that process, the newly-established regimes were reshaped to accommodate the constraints posed by collective actors as well as the wider policy and institutional climate. Rural corporatism evolved into a populist project. Populism augmented the need for deficit financing, which thickened the interdependencies between the Central Bank and public banks. Both the public and the private variants of commercial banking were developing, but they were forced to strategize around each other. In short, the clay was still damp, so it took mold easily.

(3) Given this socially and politically accommodative path, the open adoption of import substitution in the early 1960s, which Turkey had been inching toward in much of the previous decade, did not pose a significant challenge for either regime. The built-in responsiveness of financial and agricultural arrangements ensured that they had already been evolving in the direction where the Turkish ISI needed them to be. So, in the 1960s, financial repression was deepened and populist corporatism was perfected. Any changes that were made to these regimes in order to harmonize them with the requisites of the development policy squarely fell within design parameters. Toward the end of the
decade, the rate of change and innovation greatly decelerated, and institutions started to serve and reinforce the emergent market and political status quo in these sectors.

(4) By the mid-1970s, financial repression and populist corporatism had matured. Market consolidation in the banking sector, with holding companies’ control over private banking, was complete. Deficit financing was the order of the day. The support machine was transferring substantial income to the countryside. This clearly was a period of institutional reproduction, which could be analyzed with common notions of path dependency. Credit activism not only reflected, but also deepened private sector cleavages, generating important increasing returns for dominant industrial interests in the process. Likewise, the support regime had the unforeseeable feedback effect of empowering regional and crop-specific lobbies that created additional circles of clientelism. And the agrobureaucracy, with cooperatives and state enterprises included, had grown so large that in time it became a political constituency itself, contributing to the locking-in of rural corporatism. As a result, the institutional regimes in Turkish finance and agriculture grew increasingly resistant to change throughout the 1970s.

This story also teaches a couple of important lessons about institutional development. First, provided there is generous configurational flexibility and openness to societal negotiation, nondomestic designs can be fruitfully translated into domestic spheres. The cases analyzed in this chapter leave little empirical justification for essentialist notions of institutional endogeneity. At the same time, the complexity and scale of modification these externally-inspired designs underwent and the remarkable longevity of their stabilization process suggest that a quick transplantation of alien norms, as neoliberal institutionalists advocate, would make an unfeasible strategy. Second, there
is something to be said for *longue durée* institutional analysis. A long-term focus appears particularly conducive to developing a ‘thick’ vision of institutions, allowing the researcher to gain clearer insight into the historic coevolution of institutional forms, collective preferences, and ideological proclivities. We lose this analytic higher ground in the following chapters as we move on to cases that represent much shorter time periods where these connections and their effects are not always in plain sight; on top, we face the challenge of incorporating nondomestic variables into an exploration of domestic institutional histories.

Financial repression and populist corporatism were indispensable for Turkey’s inward-oriented, state-induced project of capitalist industrialization. When this project was abandoned, the corresponding governance arrangements in finance and agriculture would lose their ideational and political legitimacy. In turn, their fates after market opening would differ both from the common neutral trajectory described in this chapter and from one another. Under liberalization, Turkey’s financial and agricultural regimes would be reshaped along discordant pathways.
CHAPTER FOUR

DISCORDANT PATHWAYS

This chapter investigates the diverse ways in which Turkey’s fiscal-financial and agricultural regimes were reshaped during the early phase of its market reforms. It contends that the primary cause of this diversity was the policy response to the distinct patterns of internationalization of the Turkish economy. Manufacturing export-led integration with the international economy, continued problems of foreign indebtedness, and pressures from international lending agencies convinced Turkey’s early market reformers to break with pre-existing regimes in both public and private finances, opening up a path of innovation. By trial and error, a novel fiscal-financial order was erected. Yet patterns of internationalization offered no discernible incentive for reorganization in Turkish agriculture. In turn, reformers settled on a strategy of accommodation by adapting pre-existing arrangements to new policy objectives. Rural corporatism persisted, although it was set to serve ends that contravened its redistributive functions. Facilitating these institutional choices was the political anomaly of the period, namely, extreme policy insulation from societal as well as intra-state pressures. At that level finance and agriculture were alike. Authoritarian politics and the primacy of executive authority allowed neoliberal rulers to experiment fairly freely with both regimes in accordance with shifts in technocratic policy priorities. Little say did collective interests have in the remaking of the institutions that governed their livelihood.
The analysis begins with an exploration of two fundamental features of reform opening that also relate to the explanatory variables of the research: export orientation as the dominant mode of internationalization, and policy insulation that rested upon obstacles to political competition. The discussion then turns to institutional trajectories in finance and agriculture. The second section examines processes of insulated innovation that characterized the remaking of the financial regime. This included a full range of strategies, from outright innovation to institutional layering and organizational regrouping. The third section focuses on agriculture, in which the evolution of sectoral governance exhibited a pattern of insulated accommodation. At the center of this was the conversion of rural corporatism from a tool for income transfer to one of income repression. In analyzing both regimes, special emphasis is placed on the implications of these institutional pathways for the fortunes of peasants and bankers. The chapter concludes with some extended remarks on this last point.

4.1 The Path to the Market

The early stage of market reforms in Turkey has been exhaustively researched. In this section I briefly introduce this reform push, and then focus on two important attributes of market-oriented policy change, one providing it with economic momentum and the other greatly facilitating its political implementation: export orientation and technocratic insulation.

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1 See, among many others, Hershlag (1988); Celasun and Rodrik (1989); Arıcanlı and Rodrik (1990); Rodrik (1991); Nas and Odekon (1988; 1992); Eralp, Tümay and Yeşilada (1993); Öniş and Riedel (1993); Öniş and Webb (1994); and Boratav, Türel and Yeldan (1995).
Turkey’s reform opening came at a time of full-blown political and economic crisis. The transformation proposed by the January 1980 reform package, the handiwork of Turgut Özal, then the undersecretary to the prime minister, was unprecedented in Turkish economic history in terms of the sweeping manner in which it spurned prevailing policies and institutions. Along with a sizeable currency devaluation and various austerity measures, the program called for reforming the exchange rate regime, abolishing price controls and subsidies, deregulating interest rates, relaxing the trade regime, and promoting exports and foreign investment. Its architects did not hide their commitment to structural reforms down the road either, laying out plans for substantive financial and trade liberalization, comprehensive tax reforms, and privatization. Yet the early implementation of the program was inescapably skewed toward curing the more urgent problems of the economy, that is, foreign exchange shortages and the accompanying output depression. In the early 1980s, reformers emphasized export promotion over import liberalization, price hikes in SOE output over privatization, and simple fiscal austerity over a structural reorganization of the public finance regime.

Another reason for this modest track record relative to the ambitions of reformers was the environment of political uncertainty under direct military tutelage. In September 1980, the Turkish military toppled the center-right minority government to put an end to the prolonged regime crisis, which by then had descended into intense street violence. The coup dissolved the parliament, shut down all political parties, and instituted a country-wide martial law. The generals kept Özal at the helm of the economy, though, largely for lack of a plausible alternative, but also in order not to further alienate Turkey’s international allies. Still, there were limits to how much they were willing to indulge Özal
and his team in a costly process of adjustment that had no clear political ownership. In the wake of a failed episode of interest rate liberalization in 1982, both Özal and his finance minister were sacked, even though the program itself continued.

Özal made a comeback in late 1983 with his newly established center-right Motherland Party (ANAP), winning the popular vote in the first general elections against the handpicked candidates of the generals. By then the crisis was over. Exports were booming, inflation was down to more acceptable levels, growth had resumed, and Turkey had regained its good standing in international credit markets thanks to a generous debt restructuring scheme. Once in power, Özal quickly picked up from where he had left off, deepening the policy focus on structural reforms. In the mid-1980s, export promotion and fiscal adjustment accelerated and reformers’ attention shifted toward import and financial liberalization, infrastructure investment, and state reorganization. In this process, Özal’s technocratic change team fully exploited the country’s unique political juncture to neutralize the traditional, statist bureaucracy while also insulating policy decisions from societal interests.

The Making of a Proto-Competition State

The most dramatic aspect of Turkey’s economic recovery during the 1980s was its impressive manufacturing export performance, effectively ending the era of inward-orientation. From 1979 to 1984, the ratio of exports to GNP more than quadrupled, from a lowly 2.8 percent to 12.1 percent. Meanwhile, the sectoral composition of exports also changed structurally. The share of agriculture in total exports steadily declined from 58
percent to 24 percent during this same period, while the share of industry doubled, from 36 percent to 72 percent. In nominal terms this corresponded to more than a six-fold increase in industrial exports in just five years, from about $800 million to over $5 billion (DIE 2003).

Several factors contributed to this record. Some of these were the result of fortuitous circumstances, such as rapid export expansion to markets in the Middle East, due primarily to the Iran-Iraq war, but also thanks to increased demand from other countries in the region at a time of handsome oil revenues. Another factor was the utilization of excess capacity which lay dormant during the crisis of import substitution. Turkey’s exportable surplus did not come from comparable increases in fixed capital formation in industry. The traditionally import-substituting sectors such as textiles and iron and steel spearheaded the export drive.

But exports increased in all manufactured goods and to all regions, which indicates that a qualitative change was underway. The crucial difference that marked the transition from the export pessimism of the 1970s to the export boom of the 1980s was neoliberal reformers’ structural commitment to export promotion. It must be emphasized, however, that Turkey’s export push in the 1980s bore little resemblance to the export-led growth strategies of East Asian developmental states, illustrated in well-known accounts by Johnson (1982), Amsden (1989) and Wade (1990). The Turkish experience lacked such integral components of the East Asian model as strategic industrial policy, selective micro-planning, price distortions, and tight financial control (Öniş 1992a). Rather than

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2 Exports to the Middle East were particularly attractive, as about half of these consisted of capital-intensive manufactures, including chemicals and machinery (Şenses 1990, 66).

3 Capacity utilization in manufacturing increased from 50 percent in 1980 to 75 percent in 1987 (Şenses 1994, 63).
guide industrial development and discipline the private sector as a means to obtain international competitiveness, Turkey’s reformers de-emphasized planning and sectoral control, and relied instead on across-the-board measures that did not contravene on the whole the overarching objective of liberalizing the economy.

Seen this way, the policy and institutional changes underlying Turkey’s export-orientation did not converge on the developmental state example, but fit the much looser pattern of ‘competition state’—a popular term in the international political economy (IPE) literature during the 1990s—of which the developmental state in its more contemporary incarnations could be considered but one sub-type. Philip Cerny (2000, 136) describes the main focus of the competition state as “the promotion of economic activities, whether at home or abroad, which will make firms and sectors located within the territory of the state competitive in international markets.” As Ronen Palan and Jason Abbott (1996, 4) note, this not only involves a “pervasive belief in national competitiveness as the means for generating economic growth”, but is also based on a shift from “predominantly demand-side measures to supply-side measures” for enhancing competitiveness. ‘Competition state’ is therefore an umbrella term that denotes a state’s commitment to competitive integration into the international economy while simultaneously subscribing to a more liberal capitalism at home.

Three interlocking policy measures characterized the move toward a competition state in Turkey in the early 1980s: exchange rate policy, wage repression, and export incentives. The first two were crude measures that entailed little in the way of institutional innovation. Reforms replaced the fixed exchange rate regime with a policy of “continual real effective depreciation,” whereby nominal rates were actively managed
via daily adjustments (Aşıköglu 1992, 106). By the mid-1980s, the lira was depreciated against the dollar by over 50 percent compared to its pre-reform levels. A parallel decline in wages helped drive down production costs. From 1979 to 1984, real wages in manufacturing shrank by about 30 percent (Boratav 1990, 204-5). This, above all else, was achieved through brute political repression of worker activism, with the military regime outlawing strikes and banning most union activity. Along with the comparable erosion of public salaries and agricultural prices, wage repression pointed at the overall deterioration of popular incomes, which the reformers considered a necessary measure for restraining domestic demand.

The system of export incentives, on the other hand, did require some institutional footwork. The government subsidized the export sector through four mechanisms simultaneously: tax rebates, export credits, foreign exchange allocations, and import permits (Balkır 1993). Between 1980 and 1983, the weighted average subsidy rates on manufactured exports were constantly above 20 percent (Baysan and Blitzer 1990, 14). While some of these incentives were inherited from the export-hungry days of import-substitution, their rejuvenation and effective implementation necessitated changes in the structure of both the economic bureaucracy and corporate design.

On the government side, export-orientation initially empowered the DPT’s Directorate of Incentives and Implementation. More important, in 1983, the General Secretary of Foreign Trade of the Ministry of Commerce was wrenched away from this institution and was integrated with the Turkish Treasury to form a single Undersecretariat of the Treasury and Foreign Trade, now directly answering to the prime minister. As will be examined in the next section, this would represent a fusion of the Turkish public
finance regime with the requisites of the country’s export-based integration into the international economy. For the distribution of export credits, meanwhile, the reformers instituted a number of schemes, including subsidies through an Export Promotion Fund as well as an Interest Differential Fund, both working in tandem with the Central Bank. They also promoted entry into the financial sector by smaller domestic and foreign banks specializing in trade financing and, later in 1987, set up a state-owned export-import bank (Turkish Eximbank).

On the corporate side, the bulk of special export incentives was available only to Foreign Trade Companies (FTCs), a novel corporate entity of the 1980s. In order to qualify as an FTC, companies had to maintain minimum levels of export earnings and paid capital, which discriminated against smaller exporters (Balkır 1993, 152). As a result, most FTCs were affiliated with Turkey’s industrial conglomerates, serving primarily as the export outlets of their parent companies. By the mid-1980s, some 25 FTCs accounted for about half of Turkey’s total export earnings (Öniş 1992b, 77ff). The FTC system did not alter the primary dynamic of Turkey’s state-business relations, however, in that even the largest manufacturers remained dependent on the ever-changeable incentives from the political center (İlkin 1991). In fact, it expanded the scope of that dependence from the attainment of domestic competitiveness to competitiveness at the international level, exposing Turkish firms to wider country risks with which they were neither willing nor accustomed to grapple.
Questions surrounding the democratic feasibility of economic reform, as we saw in the second chapter, have inspired much scholarly debate, with emphases varying from the merits of reform sequencing and the importance of reform coalitions to the usefulness of populist projects. Such considerations, however, had little practical relevance for Turkey’s early neoliberal reformers because they were exempt from a meaningful system of democratic checks and balances. The authoritarian political context ushered in by the 1980 coup freed the policy elites from everyday concerns of political accountability vis-à-vis contending societal interests—concerns which had irreparably damaged stabilization efforts in the previous decade. At the same time, technocratic policymaking, combined with the executive bias within the post-coup regime, allowed the reformers to bypass Turkey’s traditional political society altogether, including not only the statist bureaucracy but the residues of the old political elite as well. Established modes of interest intermediation and channels of policy implementation atrophied, harboring strains that would prove detrimental to policy coherence later in the decade.

One cannot overstate the significance of political authoritarianism for the initial reform push in Turkey. A disorganized and weakened civil society was instrumental for the first generation of liberal elites to absolve economic policymaking from the yoke of the social compromises that had characterized import substitution. The military rulers of the early 1980s were determined to lock politics away in a highly restricted party system and purge the rest of the civic sphere from the pernicious effects of political contestation (Yeşilada 1988; Heper and Evin 1988). This would curtail interest representation from
below. One dimension of this process involved pre-empting any opposition from the middle and upper-middle classes. All professional associations, including organizations of smaller industrialists and tradesmen but also of doctors, lawyers and the like, were brought under strict state supervision. A considerably more important dimension concerned the working class. The coup leaders banned three out of the four major trade union confederations, and severely limited the activities of the remaining centrist confederation (Cizre-Sakallıoğlu 1991). In this way, when the ANAP came to power in 1983, organized urban-popular resistance to accelerating reforms was rendered politically impossible. A similar dynamic of political disempowerment characterized farmers’ organizations too, as I will discuss in the third section.

In terms of state-business relations as well, the early years of market-orientation did not generate an environment as amicable as one would expect. Initially, reform opening appeared to have created conditions Turkey’s industrial conglomerates had been longing for decades. Big business was well-represented in Özal’s 1983 cabinet, with 16 out of 20 ministers formerly affiliated with private groups (Arat 1991, 144). Yet this interpenetration was delusory; rather than amount to tangible policy influence by business interests, it proved an “asset for the government, to contain demands…from big business” (Ibid.). Decision making lay with a technocratic inner cabinet that in the last instance was as insulated from business groups as from any other collective interest. Metin Heper aptly summarizes this situation:

The executive inner circle…did not want to be talked to; they themselves talked to the concerned, and after the event. Those in this circle formulated policy decisions all by themselves and put them into effect. Then the prime minister or a member of the group appeared on the scene to explain the decisions taken, and where necessary, to placate the groups with vested interests, either through special meetings or by attending the scheduled meetings of the relevant interest group associations. And not all such encounters aimed at providing explanations; more often such get-togethers were occasions for the government
elites to communicate their *directives*, if not their *threats*, to the members of the private sector, e.g., ‘sell your villas and augment your capital’, ‘pay your taxes or else’, and the like (Heper 1990a, 330-31, emphasis original).

In this way, the onset of market transition put Turkish big business in an awkward position. On the one hand, business leaders felt obliged to embrace reforms, seeing the Özal government as the country’s sole ticket to a more market-friendly capitalism. On the other hand, they were cut off from everyday policymaking more than ever, facing an environment of unbearable policy unpredictability comparable only to the statist industrialization episode of the 1930s (Buğra 1991).

Policy insulation did not stop at societal interests. Özal and his young “princes” in the inner cabinet also managed to override the traditional statist bureaucracy and conventional politicians. To this end, they resorted to three interconnected measures. The first of these was the reorganization of the economic bureaucracy. This included both the creation of new technocratic agencies, as in the case of the Treasury, and the reshuffling of responsibilities between existing ones. This process invariably worked against the strongholds of the old guard by crafting a new segment of liberal-minded bureaucratic elite (Heper 1989; 1990b). The second was the proliferation of extra-budgetary funds (EBFs), such as the Mass Housing and Public Participation Fund, to meet specific reform-related needs. As “convenient ways to avoid the scrutiny of the budget process” (Öniş and Webb 1994, 152), the EBFs originally helped augment the discretionary powers of the technocratic executive vis-à-vis the old school politicians in the legislature. Finally, in the same way as the Latin American *decretismo*, executive decrees rather than parliamentary legislation emerged as the preferred instrument of policy reorientation, precluding any public debate prior to policy implementation. By reorganizing the economic bureaucracy, creating a parallel public budget, and ruling by decree, Turkish
reformers not only undermined the position of conventional bureaucratic and political elites, but also severed the deep-seated political decision-making/bureaucratic policy implementation nexus between these two groups, replacing it with patterns of rule that possessed little in the way of either intra- or extra-state accountability.

At the same time, Turkey’s change team was all too open to policy influence from abroad. The central component of this, needless to say, was relations with the international financial institutions (IFIs). The country was a favorite of the IMF and the World Bank throughout the 1980s, receiving five consecutive structural adjustment loans as well as four sectoral adjustment loans from the bank, while signing three IMF stand-by agreements on the side (ibid., 153-4; Kirkpatrick and Öniş 1991). It must be noted, however, that in its early stages the close working relationship between the IFIs and Turkey’s technocratic reformers was often an opportunity for the latter to implement the kind of policies they themselves advocated rather than an unwelcome constraint upon policymaking. Özal had worked at the World Bank in the 1970s, and members of his technocratic team were brought up on the neoliberal ‘counterrevolution’ in American universities. The ‘innovative’ policy elite already consisted of dedicated neoliberalists who closely followed the direction of global policy wisdom and were committed to turning the country around accordingly. In that sense internationalization in Turkey was just as strong in terms of openness to global policy and institutional norms as in market integration led by manufacturing exports.

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4 Turkey’s conditionality implementation rate of 95% by the end of the loan period was the highest among all structural adjusters (Mosley et al. 1991). As will be discussed later in this chapter, the IMF-WB cross-conditionality had significant implications for the divergence of institutional pathways in finance and agriculture.
4.2 Finance: Insulated Innovation

In chapter 3 it was argued that Turkey’s fiscal and financial regimes in the postwar decades were set to serve the economic as well as the political requisites of the country’s state-induced strategy of import-substituting industrialization. The Turkish state heavily intervened in the credit markets by imposing interest rate ceilings both on deposit and lending rates and engaging in preferential credit schemes toward selected sectors. The financial system was bank-based and capital markets were underdeveloped. At the same time, negative real interest rates, high reserve and liquidity ratios, and heavy taxation of financial incomes rendered banking a comparatively unprofitable activity. The Turkish banking system was domestically oriented, in that foreign banks were discouraged from entering the Turkish market while foreign operations of domestic banks were restricted. Public and private commercial banks had about equal share in the system, and by the 1970s all major private banks had come to be affiliated with large industrial groups. At another level, monetary policy was an appendage of fiscal policy. The Central Bank, despite its powers over the sector, was subordinated to the Ministry of Finance, which in turn was largely influenced by populist demands from spending ministries. The bank and the ministry also doubled as regulatory and supervisory agencies for the banking system, and while they had limited organizational means to perform these functions effectively, there was also little that could go wrong under such severe restrictions.

This picture was to change considerably in the 1980s. Financial liberalization, if understood narrowly as “the process of reducing government control over the allocation
of credit” (Haggard and Maxfield 1993, 314), was slow in that, with the exception of a failed attempt at shock therapy at the very outset of reform opening, interventions in interest rates continued in much of the decade along with some elements of credit activism. The composition of the financial sector also remained more or less the same, given the persistent oligopoly of a few public and private commercial banks in the system. Yet in time Turkish reformers proved committed to a strategy of “making haste gradually” (Caprio 1994, 61) by substantially transforming the institutional infrastructure of both public finance and the banking system. A series of legal and organizational reforms altered the rules of the game and redefined the financial playing field for both bankers and the bureaucrats. But this new order of things also exposed these actors to new collective dilemmas that would culminate in the turmoil of the 1990s.

The general point in this section is that the reformist drive to construct a new fiscal and financial order could be traced primarily to Turkey’s wider patterns of market and policy internationalization. Perceived requisites of export-led growth, strong IFI conditionality, and a concern for the sustainability of the debt burden convinced Turkish reformers of the need for comprehensive institutional reforms in both the financial sector and public finance along norms that reflected accepted practices elsewhere. My objective here is not to obscure the domestic forces involved in patterns of institutional dynamism explored below, for these forces did indeed play into this process in important ways. They were not, however, the cause of change, nor did they determine its overall direction. I present the evidence for this line of argument in two stages, looking first at the financial sector and then the fiscal regime. In a third subsection I examine the consequences of fisco-financial transformation for the various actors involved.
That markets cannot operate smoothly without attendant non-market institutions is a most elemental wisdom for scholars as well as practitioners today. Turkey’s financial reformers learned this lesson the hard way. At first, they were naïve enough to assume that once the fundamental instrument of financial repression was out of the equation, that is, once interest rate ceilings were abolished, free markets would take root to mobilize domestic savings and, subsequently, investment, regardless of the institutional structure in place or the specific circumstances of the real sector. Thus, in a bold move in July 1980, they deregulated commercial interest rates on both loans and deposits. They further allowed banks to issue certificates of deposit (CDs), which could be freely traded in secondary markets. These measures induced two important responses from market players. First, interest rate deregulation led to a bidding war for higher interest rates on deposits between the smaller banks. Attempts at interbank collusion to keep interest rates at reasonable levels failed repetitively, and within a few months after the removal of controls, most banks, including two from the Big Four, joined the frantic competition for collecting deposits. Second, the drive for higher interest rates augmented the salience of a relatively new actor in the financial system, that is, the brokerage houses—the equivalent roughly of the Chilean financieras (Hastings 1993, 213). Brokerage houses had first emerged as agencies for marketing corporate bonds which many firms saw as a lifeline when the domestic market came to a halt in 1979. After interest rate deregulation, however, they started wheeling and dealing primarily in CDs issued by banks, selling certificates to the public and in turn lending heavily at very high rates to high-risk firms.
The scheme soon started experiencing liquidity problems as most banks, instructed by the government, stopped issuing CDs by late 1981 and claims on brokerage houses as well as non-performing loans in the system mounted. Repeated attempts on the part of monetary authorities and larger banks to circumvent the problem failed, and by mid-1982 Turkey faced a system-wide banking crisis. Much to the dismay of neoliberal reformers, the government had to step in, revoking the licenses of five smaller private banks and transferring their liabilities to public banks, rescuing much of the rest through capital injections from Central Bank funds, and subsequently reinstating interest rate controls. The cost of the rescue operation was in the order of 2.5 percent of the GNP (Artun 1983; 1985; Atiyas 1990).

Popularly known as the “bankers’ crisis”, this failed episode of interest rate deregulation would have both immediate and longer term consequences. Shortly after the crisis, the military-led government removed Özal from office along with his finance minister, Kaya Erdem, and reintroduced interest ceilings. But more important, the crisis brought into sharp relief the structural weakness of Turkish financial markets, including lack of prudence in corporate financing. Neither the oligopolistic structure of the sector nor the organic connections between industrial and banking capital could assure efficient allocation of resources in unregulated credit markets. Thereafter the reformers’ emphasis shifted markedly from simple policy measures to complex institutional restructuring.

A significant step in that direction was the establishment of the Capital Markets Board (SPK) to oversee the development of securities markets. The legal infrastructure for the board was introduced in 1981. By that time it had become increasingly obvious that, with the exception of exporters qualified for subsidized credit, higher interest rates
on the one hand, and the demise of preferential credit in non-exporting sectors, on the other, were making bank loans much less accessible to most firms. Furthermore bond issuing via brokerage houses was never considered a dependable channel for raising funds, as the impending crisis would show so painfully for scores of firms. But despite the eagerness of reformers, the construction of a modern securities market proceeded slowly. The Board would become operational only in 1983 and hence after the crisis, while the reopening of the Istanbul Stock Exchange (ISE) would have to wait until 1986.

There are two issues of considerable importance about this move to create an orderly capital market. Organizationally, the SPK was the first example of a new genus of autonomous and semi-autonomous regulatory bodies with discretionary powers, which in time would come to represent an additional and more elite tier of the economic bureaucracy. Setting the precedent for its likes, the board was tied not to the Ministry of Finance but to a special ‘state ministry’, another peculiarity of the Özal era, and was considered a cut above the traditional bureaucracy in terms of organizational efficiency and the quality of the staff, who were remunerated accordingly. Functionally, on the other hand, the regulation of the securities market did not challenge the predominance of commercial banks in the financial system; to the contrary it further empowered them. As Atiyas and Ersel (1994, 106) note, under the new regime banks were not only free to engage in any activities in the primary and secondary markets, but they were granted a monopoly position in some instruments, such as establishing and managing mutual funds. Over time all major banks would set up their own investment branches at the expense of non-bank financial intermediaries.\(^5\)

\(^5\) Thus, the new regime envisioned a “decompartmentalized” (Cerny 1993, 56ff) sectoral structure from the very beginning, in which commercial banking and securities markets were interwoven.
A series of reforms fundamentally transformed the institutional framework of the banking sector as well. One dimension of this was to reverse the hitherto autarkic character of commercial banking by abolishing the Central Bank’s monopoly over foreign exchange transactions while also encouraging foreign entry into the system. Both measures emerged as alternative means to meet the new financing needs of the private sector at a time of outward-orientation. Foreign exchange liberalization in 1984 allowed residents to hold foreign currency accounts and commercial banks to engage in foreign exchange transactions (Akyüz 1990, 102-3). Effectively putting an end to exporters’ direct dependence on the Central Bank, the development of a foreign exchange market also expanded the scope of commercial bank operations in the system and encouraged Turkish banks to seek credit from external markets for the first time.

Another step in breaking the financial autarky was in the realm of foreign entry. In the absence of any notable political opposition, opening the Turkish market to foreign players appeared only a matter of technicality, accomplished with a decree. From a mere four foreign banks operating in the Turkish market by 1981, the number would quickly rise to 21 in 1989, most of which entering the system after the 1982 crisis. The major incentive for this foreign interest in the Turkish financial scene was not the domestic market itself but lucrative opportunities for trade financing at a time of intense export promotion. As Tuncay Artun, later the chairman of the Istanbul Stock Exchange, argued

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6 Pehlivan and Kirkpatrick (1992, 189). The four foreign banks operating in Turkey before 1981 were the Ottoman Bank (France-1863), Banco di Roma (Italy-1911), Holantse Bank (Netherlands-1921) and the Arab-Turkish Bank (Libya-1977). After the reforms they were first joined by Citibank (USA-1981) and American Express Bank (USA-1981), and then Bank Mellat (Iran-1982), Bank of Credit and Commerce International (Luxembourg-1982), Turkish Bank (Cyprus-1982), Habib Bank (Pakistan-1983), Chase Manhattan (USA-1984), First National Bank of Boston (USA-1984), Manufacturers Hanover Trust (USA-1984), Turkish Mitsui Bank (USA-Japan-Turkey-1985), Saudi American Bank (Saudi Arabia-USA-1985), Banque Indosuez (France-1985), BNP-Ak-Dresdner (France-Turkey-1986), Bank of Bahrain and Kuwait (Bahrain-Kuwait-1986), Standard Chartered Bank (UK-1986), Credit Lyonnais (France-1987), and Cyprus Credit Bank (Cyprus-1988) (ibid., 198).
in an early study, “[s]ince the issue is to increase exports without restraining, and in fact liberalizing, imports, increasing the number of financial organizations that would finance imports and exports…becomes the reason for the development of foreign banking at the macro level” (1985, 41-2, translation mine). What gives further credence to this viewpoint is the fact that foreign banks were restricted to a maximum number of five branches across the country. They were therefore not intended to compete with domestic retail banks in traditional banking activities, but expected to offer expertise and resources to a select few firms engaged in volume trading with Middle Eastern and European markets.

A more important dimension of institutional transformation was in the gamut of rules governing the domestic operations of commercial banks. Here, reforms proceeded on the two main fronts of ensuring post-crisis stability in the system and providing better regulation and supervision to avoid further problems. In 1983, a Savings Deposit Insurance Fund (TMSF) was established, extending coverage to all Turkish lira (TL) deposits up to 50 million. During the same year, as an additional measure to counter the liquidity problems faced by most banks during the crisis, all taxes on financial transactions, including those on deposits and loans, were reduced.7 These steps were initially considered instrumental for getting the sector up on its feet again, yet they conformed to the longer-term goals of financial reformers as well.

The centerpiece of the new order was the Banking Law no. 3182 of 1985, introduced at the height of policy insulation (Resmi Gazete, 2 May 1985). The law not

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7 According to Artun (1985, 70-71), taxes on interest income of real persons were reduced from 20-30 percent to a flat 10 percent, whereas ‘expenditure taxes’ collected from commissions and interest income from loans were reduced from 15 to 3 percent. The author calculates that these tax breaks cost the central government a total of TL250 billion (or about US$1 billion) in lost tax income in 1984 alone.
only replaced, refined, and unified under a single legal roof several executive decrees that had effected the preceding changes in the system outlined so far, but put in force a new set of guidelines for commercial banking.\textsuperscript{8} Four areas of novelty are worth noting. First, article 56 of the law mandated the Treasury to set capital adequacy requirements (under the term “standard ratio”) for banks, following strong international trends toward this norm. Second, article 51 obliged banks to follow a uniform chart of accounts to be designed by the Turkish Banks’ Association and approved by the Treasury. The aim here was to assure harmonization in balance sheets and bookkeeping in accordance with international standards. Third, articles 38 through 50 reorganized the legal framework of commercial credits and limits of loan exposure.\textsuperscript{9} Fourth, articles 57 through 65 defined the instruments and the scope of oversight and auditing. In essence the law reemphasized the central function of sworn bank auditors, now operating under the Treasury, to undertake routine on-site examinations. It also specified the various mechanisms to keep problem banks in line. In a later step, the Bank Supervision Unit of the Central Bank, established a year after the enactment of the new law, would be mandated with carrying out off-site supervision of banks on the basis of quarterly and monthly reports and with a focus on capital adequacy, profitability and liquidity (Atiyas and Ersel 1994, 107-8).\textsuperscript{10}

Finally, under the new order the sectoral functions of the Central Bank were reoriented from the allocation of credit and foreign exchange to facilitating and regulating

\textsuperscript{8} The most important of these was the executive decree no. 70 of July 1983, upon which large sections of the new law were based.

\textsuperscript{9} The amount of loans extended to a single real or legal person could not exceed 10 percent of a bank’s capital. Banks were not allowed to loan more than 15 percent in total of their capital to their affiliates of which they had more than 15 percent ownership, whereas loans extended to persons who owned more than 5 percent of a bank could not exceed a respective 5 percent of a bank’s capital.

\textsuperscript{10} Later, with the executive decree no. 512 in 1993 (article 27), banks were obliged to undergo an annual external auditing by an independent auditing firm to complement the dual Treasury-Central Bank process of control and supervision.
financial markets. To offset any liquidity problems that could arise from the abandonment of credit rationing, the bank set up an interbank money market in 1986. In the same vein, it commenced open market operations in 1987. This would be followed in 1988 with the establishment of a foreign exchange market. The bank continued to intervene in interest rates, however. After the 1982 crash, and throughout the first Özal government of 1983-1987, interest rates were set from the centre. An attempt to abolish interest rate controls in mid-1987 destabilized the system yet once again: the initial reluctance of big banks to increase the rates triggered a bidding war for collecting deposits among smaller banks that offered unsustainably higher rates to beat their more manageable competitors, forcing the Central Bank to reinstate controls.

Setting aside the consequences of these changes for now, let us account for their nature and causes. In terms of the four main ideal-types of sectoral institutional change outlined earlier in this study, the reshaping of Turkey’s financial regime of governance during the initial phase of market reforms tightly fits the pattern of insulated innovation. How and why the building of this novel financial regime was insulated from societal interests should be all too clear by now. In a context marked by technocratic exclusivism, one could search in vain for a decisive influence on the part of domestic market players. While it is true that the way commercial banks and at times private investors responded to the new measures did constrain reformers’ choices, these affected mainly the timing and sequencing of various components of reform rather than the nature and the overall direction of change. It could be argued, for instance, that the 1982 crisis, caused exclusively by the short-term profit frenzy of domestic actors, expedited the introduction of a deposit insurance scheme while obliging reformers to de-emphasize temporarily the
development of capital markets. Yet these constraints did not compel technocratic reformers to negotiate the terms of financial restructuring with sectoral interests.

In fact, not only did the policy elite strive to retain its insulation from these interests, but it actively manipulated them when necessary. This involved two simultaneous processes. On the one hand, extreme policy insulation unavoidably weakened the political influence of the banking community. As reported in a rare study on the ‘micro-politics’ of banking in the 1980s, reform opening saw “the atrophy of traditional associational and bureaucratic channels as well as the truncation of political channels of influence through party networks” (Öncü and Gökçe 1991, 100). Crucial in that context was the marginalization of the statist bureaucracy and old school politicians, which directly undermined elite interests’ pre-existing modes of access to policy:

[T]he old guard of the Turkish banking oligopoly (public and private) has not only been deprived of a voice in the immediate policy formulation and implementation process, but also found it impossible to mobilize group action to challenge the increasing autonomy of the Prime Minister’s inner circle. The Association of Turkish Banks, body with compulsory membership, having both state-owned and private banks under its umbrella, has proved ‘meaningless’ as an organizational vehicle (ibid., 109).

On the other hand, technocrats made strong inroads into the sector. Any cooperation needed from the banking community during the early reform stage was secured by appointing ‘princes’ from the inner circle to top executive positions in large public banks such as Ziraat, Emlak Kredi, and Halk, and, perhaps to a lesser extent, by maintaining the tacit approval of the largest industrial conglomerates simultaneously acting as big players in the banking system, such as Sabancı (Akbank) and Çukurova (Yapı ve Kredi).

Bringing this lack of input from domestic players into sharper focus is the fact that the main parameters of financial sector reform took shape around 1980-1983. That is, the game was already afoot by the time ANAP came to power. Özal as Prime Minister
after the 1983 elections and members of his inner circle as captains of the economic bureaucracy during the party’s first term in office should thus be credited more for implementing and overseeing the new financial order than its immediate design. In short, the contours of the new regime predated the consolidation of the political power of an elected reformist cadre.

The content of change, meanwhile, was clearly more revolutionary than evolutionary—a pattern to be partly repeated in public finance as well. From whole new constructs such as the SPK and the TMSF to new rules as in capital adequacy ratios and more restrictive credit limits, and to new players in the system such as mushrooming investment and foreign banks, novelty and rupture visibly outweiged continuity and business as usual. Here, three basic modalities of innovation can be discerned. The first and the most readily observable was the creation of a new stand-alone organization, that is, the SPK. The second was institutional layering, a process whereby “new elements attached to existing institutions gradually change their status and structure” (Streeck and Thelen 2005, 31). This was the mechanism that characterized the birth of both the TMSF and the interbank money market under the auspices of the Central Bank. The third modality is rule-based institutional reorganization. The primary examples of this were the erection of new credit limits, the partial opening of the capital account, and the reorientation of existing tools of bureaucratic control and supervision. This type of change allowed for the survival of old codifications and modes of operation, but the way these were redeployed under the new regime nonetheless made a qualitative difference in the rules of the game. All three modes of innovation had a transformative impact on the institutional framework of private financial activity in Turkey in the 1980s.
How are we to account for this innovative path? The restructuring of the financial regime is a clear illustration of how strong external incentives for sectoral reorganization can provoke substantive institutional innovation guided by exogenous norms. At the level of market integration, the primary incentive for sectoral reorganization was the specific financing needs of a fast-internationalizing industry under the banner of outward-oriented, export-led growth. The opening up of the banking system to foreign entry in 1981, and the partial relaxation of capital controls along with the abrogation of Central Bank monopoly over foreign currency operations in 1984, were important complementary steps in the reformist commitment to export-based integration with international markets. This strategic repositioning of Turkish industry also rendered the continuation of credit activism in non-exporting sectors less acceptable.

Meanwhile, at the level of policy internationalization, IMF and World Bank conditionality was crucial. The extent of policy leverage these organizations possessed during Turkey’s reform opening cannot be overemphasized. The source of that influence, quite clearly, was their active involvement in the country’s recovery from its balance of payments crisis by spearheading a generous debt restructuring scheme and providing sizeable financial assistance. Various components of financial restructuring first appeared in IMF letters of intent and World Bank loan agreements. Interest rate deregulation in July 1980, for instance, was preceded by a call for a dramatic increase in real rates of interest in both the first Structural Adjustment Loan (SAL) agreement with the Bank in March 1980 ($200 million) and the IMF stand-by agreement in June 1980 (SDR 1.25 billion) (Kirkpatrick and Öniş 1991, 14ff). Likewise, the establishment of the SPK was signaled in the “Statement of Development Policies” preceding the SAL II of May 1981.
($300 million).\textsuperscript{11} SAL IV of May 1983 ($300 million) emphasized reductions in reserve ratios and in taxes on financial transactions, which were fully implemented by the government in two steps by 1984. The most comprehensive set of conditionalities regarding the financial sector was introduced in SAL V of June 1984 ($376 million), involving some regulatory and supervisory measures targeting the banking system.\textsuperscript{12}

This IFI emphasis on finance continued in the second half of the decade with two financial sector adjustment loans, amounting to $400 million each. The first of these, approved in June 1986, also included a “technical assistance component” aimed at supporting “a comprehensive training effort to upgrade skills in the institutions involved in the implementation of financial sector reforms, namely the Treasury, the Central Bank, the Board of Sworn Bank Examiners, the Capital Market Board, the Board of Sworn Financial Advisors, and the commercial banks.”\textsuperscript{13} The second, dated June 1988, was similar in nature, to be implemented by the SPK, the Central Bank, and the Treasury. These sectoral adjustment loans were by and large extensions of the pre-existing consensus between the reformist government and the World Bank on the new institutional order in finance rather than building on a new set of conditionalities. For by then not only was domestic financial restructuring practically complete, but the influence

\textsuperscript{11} This policy document, dated 21 February 1981 and signed by Özal himself as the Deputy Prime Minister, promised to “set up an independent commission with the authority to supervise and control the capital market” (World Bank 1985, 61).

\textsuperscript{12} Some of these measures involved “elimination of tax on inter-bank transactions, …preparation of a review of standardised accounting system for banks, …enactment of law on external auditors, [and] …study of fiscal incentives to induce banks to reduce operating costs” (Kirkpatrick and Öniş 1991, 25). As the authors note, many of these measures were already on the table before SAL V. This generous reference to financial reform also served to consolidate the spirit of the Executive Decree No. 70, which had been introduced in July 1983 during Özal’s absence from office following the bankers’ crisis. In this way, the bank assured a measure of policy continuity and reform commitment in finance, blocking the path of potential policy reversals under an elected government and thus indirectly clearing the way for the Banking Law of 1985.

of these external agencies on everyday policymaking was also considerably diminished. So the aim was to reinforce institutional capacity within the new regime.

Both the reformist impetus toward financial liberalization for the sake of export promotion and the content of policy pressure from the IFIs were firmly rooted in the internationally accepted sectoral norms of the day. The innovative momentum was not inspired by circumstances exclusive to the Turkish scene, but took as its ideational anchor the global paradigm shift away from Keynesian financial interventionism. Reformers’ persistent attempts at interest rate deregulation despite clear signs of unreadiness from domestic market players, their belief in the need for strengthening the regime itself by revising old rules concerning credit exposure and public oversight while also introducing new ones such as accounting standards and capital requirements, were a reflection not of domestically-generated ideas or even tangible domestic constraints, but of an emergent neoliberal “interpretive framework” (Hall 1993) in finance among scholars as well as practitioners worldwide. Such openness to external ideas was not limited to the realm of rules and policy instruments either; in their quest for organizational alternatives as well, Turkey’s financial reformers looked outside. At that level, innovation took the form of imitation (Jacoby 2001). The new organizational framework of financial governance unmistakably converged on the US model: the SPK was patterned on the US Securities and Exchange Commission; likewise, the TMSF was the rough equivalent of the US

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14 The theoretical case for financial liberalization is often traced to the McKinnon-Shaw hypothesis of the early 1970s, which suggests that financial repression leads to lower rates of savings and thus investment and growth. See Haggard and Lee (1993, 5ff); Fanelli and Medhora (1998, 8ff); Bascom (1994, 11ff) and particularly Gibson and Tsakalotos (1994). See also Diaz-Alejandro (1985) for a critical account of early Latin American experience. In practice, however, financial deregulation invariably came in the form of “reregulation”, with “new authoritative market-constraining measures to prevent both old and new kinds of market failure” (Cerny 1994, 241; see also Cerny 1993). The clearest indicator of this condition was the early mushrooming of autonomous or semi-autonomous financial regulatory bodies across the developing world, such as the Supervisory Board of Financial Institutions in Argentina (1992) or the Board for Financial Supervision in India (1994).
Federal Deposit Insurance Corporation.\textsuperscript{15} Besides, this broad, rich vision of change, which spawned a wide range of components from general principles and more specific rules to concrete organizational models, allowed reformers considerable flexibility in the sequencing of institutional restructuring. The reform list was so long and comprehensive that when one element failed, as in the troubled path of interest rate deregulation, technocrats were able to quickly move on to alternative items rather than halt the process.

The special financing needs of export-orientation and intense exposure to policy pressures from the IFIs created powerful incentives for reorganization in finance, rendering the pre-existing sectoral regime unsuitable in the new era while simultaneously augmenting the relevance of international norms for subsequent configurations. Here, it must be underlined that neither channels of nondomestic influence followed from the internationalization of the sector itself. Heightened policy exposure to the IFIs was not the result of banking sector troubles, but followed from the overall exhaustion of Turkey’s postwar industrialization strategy, which manifested itself in the form of a deep balance of payments crisis. Likewise, market incentives that created a demand for a novel financial regime stemmed not from financial internationalization, but from the integration of manufacturing industry. The upshot is that, an analytic focus exclusively on sector-specific patterns of internationalization would have little value for our purposes, for it would categorically fail to identify the real range of nondomestic influences behind institutional innovation. A big picture approach is mandatory.

\textsuperscript{15} The creation of a semi-autonomous Undersecretariat of Treasury with powers vastly superior to those of the Ministry of Finance, as will be analyzed below, was also inspired by the example of the US Treasury.
Restructuring State Finances

Changes in the institutional structure of state finances during the early stage of reforms were no less dramatic than those in financial sector governance. Moreover, it will be shown in this subsection and especially the next that realignment in these two realms was not only synchronous; in time it gained a symbiotic character. As in financial reform, the main thrust of change in fiscal management was also conditioned by factors that went beyond domestic political considerations. But while reforms targeted the entire regime of public finance, the scale of transformation and patterns of innovation varied greatly across the different areas of that regime. Here I start with areas of Turkish public finance which were institutionally less affected by the reformist drive and build my way up to those that were most radically altered.

The main challenge for fiscal policymaking throughout the first half of the 1980s was to cut government spending and increase public revenue while simultaneously having to mobilize savings and assist output recovery. The often incompatible requisites of attending to a balance of payments crisis manifested in grave problems of sovereign debt on the one hand, and of stimulating economic growth via a reorientation of development policy, on the other, forced reformers to adopt a complex strategy of fiscal adjustment. In the short run, real cuts in public wages, SOE price hikes, and an overall expenditure restraint proved effective for fiscal stabilization. Yet these temporary measures were quickly offset by revenue losses due to a general tax break effort, designed to stimulate growth. Tax incentives toward exporters and reduction of taxation on financial transactions were mentioned before. Apart from these, personal income tax
levels as well as corporate taxes were reduced considerably. The repression of wages and salaries also ate into public revenue from direct taxes.

In the face of such constraints on direct taxation, reformers sought to shift the burden of revenue collection toward indirect taxes and non-tax revenues. Thus, whereas changes in the income tax regime were mostly quantitative, there was genuine transformation in other areas of resource mobilization. Two institutional novelties characterized that drive after 1983. First, a value added tax (KDV) scheme was introduced in 1985. The rate was set at 10 percent on most items, 3 percent on food, and 15 percent on luxury goods, to increase gradually by the early 1990s to 12, 8 and 20 percent, respectively. The second was the introduction of various extra-budgetary funds (EBFs), as briefly introduced earlier, which evolved in time into a parallel public budget circumventing the routine channels of public resource mobilization and allocation. The sources of revenue for these funds were various, and so were their uses. The largest EBFs were the ones mandated with mass housing, defense industry, infrastructure investment, and poor relief.

Yet the cornerstone of innovation in the regime of public finance was the transfiguration of the Turkish Treasury, which, after the example of the US Treasury Department, was now given vast responsibilities across multiple policy domains. As such, the most radical realignment came not in income and expenditure patterns in the short run, but in the organizational framework of public cash flow and particularly fiscal

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16 From 1981 to 1986, the basic income tax rate was dropped from 40 to 25 percent, whereas corporate tax rates were reduced from 50 to 40 percent (Karataş 1995, 160).
17 Celasun and Rodrik (1989, 733) list five main financial sources for EBFs: “(a) various earmarked taxes and surcharges on foreign trade, bank credits and other transactions, (b) income-sharing certificates of public utilities and enterprises, (c) interest income on the funds’ financial assets, (d) foreign credits, and (e) donations and transfers from other funds.”
debt management. On December 13th, 1983, the very day the ANAP cabinet assumed office, the General Directorate of Treasury was separated from the Ministry of Finance with an executive decree. It was merged with two other units, the General Secretariat of International Economic Cooperation of the same ministry, and the General Secretariat of Foreign Trade of the Ministry of Commerce, to form a single Undersecretariat of Treasury and Foreign Trade (HDTM), formally attached to the Office of the Prime Minister. The new undersecretariat “attained the powers of a ministry, but remained a non-cabinet post headed by an appointed technocrat” (Öncü and Gökçe 1991, 103).

This move represented several interrelated developments at once. First, it entailed a bifurcation of the Turkish state’s extractive and allocative arms. In effect this meant a demotion for the Ministry of Finance, a predominantly political post under continuous pressure from spending ministries. “Without control over the Treasury”, write Öncü and Gökçe (ibid.), “the Ministry of Finance became, more or less, a general directorate of customs and taxation, akin to a department of internal revenue.” Second, the new framework proved the reformers’ dedication to restructure the economic bureaucracy along technocratic lines. The undersecretariat belonged to the same elite, Jacobin tier of the bureaucracy as the SPK, but it was much more central to economic governance and was incomparably larger.

Third, the fusion of government coffers with the agency responsible for the promotion of foreign trade significantly reinforced the switch to an outward-oriented

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18 In a somewhat similar fashion, Law No. 3098 (06 December 1984) freed the Central Bank from the Ministry of Finance and tied it to the Office of the Prime Minister. This was not as significant a move as the emancipation of the Treasury since the Central Bank already had considerable organizational (if not policy) independence from the ministry. A much more important point was that both the Treasury and the Central Bank (although they were formally attached to the prime minister) would eventually come to report to the same state ministry responsible for the economy, often headed by a deputy prime minister.
development strategy, making the undersecretariat the home of Turkey’s emergent competition state. In hindsight, the merger between these two bodies with such veritable differences in function might be seen as an overstatement on the part of the reformist elite in pressing home the message that integration with the world markets was the way forward. In context, however, the creation of such a large organization at the nerve center of the Turkish economic bureaucracy had more than a symbolic meaning. Before 1980, a likewise central position in economic governance was held by the DPT, the body responsible for the well-being of the import substitution drive. Just as the DPT of the 1960s and 1970s was staffed mainly by the star pupils of Keynesian interventionism, so the Treasury of the 1980s and 1990s would become the exclusive domain of a new generation of liberal bureaucrats. The undersecretariat’s quick rise to prominence after 1983 with a vast executive authority thus did not only tip the scales against the Ministry of Finance in terms of organizational prowess; it was also a way of counterbalancing the DPT at a much more ideological level, putting the cream of the statist bureaucracy on the defensive. With a single blow the pecking order among bureaucratic elites changed decidedly in favor of those supporting liberalization and export-led growth.

Fourth, the transformation of the Treasury was a tactical response to Turkey’s persistent debt problem. The new organization reflected the reformist conviction to tackle this problem via an active debt management strategy under a separate institutional roof, keeping it outside the purview of the traditional bureaucracy. The consequences of this novel orientation were immense. The acceptance of debt as a long-term reality on the one hand, and the post-crisis disenchantment with reliance on international markets for debt refinancing, on the other, compelled the Treasury to look for solutions from within. At
home, however, both the IFIs and inflation-conscious neoliberal reformers agreed that monetization of debt (that is, managing outstanding debt via printing money) was no longer an acceptable strategy. A more feasible route to avoid dependence on international markets was domestic borrowing through government securities, which in time would place the banking system at the very center of debt management. To render these instruments attractive, banks were allowed to retain Treasury bills and government bonds against their liquidity requirements. After 1985, a weekly auction system was adopted to create an orderly market for high-interest and tax-free government papers (Celasun and Rodrik 1989, 741; Eğilmez 2004, 81ff).

Finally, since Turkey’s relationship with the IMF and the World Bank was framed in the context of its sovereign debt problems, the undersecretariat became the natural counterpart of these organizations within the Turkish state. One may very well speculate that the former General Secretariat of International Economic Cooperation, which would be renamed as the General Directorate of Foreign Economic Relations, was included in the new construct due to this simple fact. Officials from the IMF and the World Bank did not find in the Undersecretariat old-fashioned bureaucrats and stubborn politicians they had had to deal with in the 1970s; they found like-minded colleagues who spoke the same monetarist language and had similar policy sensibilities.

The changes in the regime of public finance mirrored the dynamism in financial sector governance discussed before. Rupture and innovation, rather than adaptation and continuity, was the dominant pattern, with new rules, instruments and actors characterizing many areas of the fiscal landscape. As for the modalities of change, there was again a wide variety. Rule-based reorganization seems to fit the changes in the
income tax regime, whereas the introduction of the KDV scheme constitutes a typical example of *layering*. Extra-budgetary funds (EBFs) are a difficult case, for although they represented an important procedural novelty, they did not always entail new tasks. Many EBFs were mandated with functions that had been previously or were still currently carried out under other state agencies (e.g. mass housing or defense spending). In that sense they had an auxiliary presence. And many remained strictly attached to their mother agencies, which in some instances formed a clear example of layering. More commonly, these flexible funds stood for new ways of doing old things, and often via old tools.\(^\text{19}\) The most suitable concept from the institutionalist literature to describe this type of change is therefore *bricolage*—innovation through a recombination of elements and principles that are already part of the present institutional repertoire.

Categorizing the transformation of the Treasury is not any easier. As opposed to the SPK, this was not exactly a case of institution creation from scratch, as the bureaucratic units that made up the new undersecretariat were already in existence. Yet it did not fit the pattern of bricolage either, for it involved the emergence of whole new tasks and novel mechanisms of governance. Functionally, such novelties indicate an instance of layering whereby additions to an existing structure displace older mechanisms in time. Such was the case of domestic borrowing through Treasury bills and government bonds, which increasingly supplanted Central Bank financing. Organizationally, on the other hand, the origination of the Undersecretariat was a process of *regrouping*. Simply, well-established departments were carved out of their home ministries and molded into a

\(^{19}\) One important exception that did not exactly fit this pattern was the public sale of income-sharing certificates of large state investment projects such as the Bosphorus Bridge and the Keban Dam. Revenues from these sales were used mainly in mass housing projects. Still, the majority of the EBFs relied as their main sources of income on conventional tools of resource mobilization such as earmarked taxes and levies.
brand new synthesis which in the end was more than the sum of its parts. Many attributes were carried over to the emergent organization, but new ones were also added.

As in the case of financial reform, the restructuring of state finances was conditioned primarily by non-domestic factors. If we were to assign any weight to domestic factors, our main candidate should be the secular need for fiscal retrenchment in the context of crisis. Yet it is hard to present even that constraint as a purely domestic variable, for the way it was translated into concrete policy measures was heavily mediated by conditionalities attached to program lending by multilateral agencies. The approval and guidance of the IMF and in particular the World Bank was crucial at almost every step of fiscal restructuring, from the prolonged emphasis on expenditure restraint to commitments to lower income taxes and the adoption of some institutional novelties. For instance, KDV was first proposed in the SAL II of May 1981. Likewise, among the SAL V (June 1984) conditionalities were “the installation of computerised debt management system” and “issue and diversification of the means of marketing treasury bonds” (Öniş and Kirkpatrick 1991, 25).

Much more important for explaining the institutional dynamism in the regime of public finance was Turkey’s continuing debt problem. The main trouble here was neither revenue collection nor expenditure patterns—the two potential domestic culprits. In the early 1980s public revenues did increase, from 19.8 percent of GNP to an average of 22.6 percent for the period 1981-85; during the same period total public expenditure as percentage of GNP remained about unchanged (Celasun and Rodrik 1989, 734). This meant a significant improvement in the ratio of incomes to expenditures, which rose from
about 76 percent in 1980 to 93 percent (ibid.), reflecting a smaller budget deficit and hence decidedly lower levels of public sector borrowing requirement (PSBR).²⁰

Yet despite considerable fiscal retrenchment, external debt continued to be a nuisance, rising slowly during the early 1980s but then quite sharply from 1985 onwards. The problem was aggravated, first, by the exchange rate regime and, second, by the termination of debt relief and the necessity to re-enter international credit markets on less favorable terms. Continuous real depreciation of the lira stood at the core of Turkey’s export boom in the 1980s. Active management of exchange rates proved a simple but effective policy tool for enhancing external competitiveness. According to Celasun and Rodrik’s (1989, 727) calculations, exchange rate policy alone explains 37 percent of the increase in exports during the period of 1979-1984. However, sizeable depreciations also had the adverse effect of inflating the domestic currency cost of external debt, putting additional pressure on an already tight fiscal position. This in part accounts for the heterodox patterns introduced before: “depreciations deteriorate the underlying real public-sector budget, necessitating recourse to increasing domestic borrowing, inflation and ad hoc revenue-raising measures such as price hikes for SEE products” (Rodrik, 1990: 190). In short, modest increases in external debt stock translated into a disproportionately high drain on fiscal resources.²¹ The success of outward-orientation

²⁰ Celasun and Rodrik (1989) rely on DPT and Central Bank figures. Another source on the subject, but this time resorting to Ministry of Finance figures, reports somewhat different findings, with the ratio of revenues to expenditures showing a more modest improvement, from 86 percent in 1980 to an average of 91.7 percent between 1981-85 (Karataş 1995, 133). These two sources also give different PSBR figures. Celasun and Rodrik’s (1989, 737) estimates point to a decline in PSBR from 9.9 percent of the GNP in 1980 to 4.9 percent in 1985, while Karataş (1995, 136) cites a sharper drop from 12.6 percent to 4.6 percent during in the same period. In any event, evidence for an improved fiscal balance during the first half of the 1980s is irrefutable.

²¹ From 1980 to 1984, while total external debt increased by about 32 percent (from US$15.7 billion to US$20.8 billion), its ratio to GDP rose by a disproportional 58 percent (from 21.96 percent to 34.59 percent). This was in spite of average growth rates of over 3 percent in this period. The difference stemmed
ironically rested on a worsening external position, which provides part of the explanation for the dynamism in public resource mobilization and debt management.

The other part of the explanation lay with Turkey’s relationship with international lenders. Following its debt crisis in 1977-78, Turkey managed to reschedule much of its foreign debt. Between 1978 and 1982, a total of about US$10 billion was renegotiated with the OECD governments and commercial banks with favorable grace and maturity periods (Celasun and Rodrik 1989, 754-5). The amount of debt relief granted by the OECD consortium through this rescheduling effort reached US$3.5 billion, or close to 30 percent of Turkey’s financing needs for the period 1978-81. Bilateral official assistance from OECD governments as well as generous IMF and World Bank lending took care of the rest (Ibid: 752-3). This lenient approach on the part most notably of official lenders is often attributed to international political and security considerations of Western governments at the time. In particular, it is suggested that the Iranian revolution augmented Turkey’s strategic importance as both NATO’s southern flank and the only unconditionally pro-Western government in the region (Arıcanlı 1990, 242ff).

But as Rodrik (1988, 170ff) observes, after 1982 the effects of debt relief began to wane and Turkey was forced once again to increasingly depend on short-term private inflows in order to finance its existing debt. One source of such flows was credits extended to domestic commercial banks. From 1984 to 1985, within a year after foreign exchange liberalization, capital inflows via the banking system rocketed from a mere US$66 million to US$1.17 billion (ibid., 172). Another important item was a practice known as the Dresdner Bank scheme, which accounted for about 40 percent of all short-

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purely from the free fall of the Turkish lira (calculated from HM 2003; USD-TL conversions based on average Central Bank buying rates).
term debt by 1985. This practice allowed the Central Bank to channel the savings of Turkish migrant workers in Europe via the German Dresdner Bank at very high interest rates—typically “4-5 percentage points over the London interbank borrowing rate (LIBOR)” (ibid., 173). Thus, in the absence of further opportunities for rescheduling (debt relief came to an end in 1984), Turkey was compelled to re-enter international credit markets on much less favorable terms than had been offered by official lenders. In effect it started servicing its “preexisting long-term debt...[via]...substantially more expensive short-term debt” (Celasun and Rodrik 1989, 760). This return to short-term maturities and higher interest rates increased the burden of external debt service exponentially, to 3.1 percent of GNP in 1985 compared to 0.9 percent in 1981 (Celasun 1990, 56).  

In sum, the conjunctural (that is, crisis-related and short-term) need for fiscal restraint could, to some extent, account for the relatively modest patterns of institutional novelty in public resource mobilization, even though any such change was closely overseen by multilateral agencies. Yet it was the structural and long-term problem of foreign indebtedness, triggered by the requisites of export-led growth and the unavoidability of reliance on international financial markets for public finance, which explains the more radical transformation of the regime of debt management. Reformers saw that structural problem, and addressed it by instituting at the centre of economic governance a giant technocratic organization with the capacity not only to manage public debt but supervise the cash flow of the entire public sector, enforce the foreign trade

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22 This meant that the 54 percent increase in external debt stock from 1981 to 1985 (from US$16.6 billion to US$25.7 billion) translated into an over 340 percent increase in the ratio of external debt service to GNP.
regime, regulate and supervise an increasingly internationalized banking sector, and carry out relations with multilateral lending agencies: the undersecretariat.

*From Form to Function: Institutional Effects*

So far the discussion has focused on the patterns and the causes of institutional change in the governance of the financial sector and the fiscal regime. My argument has been that the various types of innovation that characterized the construction of a new fisco-financial order could be explained with reference primarily to a series of international considerations, which disproportionately augmented the leverage of evolving international norms about financial governance vis-à-vis pre-existing designs for institutional reshaping. In this part, I wish to briefly discuss the domestic consequences of this new order. It must be warned in advance, however, that the real effects of the new order were to be felt only toward the end of the decade, but especially in the 1990s. Still, a cursory look at the mid-1980s helps us identify some novel tendencies in financial markets and debt financing—tendencies that would form an integral part of Turkey’s macroeconomic failures over the next 15 years or so.

Let us begin with a few observations on Turkish financial markets, looking at the period 1980-1986. Basic indicators of financial deepening during this period suggest that reform opening did benefit the development of financial markets. The stock of financial assets increased by about 2.5 times at constant prices (Akyüz 1990, 105), and the ratio of bank assets to GNP climbed from 31.4 to 49.4 percent (TBB 1998a). Meanwhile the ratio of deposits to GNP doubled, from 15.4 to 30.9 percent (ibid.). Yet ironically, the credit
market shrank in relative terms throughout the entire period. The ratio of credits to GNP decreased from 25 to 20 percent (Atiyas and Ersel 1994, 118), while the share of credits in bank assets displayed a correspondent decline from about 54 to 42 percent (TBB 1998a). The bulk of this decline resulted from the waning of preferential credits once extended to state enterprises by the Central Bank and state-owned development banks, leading to a sharp drop in the share of credits received by the public sector, which almost halved between 1979 and 1985, from 50.2 to 27.2 percent (Akyüz 1990, 108).

The corporate structure of the financial sector, however, remained basically unchanged until the late 1980s. Public and private commercial banks continued to dominate the sector and had about equal share of total assets, with public banks having a slight edge in credits and private banks in liquid assets. And even though the number of foreign banks rose from 4 in 1980 to 17 in 1986, this translated into an increase in their share in total assets only from about 3 percent to 4 percent, reinforcing their miniscule role in the system (TBB 1998a). The oligopolistic composition of the market also persisted, with the Big Four accounting for about 50 percent of commercial credits as well as deposits. Another element of continuity was the weakness of private capital markets. Although the institutional framework had been in place for several years, private bond and equity issues during the opening year of the stock exchange (1986) were insignificant, and so was the volume of trading in these instruments—a mere 2.5 percent of total trading (ISE 1995).

With respect to fiscal aggregates, it was mentioned before that the first half of the decade saw a rise in public revenues relative to GNP and comparatively stable levels of total expenditure. The stability in this latter item was illusory, however. In the face of the
steady increase in current transfers due in particular to the rising cost of debt servicing and refinancing, fiscal balance was maintained only by further repressing public spending, including public real wages as well as welfare expenditures such as education and health (Celasun 1990, 46-7). And although PSBR fell, deficit financing came to rely increasingly on domestic borrowing via issuing treasury bills and government bonds, pushing up their ratio to GNP from an annual average of 1.6 percent for 1982-83 to over 9 percent for 1984-86 (Celasun and Rodrik 1989, 741). Concomitantly, Central Bank financing of fiscal deficits declined sharply, from 34.3 percent of public borrowing in 1980 to an annual average of 19.4 percent for 1981-86 (Karataş 1995, 135).

This state of affairs in financial markets and deficit financing, although pedestrian at first glance, had some revolutionary implications for the collective actors involved. The first was the rapid emergence of a powerful private financial interest. Before liberalization, banking was an activity which turned safe, easy, though modest profits. But in the 1980s, especially once the dust settled after the bankers’ crisis, profit margins rose to unprecedented levels. Particularly riding on incomes from foreign exchange operations and government securities, private commercial banks were the winners of the new era. Private banks benefited from overall financial deepening and new instruments and practices brought on by the new order, but unlike their public counterparts they were neither saddled with public functions nor restrained by fiscal considerations. Data presented in Table 4.1 clearly indicate that after 1983 the balance between public and private commercial banks was reversed, with private bank net profits (after tax) as well as profit margins first catching up with and then surpassing those of public banks. Likewise, as shown in Table 4.2, private bank equities increased much
faster than public banks’, which suggests a strong momentum in private capital accumulation in the sector.

Table 4.1  
*Net profits and profitability in the banking sector (1979-1987)*

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<td>Net Profits (US$ Million)</td>
<td>(153)</td>
<td>106</td>
<td>200</td>
<td>136</td>
<td>72</td>
<td>194</td>
<td>188</td>
<td>188</td>
<td>304</td>
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<tr>
<td>Profitability a</td>
<td>-1.5</td>
<td>1.7</td>
<td>2.6</td>
<td>1.6</td>
<td>0.8</td>
<td>2.2</td>
<td>1.8</td>
<td>1.6</td>
<td>2.1</td>
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<td><strong>Private Commercial Banks</strong></td>
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<tr>
<td>Net Profits (US$ Million)</td>
<td>47</td>
<td>85</td>
<td>94</td>
<td>54</td>
<td>98</td>
<td>174</td>
<td>185</td>
<td>323</td>
<td>463</td>
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<tr>
<td>Profitability</td>
<td>0.4</td>
<td>1.3</td>
<td>1.2</td>
<td>0.6</td>
<td>1.2</td>
<td>2.3</td>
<td>1.9</td>
<td>2.7</td>
<td>3.1</td>
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<td><strong>Sector Totals</strong></td>
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<tr>
<td>Net Profits (US$ Million)</td>
<td>(21)</td>
<td>251</td>
<td>371</td>
<td>300</td>
<td>293</td>
<td>503</td>
<td>458</td>
<td>605</td>
<td>882</td>
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<tr>
<td>Profitability</td>
<td>-0.1</td>
<td>1.7</td>
<td>2.1</td>
<td>1.5</td>
<td>1.5</td>
<td>2.7</td>
<td>2.1</td>
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a Profitability = Net profits / Average Total Assets


Table 4.2  
*Owners’ Equity (1979-1987) (US$ million)*

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<tr>
<td><strong>Public Commercial Banks</strong></td>
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<tr>
<td>691</td>
<td>453</td>
<td>650</td>
<td>593</td>
<td>798</td>
<td>882</td>
<td>878</td>
<td>750</td>
<td>931</td>
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<tr>
<td><strong>Private Commercial Banks</strong></td>
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<tr>
<td>298</td>
<td>184</td>
<td>290</td>
<td>541</td>
<td>546</td>
<td>554</td>
<td>658</td>
<td>769</td>
<td>1,065</td>
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*Source:* TBB (1998a). The figure includes the sum total of paid-up capital, legal reserves, revaluation funds and losses.

A second important tendency was the growing symbiosis between this ever-strengthening financial interest and a fiscally ever-precarious state. Its main vehicle was the strategic preference to finance fiscal deficits through domestic borrowing (Table 4.3). Commercial banks would find government bonds particularly lucrative, with interest
rates exceeding the consumer price index by 15 percentage points on average between 1983 and 1986 (Celasun and Rodrik 1989, 737). They further profited by serving as the main players in the secondary markets for government papers. According to Öncü and Gökçê (1991), it was this extreme gainfulness of banking on the state along with other opportunities presented by the new era which explains the political quiescence of the banking sector at a time of extreme policy insulation: “so long as individual banks continued to profit, the Turkish banking oligopoly has been unwilling to openly challenge the prevailing policy exclusiveness” (ibid., 109).

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<tbody>
<tr>
<td><strong>Government Bonds</strong></td>
<td>685</td>
<td>238</td>
<td>366</td>
<td>894</td>
<td>545</td>
<td>1,294</td>
<td>1,895</td>
<td>2,385</td>
</tr>
<tr>
<td><strong>Treasury Bills</strong></td>
<td>822</td>
<td>1,410</td>
<td>1,600</td>
<td>349</td>
<td>1,355</td>
<td>2,345</td>
<td>2,670</td>
<td>4,613</td>
</tr>
<tr>
<td><strong>Total Borrowing</strong></td>
<td>1,507</td>
<td>1,648</td>
<td>1,966</td>
<td>1,243</td>
<td>1,900</td>
<td>3,639</td>
<td>4,565</td>
<td>6,998</td>
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*Source:* Calculated from HM (2003). Currency conversions are based on Central Bank average buying rates per year.

This new interdependence between banks and the state involved significant tradeoffs for both parties. As commercial banks started to feed heavily upon government debt, they grew a vested interest in fiscal expansion. By 1986, the idea of a lean and fiscally efficient state was no longer a happy prospect for Turkish bankers. Nor was the banking community thrilled with export promotion any more, since the heaping up of foreign credits in the system was making the opportunity cost of continuing with cheap domestic currency far exceed profits from trade financing. Thus, within a few years into financial liberalization, the macroeconomic preferences of banks were to dissociate considerably
from those espoused by neoliberal reformers. In addition, as the stakes were getting higher, radical exclusion from policymaking was becoming much less acceptable. For the state, meanwhile, increased dependence on the banking system for debt financing would undermine the goals of both fiscal and financial prudence in the long run. Domestic borrowing was considered a good alternative to more expensive foreign borrowing or inflationary advances from Central Bank, but it too proved costly. More importantly, it made strict interpretations of supervisory principles or a strengthening of the regulatory regime an unpalatable option for fear of stirring up trouble in the banking system. The more the state relied on banks, the softer it was willing to go on them. There were other reasons for this diminished appetite for keeping banks in line, including the complications flowing from the involvement of public banks in domestic borrowing. For instance, it is widely known among industry professionals that during the initial years of the bidding system the Treasury was occasionally forced to call in favors from some public banks to be able to sell the projected amount of government papers or keep interests within acceptable margins. In short, increased domestic borrowing in the mid-1980s was making bankers reconsider their support for orthodox neoliberalism while forcing the state to gradually ease its guard against the banks.

Third, the emergence of a strong financial interest with heterodox policy preferences complicated the relationship between banking capital and the ‘real economy’. Before liberalization, banking interests were not markedly different from large industrial and commercial interests; what was good for the goose was ordinarily good for the gander. Financial sector transformation in the first half of the 1980s led to a divergence of these interests. On the one hand were the changes in the cost, profitability, and
availability of bank credits extended to the private sector. Akyüz’s (1990, 112) calculations suggest that the spread between average interest on deposits and average cost of credits rose from 11 percent in 1982 to 15.3 percent in 1984 and 24.2 percent in 1986. But even though credits were becoming more expensive, they were no longer as profitable for banks. For instance, in 1986 private commercial banks’ interest income from credits did not even cover their interest expenditure on deposits. In fact, throughout the 1980s non-interest income of these banks greatly exceeded their interest income, attesting to the diminished lure of traditional banking activities (TBB 1998a). Furthermore, record levels of domestic borrowing by the Treasury after 1983 were to exert a strong pressure on the availability of credit. The share of credits in the total assets of private banks would slide from 46 percent in 1983 to 33 percent in 1988. As Atiyas and Ersel (1994, 132) put it, “the government’s recourse to the financial system to finance the budget deficit crowded out financial flows to the private sector”. By the mid-1980s, particularly non-exporting industrial and commercial interests suddenly found themselves competing directly against the central government for expensive credit.

An equally important factor that complicated the relationship between financial and real interests was the interlocking ownership structure between commercial banks and large industrial groups. In the past commercial bank ownership was the privilege only of the biggest conglomerates. The 1980s would see a proliferation of this pattern, not toward new large private retail banks but in the direction of smaller and more profitable investment and trading banks, whose hands were not as tied as the former in terms of credit limitations concerning affiliated persons and companies (Buğra 1994, 204ff). However, lucrative opportunities in banking also meant that any group bank
would now have to be treated as a firm for itself, rather than an auxiliary unit to serve group interests, openly or clandestinely. Under these conditions, the growth of interpenetration between banking and non-banking capital engendered two new collective dilemmas for big business. First, non-credit-related activities had became so attractive for banks that it was hard to gauge with any certainty which course of action on the part of the group bank would contribute more to the bottom line of the conglomerate. Especially in a context of rapidly changing macroeconomic conditions it was often impossible to determine if the group would do better in the long run by digging into bank funds to nurture affiliated companies with cheap credit or by concentrating on, say, safe and easy government papers. Second, the sharp differentiation of financial and real interests was making it difficult for the biggest holding companies, which had their feet in banking as well as industry, to settle on a coherent set of policies to lobby for. Should exchange rates go up or down? Is high inflation tolerable? Should fiscal retrenchment continue? Such questions could only be answered on a case-by-case basis and with only short-term considerations in mind. In short, when extreme policy insulation was coming to an end, the unanticipated ascendance of financial interests was obscuring the policy preferences of the most powerful segment of the Turkish bourgeoisie.

4.3 Agriculture: Insulated Accommodation

While fisco-financial governance during reform opening was characterized by dynamic patterns of institutional change, agricultural governance, by contrast, exhibited formal persistence. Turkey’s first generation reformers did not eliminate corporatist
mechanisms of market governance in agriculture. Rather, they retained the pre-existing structure, yet neutralized its redistributive effects. Devoid of its populist counterpart, the same interventionist machine was redeployed as a tool for checking rural incomes. It is this unique dissociation of long-standing institutional forms from their conventional effects that I explore in this section.

My thesis is that this reorientation of the agricultural regime falls under the type of reshaping I have termed *insulated accommodation*. In the absence of strong nondomestic incentives for sectoral reorganization, Turkey’s technocratic reformers chose to accommodate their policy preferences within pre-existing arrangements. The first part of the section presents the evidence for the retreat from rural populism in the first half of the 1980s, which I describe as a process of *institutional conversion*. I then account for the unwillingness of Turkey’s early market reformers to undo rural corporatism, emphasizing sectoral asymmetries in the process of outward-orientation and the state of global policy wisdom in agriculture at the time. Finally, I briefly reflect on the implications of institutional conversion for state-peasant relations.

_Institutional Conversion: The Evidence_

The previous chapter has demonstrated that since the end of the Second World War the Turkish state governed market relations in the agrarian periphery through a redistributive paradigm of agricultural support. For this it relied on three interlocking mechanisms: price supports, through which the state procured large amounts of produce at pre-announced prices and thus set market prices from the center; input subsidies,
including both physical inputs and credit allocated through various state and parastate agencies; and corporatist associations of interest representation, which were the original home of a complex web of party patronage and clientelism spanning the other two tiers as well. At its height during the 1970s, this agricultural machine fell under no less than five different ministries, and included the largest commercial bank in the country (Ziraat), the largest interest association (TZOB), about half a dozen state-owned enterprises, over a dozen regional cooperatives with hundreds of branches countrywide, and some two thousand local credit cooperatives. Populist redistribution through this gargantuan network was an integral part of the social compromises that underpinned Turkey’s state-led, import-substituting industrialization. And despite its enormous fiscal cost, it was not economically unjustifiable either, for it engendered a well-functioning market for commercialized agriculture and ensured respectable levels of domestic demand for an inward-oriented industrial sector by protecting popular incomes.

The advent of neoliberalism tipped the balance against the long-established social contract in agriculture. It is widely accepted that “transferring real income away from the rural economy [and] towards the urban industrial and financial ventures” was a core characteristic of economic adjustment in Turkey in the much of the 1980s (Çakmak, Yeldan, and Zaim 1996, 444). Evidence for this retreat from rural populism is strong, if somewhat patchy. The current OECD database on agricultural support estimates for Turkey starts from 1986, so there is no help there. Also, the State Institute of Statistics’ (DİE) time series for aggregate prices received by farmers begins at 1987.23 Still, there is sufficient data to piece together a fairly coherent picture for the period.

23 This is an important statistic that allows direct comparisons between the GDP deflator, various price indices and aggregate farmgate prices. Pre-1987 data set is based on individual crops and current prices.
One important source is Kasnakoğlu’s (1995, 249ff) calculations of Producer Subsidy Equivalent (PSE) for the period 1979-1990, building on the OECD methodology at the time. Kasnakoğlu estimates that in the first half of the 1980s producer subsidies as percentage of agricultural value added plunged ten times, from 28 per cent for 1979, which was very much in line with OECD figures, to a meager average of 2.8 per cent for the five-year period between 1980 and 1984. Subsidy levels recovered slightly in the mid-1980s to reach an average of just under 6 percent for 1980-1986, but still trailing the OECD average for the same period (around 35 percent) with a great margin.

A recent study conducted by two Ministry of Agriculture (MARA) researchers sheds some light on different aspects of this sharp drop in subsidies (Yeni and Dölekoğlu 2003, 44-5). Accordingly, the period 1981-1986 recorded extremely low levels of market price support, remaining under $200 million for the entire period. Fertilizer subsidies seem to have been less affected, but concessional credits dried up particularly during the first few years of the decade. Yeni and Dölekoğlu find that total transfers to agriculture in 1980-87 were quite stable, averaging around $850 million annually. Since Turkey’s agricultural GNP was in the order of US$12-18 billion for the period, this indicates that the subsidy regime contributed around 5 to 7 percent of the total agricultural value added—a conclusion consistent with Kasnakoğlu’s analysis.

Korkut Boratav’s (1990, 212ff) estimates of agricultural terms of trade during reform opening put these figures in perspective. According to Boratav, from 1977 to 1986 agricultural terms of trade plummeted by 53 percent relative to the GDP deflator.  

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24 PSE measures monetary transfers to farmers as percentage of agricultural value added, including both market (e.g. price supports) and non-market (e.g. inputs) transfers. In the 1990s OECD revised this early methodology and renamed the index as Producer Support Estimate (using the same abbreviation of PSE) which usually forms the most important component of the Total Support Estimate (TSE) of a country.
While much of this decline took place during the crisis years of 1978-79, support policies of the 1980s put further pressure on agricultural prices rather than correcting the problem. Boratav provides two sets of evidence for the policy-induced nature of price repression in Turkish agriculture. First, the government intervened less in the agrarian markets by purchasing a smaller portion of the marketable output. The value of state procurement decreased from 20.4 percent of total agricultural value added in 1976 to an annual average of 12 percent in 1980-87. Second, government intervention worked to preempt any price recovery. Weighted support prices lagged consistently behind wholesale agricultural prices as well as the general price index during this period. For example, while the wholesale price index rose by 6.1 times from 1981 to 1987, the prices received by farmers in wheat and sugar beets, the twin locomotives of independent peasantry, increased only by 5.1 and 5.2 times, respectively (DİE 2003). Boratav concludes that “government policies towards agricultural prices have, at best, aimed to keep intact the adverse price structure which had emerged during the crisis years; and, at worst, been deliberately used to depress them even further” (1990, 217). Purchasing less at lower price points explains this dynamic.

Ironically, this neoliberal suppression of agricultural incomes hinged upon the very same arrangements that had transferred wealth to the countryside for decades. Unlike labor unions, for instance, which were castrated during the 1980 coup, mechanisms that had once ensured populist redistribution in agriculture persisted. The government continued to announce base prices for support purchasing annually, and cooperatives remained in business as ever. Agricultural state enterprises, along with the colossal Ziraat, kept operating in very much the same way as in the 1970s. From a
policymaking viewpoint the difference was quantitative in essence: fewer products were actively supported, credit was scarce, and prices were not right.

This anomalous continuity of the support regime constitutes a model case of conversion. Streeck and Thelen define institutional conversion as “redeployment of old institutions to new purposes” (2005, 31). Elsewhere, Thelen describes conversion as “institutions being functionally and politically turned on their heads” (2003: 230). The guiding mechanism for such change is a reorientation of institutional objectives. This may result as much from new environmental challenges as shifts in the collective interests linked to that institution. In both circumstances structure and function are decoupled. Eventually, the same design is put in the service of formerly alien goals.

The conversion of the support regime from an instrument of income transfer to one of income repression poses the key question of why early neoliberal reformers ditched rural populism while preserving corporatist market governance in agriculture. Four factors account for this odd transformation. Fiscal restraint and technocratic insulation were the principal reasons behind the reversal of rural populism. These two are rather straightforward and will be readily dealt with below. The pattern of market integration and the absence of design-specific policy pressures from outside explain why the interventionist machine was kept intact. These latter two factors are less obvious, yet more important for the general line of argument. They will thus be discussed in a separate subsection.

Policy insulation under authoritarian rule and a contractionary fiscal policy typical of orthodox neoliberalism worked directly against the one crucial factor of resilience behind rural populism—its distributive effects. The former made redistribution irrelevant;
the latter made it unfeasible. The 1980 coup closed the Turkish polity to party competition along old lines, cutting off rural interests from policymaking. Freed from the yoke of democratic contest, Turkey’s liberal reformers lacked any incentive to honor the populist contract. Besides, the reduced influence of the traditional, statist bureaucracy vis-à-vis neoliberal technocrats pre-empted any intra-state opposition to price repression. Fiscally, meanwhile, government resources were simply needed elsewhere. Decent growth rates did not bear old style fiscal expansion. For instance, as part of the decline in non-interest expenditures, transfers to state economic enterprises, a sizeable segment of which were agricultural, decreased from 16.4 percent of consolidated budget expenditures in 1980 to just 1.6 percent in 1986 (DİE 2003). This left large agencies such as the Turkish Grain Board (TMO) or Sugar Factories with much less room for maneuver. Equally decisive was the Central Bank’s abandonment of its status as a semiofficial development bank, leading to a diminution in cheap funds for subsidized credit via Ziraat as well as support purchasing through sales cooperatives. In short, while technocratic insulation under authoritarian politics made side payments to the countryside politically unnecessary, fiscal restraint made them economically unsustainable.

**Explaining Persistence: Sectoral Asymmetries**

Although bent on putting an end to rural populism, Turkey’s early market reformers were unmistakably apathetic toward the institutional shell of the subsidy regime. Not a single step was taken to dismantle prevailing policy tools, let alone any attempt to devise different mechanisms of support. As a senior observer of Turkish
political economy noted, agriculture was the “forgotten sector” during Turkey’s initiation into market reformism (Ergüder 1991). This was the tendency not simply because neoliberal elites broke the social contract with the peasantry but also because they had little interest in the sector as a whole. The causes of this should be sought in the sectoral asymmetries in the process of internationalization, which, in stark contrast with financial governance, indirectly reinforced pre-existing mechanisms of corporatist intervention.

The stasis in the support regime was in part a reflection of the marginal relevance of Turkish countryside for the new export-oriented strategy of development. One reason for this, of course, was a built-in bias on the part of Turkish reformers toward manufacturing exports as the preferred channel of integration with international markets, reflected in the advent of a comprehensive export subsidy regime. I have argued in the previous section that the strategic reorientation of Turkish industry was one of the main motives behind financial restructuring as well. This bias toward industry in the real sector was further reinforced by the broader international price trends in agricultural commodities. Lying in the vicinity of Europe’s overprotected agricultural markets and in a world conjuncture of falling commodity prices, Turkey’s relatively inefficient, smallholder-dominated agriculture was hardly a good candidate for competitive integration into the international economy. From 1971-73, when Turkey’s support machine reached maturity, to 1981-83, when policymakers turned away from rural populism, real international prices of crops that were of largest economic and political significance to Turkey either remained stable (e.g. wheat and tobacco) or declined considerably (e.g. sugar by about 30 percent and cotton by about 20 percent) (FAO 2004, 38). Moreover, prices of almost all major agricultural commodities would take a plunge.
in the remainder of the 1980s, bashing any hopes for restoring agriculture’s status as a
crucial exporting sector. Consequently, from 1980 to 1987, the share of agricultural
commodities in Turkey’s export income would plummet from 56.6 percent to 17.6
percent. Compare this to the share of generously subsidized industrial exports, which
jumped from 36.9 percent to 79.7 percent (DİE 2003).

That the dominant pattern of market integration largely bypassed Turkish
agriculture simply meant that it deserved neither the institutional attention nor the
administrative energies of the technocratic elite. Insofar as the fiscal consequences of pre-
existing arrangements did not undermine the wider goals of economic adjustment,
reformers were more than willing to let them be, rather than engaging in a costly process
of reorganization with incalculable outcomes. The support machine, historically designed
to operate as a tap of sorts by regulating peasants’ incomes at politicians’ will, met this
criterion. When democratic channels were closed, orthodox economic rationality
managed to override the redistributive effects of the support schemes, and strategic policy
input shaped institutional performance, shifting resources away from a disempowered
peasantry. By conforming to the goal of fiscal austerity while also doubling as means to
check domestic demand, corporatist interventionism turned out to be unexpectedly handy
in accommodating the macroeconomic policy preferences of early market reformers.

Nor did the intense external policy pressures of the period create discernible
incentives for sectoral reorganization and thus for substantive institutional adjustment.
Both the IMF stand-by agreements and the World Bank Structural Adjustment Loan
(SAL) projects of the 1980s centered mainly on the fiscal and inflationary strains posed
by the support regime, and were at best minimally interested in specific institutional
configurations. SAL III (July 1982), for example, made reference to “institutional reform”, but what the World Bank understood from the term at the time was nothing other than a superficial reorganization of the Ministry of Agriculture (World Bank 1985, 16-7; 81-2). Instead, the Bank’s main concern about the subsidy regime was the ‘rationalization’ of price supports and the eventual phasing out of input subsidies. The government’s response to this World Bank position was to cut down price supports considerably, as mentioned before, which indeed saved the day as these had the most visible price-distorting effects. Input subsidies were never phased out, however. The Bank not only ignored this policy ‘slippage’ but continued supporting Ziraat’s preferential credit schemes by extending three separate agricultural credit loans throughout the 1980s, while also extending a $300 million sectoral adjustment loan.

It was this latter arrangement, the Agricultural Sector Adjustment Loan Project of June 1985, which was most indicative of the spirit of the Bank’s policy guidance in the 1980s. The project merely called for cosmetic changes to the existing system without touching the core of the support regime. Accordingly, for the structural adjustment of the sector it was necessary to:

(i) reduce producer subsidization while maintaining adequate incentives; (ii) improve the input distribution, marketing and credit systems; (iii) improve the public investment allocation system in the sector (…); (iv) enhance the research, extension, protection and disease control services; and (v) strengthen management, planning, policy analysis and public expenditure programming for the sector.25

Nothing in this list, as it should be obvious to the reader by now, even remotely implies a renovation of the support regime or the introduction of an alternative design. Compared to the scale of transformation expected of financial governance at the time, the Bank’s

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stance toward agriculture could only be described as indifferent to the institutional arrangements already in place, with lending conditional upon minor changes and improvements along existing lines.

This external policy indifference toward corporatist interventionism had two main causes. First, the IFIs seemed to agree with Turkey’s technocratic elite that agriculture was destined to lose its significance as other sectors, mainly industry and but also finance, stepped in to serve as the main engines of outward-orientation. For the sector was already an overproducer in a number of cash crops and had also attained very high levels of commercialization in foodstuffs; its potentials, seen from the narrow neoliberal perspective of the time, were already well-tapped. In the final analysis, there was little to be gained by the types of sectoral reorganization achievable via institutional reforms.

Second, and more important, the current international policy wisdom in agriculture ran contrary to the tide of internal and external liberalization that had engulfed finance and industry. True, developing countries were routinely encouraged to deregulate their rural sectors, but in leading industrialized countries rural market governance was marked by the continued predominance of interventionist and protectionist norms, upon which Turkey’s support regime was also modeled. Further, the Uruguay Round of trade

26 The themes of interventionism and protectionism figure prominently in the discussions of agricultural policy in developed countries. Peter Lindert, for instance, points to two relatively continuous policy tendencies in postwar decades that “conflict directly with economists’ models of efficient resource allocation”: “the developmental pattern— the more advanced the nation, the more its government favors agriculture—and the anti-trade pattern—governments tend to tax exportable-good agriculture and protect import-competing agriculture” (1991, 29, emphasis original). The combined effect of these policy patterns has been an extreme case of interdependence between national agricultural policy preferences and international commodity flows, with a select few countries possessing the capacity to rig global prices of core products on the basis primarily of domestic political considerations (see, for instance, McCalla and Josling 1985). As the wider economic policy framework shifted decidedly toward liberalization in the 1980s, the resilience of interventionist and protectionist policies made agriculture look increasingly out of sync with other sectors. As Gale Johnson in his classic treatise on world agriculture observes, “agriculture surely stands out as the most important single case in which the governments of most industrial countries are willing to permit domestic policy considerations to override so completely their interests in achieving
negotiations, where the need for domestic agricultural policy reforms gained widespread acceptance for the first time, had not even begun. In fact, agricultural policy in the advanced economies would be guided by an interventionist paradigm well into the 1990s, delaying the emergence of plausible alternatives to such universal mechanisms as market price supports or input subsidies (Moyer and Josling 1990; Skogstad 1998). This exceptional position of agriculture in terms of global normative trends provided little inspiration or leverage for multilateral lending organizations to develop a vision of structural change in the governance of the sector other than a routine call for state withdrawal. Even though policy insulation presented Turkey with a rare window of opportunity to redesign its antiquated support mechanisms, there was no ideational foundation for such a move in the early 1980s.

Could external policy pressures have posed formidable incentives for replacing the corporatist support regime had there been internationally well-established alternative norms and designs in agriculture at the time? To answer this question, we need to fast forward some two decades, for this precisely is the problem Turkish peasants faced by 1999. Their experience since then highlights the significance of domestic politics: when insulated from the policy process, rural interests failed to defend against normative encroachment from outside; but once they took part in ruling coalitions, they were able to partially thwart top-down attempts on the pre-existing regime. In light of this insight, and given the technocratic exclusivism and intense IFI influence of the early 1980s, it is conceivable that stronger alternative norms could have inflicted considerable damage on

the advantages from increased international specialization in production” (1991, 7). And perhaps as a result of that policy dilemma, agriculture has also stood out, particularly since the early 1990s, as one sector in which incentives for domestic policy and institutional change almost solely came from considerations of promoting international trade of agricultural commodities.
corporatist-interventionist forms. Even then, because such a drive would still have lacked the company of strong market pressures, it is unlikely the scale of change would have ever matched the experience of the fisco-financial regime, which came as close to a clean break with the past as imaginable.

*Peasants and the State: The Neoliberal Paradox*

The conversion of the subsidy regime into an instrument of checking rural incomes meant that the traditionally cozy relationship between the Turkish state and the rural society was no more. Instead, there grew a deep rift between agrarian interests and policymakers. Mechanically, this fissure in agriculture was not so different from those in other sectors: it fed on policy insulation of the kind from which industrialists, bankers, and workers also suffered. Thus, during the early stages of market reform, farmers’ organizations were as functionless as business chambers, trade unions or the banking association: “there were no meetings and consultations with the leaders of the [agricultural] chambers and the other interested associations on the problems of the agricultural sector. Inputs from the representatives of the sector were not welcome; policy formulation was simply a technocratic affair” (Ergüder 1991, 76).

And yet, compared to other collective actors that had once been part of the societal coalition underpinning Turkey’s import substitution, there was something unique about the political exclusion of the peasantry. It is true that domestic bourgeoisie was also excluded from the technocratic policy process, but in the end market reform served business interests quite well. Workers, on the other hand, were never true insiders of the
political establishment. Mainstream trade unions were permeated by center-left parties in the 1970s, but strengthening working class opposition in the latter half of that decade was widely perceived as destabilizing among traditional political elites and as the biggest threat to the regime by the military. By contrast, smallholder peasantry constituted not only the largest popular class but it was also politically quiescent. Farmers’ organizations, particularly smallholder-oriented and state-guided chambers, were inextricably linked to the dominant parties of the center-right, the Democrat Party (DP) in the 1950s and its successor, the Justice Party (AP), in the 1960s and 1970s. And because support policies benefited practically all agrarian interests, peasants, unlike workers, were not in visible competition with any other social group for their share of the pie. Their declining fortunes in the 1980s therefore lacked any sociopolitical or intra-sectoral justification. Whereas wage repression was pivotal in the country’s manufacturing-export drive and business interests greatly, there were no direct societal winners or any sectoral gain from the reversal of rural populism. The only justification for the suppression of rural incomes was the cold logic of fiscal austerity.

Herein lay the paradox of institutional conversion in agriculture. The retreat from populism pitted rural interests and the state sharply against one another. The lower the agricultural prices and the smaller the subsidies, the healthier was the bottom line of the Turkish state. But at the same time, the preservation of the corporatist-interventionist framework meant that rural interests remained formally wedded to the political centre. The agricultural machine kept running in the background, although in low gear, with clientelistic channels of policy influence kept idle yet virtually intact. The problem was
not lack of means to resume conventional state-peasant relations, but lack of cooperation on the part of governing elites at the center.

This paradox, the intense policy rift between neoliberal elites and the rural society despite the presence of an institutionally thick and perfectly viable system of interest articulation, had two major implications with profound consequences to be explored in the following chapter. First, as with most popular classes in late developers, for Turkey’s smallholder peasantry as well, neoliberalism exacted significant political and economic losses. It did not, however, lead to a rapid and qualitative transformation of the rural society and politics as it did in some well-studied Latin American cases, such as Chile and Mexico (e.g. Kurtz 2004). To the contrary, in order to introduce policy change, Turkish reformers depended on the continuation of the societal and institutional balance in the countryside. Most important, the decline in rural fortunes applied to the entire sector rather than creating clear intra-sectoral winners and losers, and therefore did not result in a fragmentation or reshuffling of rural interests. Likewise, reform opening did not have an inherently corrosive impact on farmers’ organizations. Although cut off from policy formation, agricultural chambers and regional cooperatives were neither dismantled nor, as was the case in banking, co-opted by technocrats. The point, in short, is that while neoliberalism impoverished rural society and paralyzed rural politics, it did not usher in a brand new world. Market reform dealt the Turkish peasant a terrible hand, but the venue and the players remained the same.

Second, the survival of the corporatist order could help explain why rural interests did not protest against, or seek alternatives to, a now income-depressing agricultural machine even after political authoritarianism began to weaken by mid-decade. Peasants
were so firmly entrenched in but also so tightly constrained by corporatist networks that they were neither willing nor able to articulate their interests by seeking alternative organizational and political means. Rather, they hoped authoritarian insulation would soon come to a natural end, which would mean the restoration of their electoral clout. This in turn would rejuvenate populist political projects, for which corporatist-interventionism, already preserved by the technocrats, was the best possible vehicle. From that perspective, sticking with the existing framework that in the past had generously served rural interests made good tactical sense.

### 4.4 Institutions, Interests and the State

This chapter has revolved around two sets of stories. The principal storyline presented the disparate trajectories of Turkey’s financial and agricultural regimes of governance during the initial phase of market reforms. The second storyline followed the changing fortunes of collective interests that fell under these regimes. In the unfolding of events the first story almost exclusively dictated the second: collective fortunes rose and fell depending on what old and new institutions had in store for them. Furthermore, these interests had hardly any say over the construction or reorientation of the arrangements that shaped their destinies. Such was the outcome of technocratic insulation in a context of authoritarian obstacles to political contestation. In fact, policies that placed the institutions in question on such dissimilar paths were characterized by a strikingly similar disregard for domestic political considerations. This contextual lack of societal influence helps sharpen the central message of the chapter: the formative impact of wider patterns
of market and policy internationalization over sectoral institutional pathways in contemporary late developers.

Still, we are looking at a fairly brief and unusual juncture unparalleled in Turkey’s postwar history in terms of the scope of economic reorganization and the degree of political exclusion. With that caveat in mind, there is something to be learned from these sectoral patterns. The emergence of a new fisco-financial order and the conversion of the agricultural subsidy regime alert us to the wide range of institutional possibilities under marketization. Although bound only by their firm commitment to a supposedly coherent neoliberal reform agenda, Turkish policymakers adopted fundamentally different approaches to the rules and mechanisms that governed these sectors. The scale and the rapidity of transformation in the governance of Turkey’s public as well as private finances under insulated innovation, and the speed with which market players adapted to this new environment, were nothing short of amazing. Just as remarkable was the adaptive efficiency of the subsidy regime under insulated accommodation, whereby corporatist-interventionist mechanisms of market governance remained frozen in time, but rural populism was no more.

Finally, the sectoral choices made during the formative years of market reform put the Turkish state in an awkward position vis-à-vis elite/financial and mass/rural interests. The objectives behind these choices were rather innocuous: to create orderly financial markets, to modernize state finances, and to plug the fiscal drain. Translated into policy and taken as inspiration for institutional change, however, they had massive political and distributive consequences. In sharp contrast with the essence of free markets, Turkish reformers found it more opportune to retain the tight hold of the central
authority over rural incomes. But in that process they effectively reversed the direction of resource transfer, thereby estranging a disempowered peasantry. In their attempts to establish a new financial order, meanwhile, reformers not only instituted thicker mechanisms of bureaucratic control over the sector but inadvertently created new incentive structures that rendered everyday fiscal policy a vital concern for financial interests. In short, despite reformers’ avowed intention to pull the state out of the distributive game, within a few years into the reform process the Turkish state remained just as deeply embroiled in collective fortunes.

There was a major difference, though. In the past, state involvement in the economy boiled down to a delicate intermediation between collective interests on the basis of a set of reciprocal compromises. There was a distinct political balance at work. But now the Turkish state would increasingly find itself rewarding or punishing collective interests individually, without having to take into account the inter-sectoral and inter-class repercussions of such pattern. When formal and informal channels of interest articulation were clogged, this did not pose a big problem. It became one, however, as authoritarianism began to fade and party competition resumed, making governability dependent on societal and eventually party-political coalitions. The next chapter will explore the dynamics and institutional outcomes precisely of this.
CHAPTER FIVE

DOUBLE REDISTRIBUTION

The discussion in this chapter covers the evolution of Turkey’s financial and agricultural regimes of governance roughly from the late 1980s, when technocratic policymaking came to an end, until 1999, when macroeconomic imbalances reached unbearable proportions and ushered in a new episode of top-down reforms. Overall, this period differed from the first phase of liberalization, which was the subject of the previous chapter, in two fundamental ways. First, in terms of dominant patterns of internationalization, it was characterized not by manufacturing export-orientation, but rapid integration with global financial markets. This, though, did not result in a qualitative difference in the way international constraints contributed to the shaping of financial and agricultural regimes; rather, it accentuated, at least initially, the paths that had emerged earlier in the 1980s. Second, in terms of policymaking, the period was marked not by technocratic exclusivism, but complex coalition efforts under intense democratic competition. Unlike the first one, this second condition would have path-altering implications. From the late 1980s onward, negotiation with societal actors, rather than insulation from them as had been the case during reform opening, would set the tone for policy and institutional decisions. Collective interests were back.

The fact that finance replaced industry as the main engine of Turkey’s integration with international markets exposed the sector to further pressures toward convergence on global norms. In that sense the basic innovative impulse in financial governance
continued. Yet since much of that demand for convergence had already been met in the 1980s, *negotiated innovation* in finance would take the form of *continuous adjustments* and selective updates. The maturation of a strong financial interest by mid-decade and the locking-in of fiscal expansion around the same time would undermine these efforts considerably, however. Thereafter, the link between international immersion and institutional convergence in finance gradually weakened. In the countryside, agriculture’s marginal position in Turkey’s market and internationalization also continued, and thus so did the *accommodative* pattern in this sector. But with the peasantry back in the political game, *negotiated accommodation* in agriculture would see a full *restoration* of populist redistribution and a re-emphasizing of mechanisms of corporatist control.

It must be noted at the outset that the scale of change in institutional forms during this period pales in comparison to the technocratic 1980s. There is much less to report here: no brand new agencies, no revolutionary bureaucratic reorganization, and no hurried legislative activity. And even though finance, as predicted by the typology, was the more energetic sector institutionally, the extent of change in fiscal and banking regimes hardly reflected the tumultuous developments on the ground. One reason for this relative stability was all too obvious—namely, a lack of risk-taking appetite on the part of weak coalition governments motivated by instincts of short-term survival. Yet there was another reason that discouraged Turkey’s rulers from engaging in deep-seated institutional reforms in either sector despite clear signs of macroeconomic trouble: an unusual instance of complementarity between financial and agricultural regimes.

Briefly, the novel financial regime was crucial for the reinstatement of antiquated patterns of rural populism. In addressing emergent redistributive demands from popular
interests, Turkish politicians in the 1990s came to rely on deficit financing through unchecked capital inflows, channeled by the under-regulated banking system. But this process emphasized a second avenue of income transfer as well, this time toward the financiers of the public debt, mainly, commercial banks. These synchronous transfers of income toward peasants and bankers I term double redistribution. The consolidation of this accidental pattern by mid-decade would have significant political and institutional consequences. Politically, double redistribution pointed at a coalitional kernel, a de facto ruling alliance comprising populist politicians, financiers, and the peasantry, all having a vested interest in unabated fiscal expansion. Institutionally, on the other hand, double redistribution put the populist subsidy regime in agriculture, regulatory forbearance in banking, and unsound practices of debt management in public finance on a trajectory of mutual reinforcement, illustrating a coevolutionary dynamic in these institutions in much of the 1990s. Over time these arrangements got so deeply entangled that structural change in either became progressively difficult.

The material presented in this chapter also helps substantiate some broader theoretical arguments introduced earlier. In the first place, it affirms the value of institutional analysis for understanding the complex politics of market reform—a theme largely missing from the conventional, policy-oriented literature on the topic. Given much of the coalition efforts in the 1990s centered around the design and especially the effects of the institutional regimes in question, our analysis provides powerful insight into the politics behind Turkey’s lost decade. Second, the discussion here also offers some clues as to the origins, workings, and the reproduction of ‘bad institutions’, as neoliberal wisdom would come to perceive these regimes in the postcrisis period. It becomes clearer
throughout the analysis that configurations that were deemed inefficient over time did not have isomorphic trajectories after all; furthermore, not all such institutions were inherited from the pre-reform era, and none of them was marked by a complete lack of adaptive capacity to warrant being portrayed as immutable constructs standing in the way of successful market transition. Rather, underneath the relative institutional stability of this period lay a great deal of organizational and policy dynamism reflective of vibrant political struggles, which in turn rode on the unresolved dilemmas of the exclusionary reformism of the previous decade. ‘Bad institutions’ in that sense were just as much a symptom as a cause of Turkey’s transitional failures.

5.1 The Age of Coalitions

A certain double-bind characterized the Turkish political economy in the 1990s, the first signs of which had emerged during the formative juncture of the late 1980s. On the one hand was rapidly deteriorating economic performance, exposing the limitations of the primitive growth stimulus of the early reform stage and indicating the need for strong-willed policy intervention. On the other hand, intense democratic competition after 1987 would quickly degenerate into party fragmentation and political instability, rendering cohesive and far-sighted economic policymaking a distant possibility in the forthcoming decade. It was this ‘worst of both worlds’ scenario, in a perilous context of carefree financial internationalization, that would throw Turkey’s market transition off track. Below I first look at the economic troubles of the late 1980s, and then reflect on the tumultuous politics of the 1990s.
The initial years of marketization in Turkey had generated decent growth rates, averaging about 6 percent from 1981 to 1987. This, however, was achieved through a rather rudimentary strategy which included tight fiscal policy, high levels of export promotion, and a severe repression of domestic demand. Despite these efforts, the Turkish economy continued to accumulate structural weaknesses on all these fronts. Public debt proved to be a persistent problem as interest payments shot up from less than 5 to over 15 percent of fiscal expenditures from early to mid-decade. The trade balance did improve considerably during this period, but the ratio of exports to imports plateaued in the range of 70 percent due basically to the traditional import dependence of Turkish manufacturing exports. As such, the idea that Turkey could return to high current account surpluses of the interwar period by ditching its postwar regime of import substitution remained a neoliberal myth. Finally, high inflation of around 30 to 45 percent became a fixture of this early period, even though wages and agricultural prices were harshly suppressed and consumer demand lagged behind GDP growth (DİE 2003).

The slump of the late 1980s was a watershed event in that it made these structural weaknesses much more visible and consequential. Evidence for the unsustainability of the rudimentary growth strategy of early neoliberalism came in the bitter form of negative per capita growth rates in 1988 and 1989. Poor economic performance of course has many causes, and I do not attempt to offer a proper explanation of these end-of-decade troubles here. Rather, I emphasize two important facets of it: the inability of Turkey’s proto-competition state to reorient industry, and reform fatigue.
The first, and perhaps most critical from a long-term vision of economic development, was the lack of qualitative transformation of Turkish industry during the early stages of liberalization. This in part explains why export manufacturing ceased to lead Turkey’s integration with international markets in the 1990s. It was mentioned in the previous chapter that Turkey’s export boom rather anomalously relied on the utilization of excess capacity in the traditionally import-substituting sectors. Looking closer at that picture, it is noteworthy that in some such sectors (e.g. iron and steel) there remained a heavy concentration of public ownership, the antithesis of marketization. And although the emergence of the holding company, Turkey’s particular form of private sector conglomerates, had assured some diversification of activities of big capital in the 1960s and especially 1970s, unlike the South Korean chaebol (Amsden 1988, 125ff), this neither led to radical gains in productivity, nor did it concentrate in what would become the main exporting sectors. These broad tendencies would continue into the 1980s, and indeed would be reinforced by the peculiarities of that decade.

For instance, there was little strategic reorientation of private manufacturing into higher value-added goods. As late as the mid-1980s, the Turkish state was committed to encouraging private initiatives in low value-added sectors such as food processing, textiles, and forestry, while promising large-scale public investment in higher value-added ones such as petrochemicals and defense (DPT 1984, 38ff). And even in that goal it failed miserably. In fact, a most disturbing feature of Turkey’s manufacturing-led export boom was “the absence of an underlying investment drive” (Rodrik 1991, 346). Public sector manufacturing investment simply collapsed in the 1980s, while private investment, after being halved during the late 1970s crisis, recovered very gradually, and
by the end of the decade still remained well below its pre-crisis levels. As a result, “the post-1980 export orientation could not carry over into productivity gains in the leading exporting sectors and could not be sustained as a viable strategy of ‘export-led-industrialization’” (Boratav, Yeldan, and Köse 2000, 14). Rather, competitiveness in the 1980s had depended upon everyday incentives such as low wages, cheap currency, and export subsidies. The general point is that Turkey’s precocious competition state in the 1980s could not achieve the type of industrial transformation Asian developmental states had in the 1960s and 1970s.¹ From 1987 onwards, the growth rate of exports tapered off.

Not only did Turkey fail to support its export-oriented growth strategy with complementary adjustments to its industrial sector, but in hindsight and particularly in comparison to subsequent examples from Latin America and the postsocialist world, it actually did not go too far down the neoliberal path either. If one takes the policy measures listed in Williamson’s (1990) depiction of the Washington Consensus as a good summation of ‘first stage’ reforms to be undertaken by liberalizing countries, Turkey, although praised by the IFIs for its commitment to economic restructuring in the early 1980s, was only partway through that stage after a decade of efforts. The initial enthusiasm of neoliberal reformers proved illusory in the face of policy items that were either originally or later turned out to be politically and organizationally challenging: reform fatigue quickly set in. With the economy slowing down, and in a context of emergent distributive pressures to be discussed later, fiscal austerity became an insufferable political burden. Taxation, as analyzed earlier, was already the least dramatic component in the reorganization of the public finance regime; and yet the government

¹ See in particular Öniş (1995). See also Onaran and Stockhammer (2005) for the contrasting export-oriented growth strategies of South Korea and Turkey. The authors argue that decreasing wage shares in the Turkish case is one important factor that hindered the growth of both investment and productivity.
refused to restructure the income tax regime and instead expanded its reliance on indirect taxes. Most telling, however, was the impasse in privatization, the predominant policy instrument in the global transition out of state-led development strategies. The promise of privatization, expressed in the formation in 1984 of a novel agency specifically for this purpose (Mass Housing and Public Participation Fund), was the main excuse for declining public investment in manufacturing. Even then, the public sector remained large in Turkey, especially in heavy industry and banking. Indeed, by the time party competition—and hence large-scale patronage politics—resumed in the context of the 1987 elections, there was not a single sale of importance. In subsequent years, attempts at state divestiture encountered significant legal and political challenges (Karataş 1992, Patton 1992). By 1991 total privatization revenue was less than $1 billion, to reach only about $2.5 billion by 1995 (Celasun and Arslan 2001, 244f). In comparison, Mexico’s privatization revenue was in the order of $9.5 billion by 1991, and Argentina’s was $12 billion by 1992 (Teichman 1997, 41ff). As Ziya Öniş notes, “the projected retreat of the state did not materialize in the Turkish case” (1991, 38). At the root of this diminishing enthusiasm to deepen market reforms was a changing political environment.

*Political Distortions*

Turkey’s technocratic policy process in the early to mid-1980s fit an exclusionary pattern of reformism that would soon prove popular in a number of countries moving

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2 A notorious problem here was the growing weight of the informal sector in the Turkish economy under liberalization. That a substantial portion of the workforce relied on unreported incomes not only constrained the tax base, but in time would cripple the social security regime as both the primary reason for low levels of contributions to the system and by disproportionately increasing the number of dependents per beneficiary. See in particular Buğra and Keyder (2006, 216ff).
toward free market capitalism. It was shown in the previous chapter that the political restrictions and the executive bias that followed the military intervention further accentuated the non-deliberative character of this pattern. But the Turkish case had its idiosyncrasies as well. Notably, the excesses of technocratic policy insulation debilitated reformers’ political fortunes by alienating both civil and political society. Unlike postsocialist transitions, Turkey had an established capitalist class structure. Any major political-economic realignment had to work its way through the pre-reform status quo between well-demarcated collective interests. Radical exclusion of these interests at the early stage of reform was to make reconciliation problematic in subsequent years. At the same time, and unlike, say, Mexican or Argentine reformers, Turkey’s liberal policy elites lacked connections to a deep-seated political tradition, party organization, or bureaucratic presence within the state machinery to fall back on for building workable reform coalitions as distributional costs set in. In spite of these foreseeable shortcomings, Turkey’s first generation reformers, organized under the ANAP, disowned the entire machine of politics that once had connected together politicians, bureaucrats, and dominant as well as popular class interests, and replaced it with nothing other than sheer executive determination at a temporarily authoritarian juncture. In doing so, they also breached within a few short years the gamut of class compromises that had kept Turkish industrialization afloat in the postwar decades. It was obvious, then, that the gaps and fissures that had opened up between the policy path of neoliberal reformism on the one side and the remainder of the Turkish state and society on the other were to cost reformers dearly once electoral competition resumed.
Turkey’s political-economic history in the 1990s could be read in terms of constant efforts on the part of neoliberal as well as old-style political elites to patch up these gaps and fissures as the precondition of everyday governability. This process began quite precisely in 1987 when a referendum lifted the political ban on the ruling cadres of the parties abolished during the 1980 coup. In the general elections of the same year, Özal’s reformist ANAP managed to remain in power only by relying on some age-old redistributive mechanisms to win the favor of popular interests—tactical delays in public sector price hikes, generous subsidies in agriculture, and so on. For the next few years, the ANAP tried in vain to hold on to a narrow-winning center-right coalition; it now openly aimed at complementing export-led growth with discretionary side-payments toward urban and rural losers of reform (Waterbury 1992). Its rivals, mainly the successors of the leading center-right and center-left parties of the 1960s and 1970s, were much more adept in connecting with social forces, though. The ANAP eventually lost the 1991 elections to parties that brought together old school politicians and traditional bureaucratic elites. This marked the beginning of a string of weak coalition governments that were interested more in short-term political survival through opportunistic alliances with collective actors than far-sighted, coherent economic policymaking. The ANAP stayed alive, however, and was frequently called on to join these coalitions, mainly in the second half of the decade.

Our analysis cannot afford a lengthy description of the governmental coalitions of the 1990s, whose rise and fall invariably coincided with a mix of political crises, economic troubles, and classic cloak-and-dagger politics of the purest kind. The reader can refer to Tables 5.1 and 5.2, which offer a chronological list of these coalitions, along
with a run-down of the main political parties and leaders during that decade.\(^3\) What is important here is that the intense electoral competition of the post-1987 period was not accompanied by democratic deepening or consolidation. It would perhaps be too harsh to judge this period as one of ‘antipolitics’ (Cizre-Sakallıoğlu and Yeldan 2000, 503ff), for this would be a more suitable characterization of the technocratic reformism of the 1980-1986 period. Still, it was certainly marked by a deep democratic deficit (Alper and Öniş, 2003a). Civil society flourished throughout the decade, but political society was in worse shape than it was in the 1970s. Years of authoritarian rule led to the deinstitutionalization of the party system; center-right and center-left remained fragmented among two major parties each, and were dominated by mostly autocratic, corrupt and uncompromising leaders (Özbudun 2000, 73ff). The result was high electoral volatility, loss of legitimacy, and the erosion of the political center as reflected in the success of fringe political movements such as Islamists under the RP and ultra-nationalists under the MHP. Meanwhile the restrictions of the 1982 constitution, drawn by the coup leaders of the time, continued to strangle the polity. Crucial in that context was the rise of two regime-challenging political forces that had long been brewing in the straitjacket of Turkish nation-building: Kurdish separatism and Islamic fundamentalism.\(^4\) The former was confronted militarily on and off the battleground during a long civil war; the latter was to be domesticated and then slowly and conditionally incorporated into the system. In both

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\(^3\) For detailed accounts of main Turkish political parties and leaders in the 1990s, see compilations by Sayar and Esmer (2002) and Rubin and Heper (2002).

cases, the defensive stance adopted by Turkey’s ruling civilian-military elites served as a practical blockade on the prospects for democratic consolidation.

**Table 5.1 12 Governments in 12 Years (1987-1999)**

<table>
<thead>
<tr>
<th>Tenure</th>
<th>Ruling Party / Parties</th>
<th>Prime Minister</th>
</tr>
</thead>
<tbody>
<tr>
<td>December 1987 (+ 1 year 11 months)</td>
<td>ANAP</td>
<td>Turgut Özal</td>
</tr>
<tr>
<td>November 1989 (+ 1 year 7 months)</td>
<td>ANAP</td>
<td>Yıldırım Akbulut</td>
</tr>
<tr>
<td>June 1991 (+ 5 months)</td>
<td>ANAP</td>
<td>Mesut Yılmaz</td>
</tr>
<tr>
<td>November 1991 (+ 1 year 7 months)</td>
<td>DYP-SHP</td>
<td>Süleyman Demirel</td>
</tr>
<tr>
<td>June 1993 (+ 2 years 4 months)</td>
<td>DYP-SHP</td>
<td>Tansu Çiller</td>
</tr>
<tr>
<td>October 1995 (+ 1 month)</td>
<td>DYP</td>
<td>Tansu Çiller</td>
</tr>
<tr>
<td>November 1995 (+ 4 months)</td>
<td>DYP-CHP</td>
<td>Tansu Çiller</td>
</tr>
<tr>
<td>March 1996 (+ 4 months)</td>
<td>ANAP-DYP</td>
<td>Mesut Yılmaz</td>
</tr>
<tr>
<td>July 1996 (+ 11 months)</td>
<td>RP-DYP</td>
<td>Necmettin Erbakan</td>
</tr>
<tr>
<td>June 1997 (+ 1 year 7 months)</td>
<td>ANAP-DSP-DTP</td>
<td>Mesut Yılmaz</td>
</tr>
<tr>
<td>January 1999 (+ 4 months)</td>
<td>DSP</td>
<td>Bülent Ecevit</td>
</tr>
<tr>
<td>May 1999 (+ 3 years 6 months)</td>
<td>DSP-MHP-ANAP</td>
<td>Bülent Ecevit</td>
</tr>
</tbody>
</table>

Turkey’s democratic mishaps in the 1990s are important because they defined the main character of the *negotiative* patterns through which financial and agricultural institutions were shaped in that decade. To be expected by now, the incorporation of collective interests into the policymaking process during that period did not take the form of meaningful policy debate based on democratic social deliberation, although there were some feeble attempts precisely at that. Rather, the general pattern was the resurfacing of older forms of patronage politics and constituency clientelism (Heper and Keyman 1998). Yet an important problem was that such articulation of collective interests did not rely on a developmental reciprocity, as had been the case with the broad social compromises and cross-class coalitions that had characterized the era of import substitution. To the

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5 Most notable here was the establishment of the Economic and Social Council in 1995, which brought together representatives of the economic bureaucracy and the main interest groups, including business associations, labor unions, and chambers of agriculture and of the self-employed. The Council, which already operated in a consultative capacity, met only a few times in the remainder of the decade to discuss some general matters.
### Table 5.2  Parties and Leaders

<table>
<thead>
<tr>
<th>Party (Abbreviation—Full Name)</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>ANAP</strong> (Anavatan Partisi—Motherland Party)</td>
<td>Center-right, neoliberal. Considerable weight of conservative factions in the 1980s and political populists in the 1990s. Garnered support mostly from urban middle and upper classes. Led by reformist Turgut Özal in the 1980s, who went on to become President in 1989. In much of the 1990s, led by Mesut Yılmaz, a young neoliberal with strong business connections.</td>
</tr>
<tr>
<td><strong>DYP</strong> (Doğru Yol Partisi—True Path Party)</td>
<td>Center-right, liberal-populist. Successor to the dominant AP (Adalet Partisi—Justice Party) of the 1960s and 1970s. Peasantry and private sector as traditional support base. Led by veteran politician Süleyman Demirel, a patrimonial figure, until his Presidency in 1993 upon Özal’s death. Afterwards Tansu Çiller, an economics professor, took control of the party.</td>
</tr>
<tr>
<td><strong>DTP</strong> (Demokrat Türkiye Partisi—Democratic Turkey Party)</td>
<td>A splinter group of DYP dissidents, founded in 1997 in reaction to DYP’s coalition with the Islamist Refah. Had some parliamentary presence in subsequent years, but failed in the 1999 elections.</td>
</tr>
<tr>
<td><strong>SHP</strong> (Sosyal Demokrat Halkçı Parti—Social Democratic Populist Party)</td>
<td>Center-left, statist, progressive. Successor to CHP (see below) from the mid-1980s onwards until it joined the latter in 1995. Decent performance at the polls in the late 1980s and early 1990s. Led by Erdal İnönü, a physics professor, and Murat Karayalçın, former mayor of Ankara.</td>
</tr>
<tr>
<td><strong>CHP</strong> (Cumhuriyet Halk Partisi—Republican People’s Party)</td>
<td>Center-left, statist. Founded by Atatürk, and turned into the main party of the mainstream left in postwar decades. Workers, civil servants and Alawi minority as traditional support base. Its electoral fortunes declined in the latter half of the 1990s after joined by SHP and under the leadership of Deniz Baykal, a sectarian figure from the 1970s.</td>
</tr>
<tr>
<td><strong>DSP</strong> (Demokratik Sol Parti—Democratic Leftist Party)</td>
<td>Center-left, nationalist-populist. Founded by Bülent Ecevit, CHP leader in the 1970s, but remained the smaller party of the left. Gained popularity in the late 1990s and eventually came to power in 1999 thanks to its strong nationalist rhetoric.</td>
</tr>
<tr>
<td><strong>MHP</strong> (Milliyetçi Hareket Partisi—Nationalist Action Party)</td>
<td>Ultra-nationalist, statist. Represented the Turkish far-right during the violent political polarization of the late 1970s. Led by Alparslan Türkeş, of military background, from the 1960s on until his death in 1997. Did well in the 1999 elections under Devlet Bahçeli, an academic, securing a place in the three-party coalition government.</td>
</tr>
</tbody>
</table>

Contrary, Turkish governments of the 1990s bowed to distributive demands from both winners and losers of market transition individually, with little concern for long-term macroeconomic consequences.
Since the rest of the discussion in this chapter is on peasants and bankers, it is only fair to reflect briefly on the fortunes of the other two major collective actors during this period: labor and industry. These cases are useful not only because these groups are the main social contestants in a capitalist society but also because, compared to other interests in the Turkish context, they include more universal mechanisms of interest intermediation, that is, labor unions and business associations. In the case of labor, resurgent union activity in the late 1980s paid off remarkably, with a 90 percent increase in real wages in manufacturing from 1988 to 1991 (Boratav, Yeldan, and Köse 2000, 5). Such spectacular hikes, spearheaded by a populist drive in public sector wages, were absorbed through foreign financing after capital account opening, high mark-up rates in private sector, and labor-shedding (ibid., 6-7). Likewise increases were observed in the salaries of civil servants, completing the recuperation of the reform losses of the two major urban popular classes. There were two main problems, though. First, the wage boom was short-lived, and was quickly reversed in the aftermath of the 1994 shock. Annual rate of growth of real wages in manufacturing for the 1994-1997 period was -2.01 percent (Boratav and Yeldan 2001, 65). Second, the 1990s also witnessed an explosion of the informal sector, paralleling the expansion of small and medium size firms both in metropolitan areas and the Anatolian heartland, in which wage levels were (and still are) much lower. In short, continued worker activism in the second half of the decade failed to sustain and expand labor-based populism. If the growing inability of both private and public sectors to absorb further wage increases was one reason for this, another, and perhaps more important, reason was the drastic right-wing tilt in Turkish politics after
1995. This condition, as will be discussed later in this chapter, saw peasantry as the more permanent and dependable popular-class ally of governmental coalitions.

As for the articulation of industrial interests, there was a dual process at work. On the one hand, persistent macroeconomic instability under rapid financial globalization complicated industrial preferences, creating considerable uncertainty but also niches for easy gain. True, the exponential growth in PSBR did divert domestic bank credits away from industry, and inflationary strains and diminished export incentives produced a particularly unattractive investment climate. Yet at the same time, high inflation permitted some flexibility in pricing, and financial integration made it possible to find cheap foreign credit, especially given an overvalued lira in much of the decade. Further, toward the end of the decade, fiscal expansion began to prove quite lucrative for large industry as well, as interest income from government securities were deployed to cover losses of profitability (Sönmez 2002, 91).

On the other hand, and unlike the technocratic insulation of the early reform stage, the 1990s brought about tighter connections between industry and policymakers. At the formal level, and surprisingly, the DYP did a better job than the ANAP of carrying organized industrial interests into the parliament, such as Jefi Kamhi, heir to one of the largest industrial groups very active in the elite business association of TÜSİAD, and Yalım Erez, the long-time president of the Union of Chambers (TOBB), who went on to serve as the Minister of Industry and Trade in consecutive Çiller cabinets. Informally, meanwhile, and this point holds true for the entire private sector, patronage politics, nepotism, and personal networks gained much salience from the late 1980s onward. Given the lax regulatory mood of the decade, this in turn was the source of rampant
corruption, evidenced in a series of political scandals involving family members or former associates of most major political figures, particularly of the center-right. In that regard Turkey in the 1990s clearly mirrored the wider trends in liberalizing late developers, with marketization exacerbating existing problems of graft and often creating new channels for personalistic gain (Harriss-White and White 1996).

5.2 Finance: Negotiated Innovation

The first half of the 1980s had seen the rise of novel regimes of governance in both the financial sector and public finance, including an extensive reregulation of the banking sector, a bold remodeling of the Turkish Treasury, and the emergence of an autonomous agency in capital markets. I have argued in the previous chapter that the main type of change during this time was one of insulated innovation: a dynamic generation of neoliberal technocrats, concerned with problems of foreign indebtedness and the requisites of export-led growth, engaged in sweeping institutional reforms with practically no challenge from social actors.

By contrast, there was much less institutional fanfare in the post-1987 period. The regimes established during the era of insulated reformism mostly persisted, but there were attempts at selective innovation in the spirit of evolving international norms. Two factors appear to be crucial in the design and implementation of these changes. First, international opportunities and constraints, but this time stemming directly from the internationalization of Turkey’s financial markets, became an important motive for innovation and adjustment early in the decade. Second, now open, now hidden social
bargains, especially after 1994, drew the limits of how much and what sort of change
would be permissible. In this way the main pattern of institutional reshaping in fiscal and
financial regimes came close to an ideal-type I have depicted as *negotiated innovation*,
although this was not a very tight fit, as analyzed below.

*Continuous Adjustments*

Major institutional changes typically come in the form of drastic measures, such
as whole new laws or substantive organizational shake-up. There are, however, instances
where formally unassuming policy acts set in train larger events and, in their outcomes,
would qualify as fundamental institutional change. Turkey’s capital account opening was
one such instance. In August 1989, months after local elections that saw the ANAP
trailing the SHP and the DYP with a considerable margin, Özal unveiled before an
audience of Istanbul industrialists a new Council of Ministers decision that practically
lifted all controls over capital movements and established the full convertibility of the
lira. The Decision No. 32, a concise document which was neither a law nor even an
executive decree, took as its legal basis the ancient Law No. 1567 on the Protection of the
Value of Turkish Currency, dating back to 1930 (*Resmi Gazete*, 11 August 1989).6 The
decision famously stipulated that “import of foreign exchange into Turkey is free”, and
allowed banks and other financial institutions to engage liberally in foreign exchange
operations of all kinds, leaving most regulatory technicalities to the Central Bank.

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6 The way capital account liberalization was introduced mirrors Özal’s changing mindset in the late 1980s
from bold reformer to cautious politician. Ercan Kumcu (2003), deputy governor of the Central Bank at the
time, later revealed the legal backstage of this move: “[T]he logical step was to write up a new foreign
exchange law in the spirit of the Decision No. 32 and to annul Law No. 1567. (…) This proposition, along
with a draft law, was submitted to Özal, the architect of Decision No. 32. Özal did not like the proposition
to annul Law No. 1567. ‘This law might be useful to some government some day. Let it stay,’ he said.”
As mentioned in chapter four, the move to liberalize the capital account had indeed started in 1984 by allowing banks to retain foreign exchange deposits, although there were significant restrictions in place. The 1989 decision in that sense was the maturation of that policy inclination to financially integrate with international markets, and thus represented a continuation of an existing path rather than a radical break. But there was an important and novel domestic consideration as well. It was thought that such integration would also help sustain growing fiscal outlays that had become politically inexorable given the popular distributive pressures of the late 1980s (Ersel 1996). Celasun and Arslan (2001, 131) nicely sum up this dual rationale:

Evidently, the deregulation of capital account aimed at the unification of domestic and world financial markets as a further step toward integration with the international economy in general and the European Union in particular… [A]nother important motive was to encourage and facilitate capital flows to relax the financial constraint on surging public expenditures.

This pattern of simultaneous international and domestic considerations would be partly reflected in other institutional efforts around the turn of the decade. Chief among these were regulatory measures concerning the banking sector and the capital markets. In both, convergence on novel international norms along the already existing path was considered instrumental for the stable development of domestic financial markets.

In banking, the transition out of interest rate controls, which had encountered significant setbacks during the early reform stage, was finalized. 1988 saw the last of Central Bank interventions in deposit rates. In 1990, and following the Decision No. 32, banks were also allowed to set their exchange rates as well as interest rates on foreign exchange deposits freely (Atiyas and Ersel 1994, 108ff). Perhaps more important was the adoption of the Basel framework for capital adequacy ratios. The original Banking Law of 1985 already empowered the Central Bank to set adequacy ratios. Shortly after the
Basel I Capital Accord of the Bank for International Settlements (BIS) in 1988, and with the by-law No.6 of October 1989, Turkish policymakers signaled their commitment to conform to emerging international benchmarks in this area. The required ratio was set at 5 percent for 1989 to incrementally reach the recommended 8 percent by 1992.7

In capital markets, meanwhile, and this was about the only major piece of legislation regarding the financial sector in the 1987-1999 period, the Law No. 3794 of 1992 refined and updated the original Capital Markets Law, which had been introduced over a decade ago during the infancy of market transition. Just as capital account opening and regulatory measures in banking, this too was not a rupture but a progression along existing principles: “The scope of authority of the [Capital Market] Board was enlarged and financial innovations were made easier in terms of the development of new instruments and institutions by the market itself” (Balkan and Yeldan 1998, 140). The new law defined and regulated the activities of investment companies and mutual funds, and set the framework for criminal responsibility in capital market operations (Resmi Gazete, 29 April 1992). Here again, a primary motive appears to be adaptation to changing realities on the ground, namely the growing internationalization of Turkish financial markets. Paralleling the increased foreign presence in the Istanbul Stock Exchange, for instance, and in a foresighted act of wishful thinking one might add, the law also set a basic framework for the exportation of Turkish private sector bonds.

All three major institutional changes of the late 1980s and early 1990s, then, could be interpreted as efforts toward consolidating the novel financial regime that had

7 The Basel framework defines capital adequacy as the ratio of a bank’s capital to its risk-weighted assets. The original accord in 1988 was often criticized for taking into consideration credit risk only, and would be substantially revised in 1996 to include market risk as well. The Basel I Accord was eventually replaced with Basel II in 2004, also known as the New Accord. See Baker (2002) for the evolution of the BIS standards in banking regulation. See also Seabrooke (2006).
emerged during the heyday of technocratic reformism. Their innovative content, however, should not be dismissed as they introduced significant adjustments to the existing framework. Furthermore, both capital account liberalization and the improvements in banking as well as capital market regulation signified a qualitative shift in the policy proclivities of neoliberal reformers, from financial liberalization for the sake of facilitating export-led growth to international financial integration as a goal in itself.

On the other hand, the negotiative character of these changes was quite indirect. Capital account opening, insofar as it also aimed at facilitating deficit financing, was certainly influenced by the fiscal burden of the social alliances an electorally battered ANAP attempted to strike with peasants and workers around that time. Yet it was not negotiated with any social parties, and was perhaps the last major example of Özal’s insulated reformism.\(^8\) This lack of societal deliberation applied to banking and capital market reforms as well. Still, from the absence of any opposition to these measures from within the private sector at a time when authoritarian repression was no longer a factor, we can surmise that they did indeed receive the tacit approval of increasingly powerful financial interests. After all, the changes discussed so far ensured the continuation and the deepening of the structural trends commercial banks had found very profitable from the mid-1980s onwards. But when, later in the decade, policymakers tried to implement institutional measures that could jeopardize financial profits, they would encounter stiff resistance and be forced, through both market and political pressures, to cut deals that invariably favored these collective interests. The 1994 shock was a milestone in that process.

\(^8\) Indeed, Celasun and Arslan (2001, 231) note that Decision No. 32 even took bureaucratic planners by surprise, with no mention of it in the Sixth Development Plan (1990-94). So it rode on a dynamic of intra- as well as extra-state insulation that so fundamentally characterized Turkey’s early neoliberal reforms.
The Turkish meltdown of 1994, along with the Mexican crisis of the same year, was one of the first manifestations of the perils posed by unregulated capital flows in an age of financially-driven neoliberal globalization. For the purposes of our analysis, though, its story should be started from 1990, when Turkish technocrats, in a context of soaring public debt, high inflation, and record interest rates, quickly diagnosed the danger that would be fulfilled in the coming years—that is, the ease with which fiscal deficits were financed through increasingly internationalized domestic commercial banks. Their solution was not a retreat from capital account opening, but to discipline the regime of public finance. In this spirit, a protocol was signed between the Treasury and the Central Bank to “limit public sector borrowing requirement and the monetization of the fiscal deficit” (Balkan and Yeldan 1998, 132). On the basis of this protocol the bank even announced a new anti-inflationary monetary program. This first move toward central bank independence—an old idea with renewed popularity among inflation-conscious monetary authorities worldwide (e.g. Alesina 1988)—did not go far, though. Quite simply, given the fiscally expansionary impulse in Turkish politics around the election year of 1991, the Treasury did not honor the protocol and resumed its traditional practice of tapping Central Bank resources for debt financing, basically ordering the bank to print money. And the new coalition government, led by Demirel’s populist DYP and the social democratic SHP, certainly had no interest in this sort of fiscally constrictive institutional arrangement. To the contrary, in 1992, and in the context of an ‘arbitration law’ that rescheduled the debt to Treasury of some public agencies (primarily public enterprises

9 The issue here was that the Treasury had made a habit of asking the Central Bank repay government securities on their maturation date without subsequently depositing the amount back into its account in the Bank. Continually surpassing the legal limit of its cash advances from the Bank, the Treasury account was often ‘in the red’. In other words, by the late 1980s there emerged a mini “overdraft economy” (Loriaux 1991) between the Turkish Treasury and Central Bank.
facing increased wage costs), Demirel managed to sneak in a write-off scheme for the Treasury’s negative account balance in the Central Bank, thus allowing a second round of cash advance (Eğilmez 2004, 41).

The problem of intolerable fiscal deficits was there, nonetheless, and the rise of Tansu Çiller, an economics professor, to DYP leadership and prime minister in 1993 appeared to have provided a window of opportunity to tackle it. Convinced that the main source of vulnerability in Turkish economy was the high interest cost of fiscal borrowing due in particular to the Treasury’s structural dependence on the banking sector, Çiller decided to break this cycle by canceling previously announced Treasury auctions and relying instead on low interest rate Central Bank advances. This attempt on the part of the Turkish government to exit financial markets for managing its deficits backfired rapidly. In early 1994, the excess liquidity in the system, coupled with the lowering of Turkey’s investment rating by international credit rating institutions and rumors of a pending major devaluation, caused a run on foreign exchange. In the following months, a sharp capital outflow halved Turkey’s international reserves, and overnight rates in interbank markets reached 1,000 percent (Öniş 1996; Öniş and Aysan 2000; Özatay 1996; Yentürk 1999). Yet only after the March 27 local elections did the government announce an economic package, which included a severe devaluation of the lira, and sharp rises in taxes and public sector prices. The crisis took its toll on the real sector as well, forcing halts in production in several major manufacturing plants and a string of bankruptcies in the commercial sector. The Turkish economy shrank by over 6 percent in 1994.

Perhaps the most important consequence of the 1994 shock for our purposes was that it catapulted financial interests onto the Turkish political scene. Çiller’s attempt at
bypassing market forces, even momentarily, for fixing fiscal problems proved disastrous. And with it died hopes of disciplining the sector, at least in the absence of powerful international anchors. In institutional terms, the crisis induced two important measures. The first was the introduction of 100 percent state guarantee on all commercial bank deposits, which was seen as the price of rebuilding confidence in the Turkish financial system. This essentially wrote a blank check to banks as to the terms by which they could collect deposits, and would prove to be a major source of moral hazard in the sector in the rest of the decade. The second was yet another reorganization of the Treasury. In 1983 export-obsessed neoliberals had merged two state agencies, one responsible for public cash flow and the other for export promotion, under a single massive technocratic organization, the Undersecretariat of the Treasury and Foreign Trade. In late 1994 Çiller separated the two into different undersecretariats that answered to different ministers, putting an official end to the early neoliberal conviction that state finances and the country’s export-based growth strategy had to be governed single-handedly.

Recovery from the 1994 shock was quick, though, with both industrial production and growth bouncing back strongly in 1995, thanks in part to a symbolic IMF loan in the order of about SDR 600 million that helped re-establish investor confidence. This in turn brings us to another important feature of the 1990s, that is, the absence of policy compulsion from international organizations. IMF and World Bank conditionality had been crucial in guiding Turkey’s reform efforts in the 1980s. The structural and sector adjustment loans of that decade had accorded high priority to the recasting of the country’s fiscal and financial regimes. By contrast, with the exception of 1994, Turkey was outside the purview of the IFIs throughout the 1990s. The World Bank, for instance,
remarks that “by 1993 the Turkey portfolio was considered one of the weakest in the
Bank”, and in the years that followed the 1994 crisis “the Bank-Turkey relationship was
at low ebb” (World Bank 2005a, 5-6). Furthermore, until the Asian crisis of 1997, the
IFIs had little to offer in terms of new institutional norms in finance other than encourage
further internal and external liberalization as in the 1980s. The primary international
constraint for Turkey during this period, then, was the preferences of global market
players—more specifically, how much they were willing to risk in a country with bad
macroeconomic fundamentals but, and indeed precisely because of this, offered
handsome arbitrage gains. And given the option between long-term direct investment and
short-term capital movements, the international preference was unmistakably toward the
latter.  

The aftermath of the shock also saw the ossification of the mechanism of deficit
financing through capital inflows. The years 1995-1997 represented a “reinvigoration of
short-term foreign capital-led growth” (Boratav and Yeldan 2001, 5), fortifying the
erroneous policy belief that this mechanism might yet prove viable in the medium term,
provided some adjustments were made to prevent its abuse. The most critical of these
was a renewed attempt at reorganizing the relations between the Treasury and the Central
Bank. A 1994 legislation put a cap on short term bank advances to the Treasury, from 15
percent of total budgetary appropriations progressively to 3 percent of deficits by 1998,
although the stock value of these advances increased in 1995 and 1996 (Evgin 1998, 3;
66). This was followed by a 1997 protocol by which the Treasury committed itself not to
resort to cash advances at all (Eğilmez 2004, 61). During the same year a more active

10 Foreign direct investment in Turkey during the period 1990-99 averaged a dismal US$600 million per
year, less than half of net short term capital inflows despite sizeable outflows in 1991 and 1994 (TCMB
Annual Reports, various years).
debt management strategy was adopted; the Treasury expanded its operations and began repurchasing government securities from secondary markets to increase efficiency in its cash flow (Sağlam 1997a). Finally, upon Turkey’s membership in the Financial Action Task Force, an Anti-Money Laundering Law (No. 4208) was passed in 1996, leading to the creation of a Commission for the Investigation of Financial Crimes (MASAK) under the Ministry of Finance (Bakdur 2003, 24). None of these measures, however, addressed the fundamental weakness of Turkish deficit financing—that is, structural reliance on the open foreign exchange positions of commercial banks. Fiscal debt was ‘manageable’ insofar as Turkey’s bank regulators turned a blind eye to balance sheets.

The difficulties Turkish banks began to face in finding affordable foreign financing from 1997 onwards, due primarily to global volatility following the Asian crisis, exposed this problem by leading to a sharp increase in the interest cost of debt financing. In turn, 1998 was a year of intense policy debate around new bureaucratic proposals, the cornerstone of which was a legal package that made various amendments to existing tax laws. In essence this was a pro-industry and anti-finance move: it included overall tax cuts (10 to 15 percent) and granted tax amnesties, but in return expanded the tax base toward financial incomes, including a stoppage tax on all interbank transactions and taxation of government securities (Cizre-Sakallıoğlu and Yeldan 2000, 491; TBB 1999 Annual Report, 5-6). Another effort was a draft ‘Financial Sector Reform Bill’, prepared by the Treasury, which proposed the creation of an autonomous banking agency to regulate the sector. Finally, as part of a monitoring agreement with the IMF during the summer of 1998, banks’ open positions were limited to 30 percent of their paid capital.
All these efforts encountered strong resistance from the banking community. Especially smaller banks lobbied the weak three-party government to reconsider these drastic proposals, and won. The tax package passed, but its stipulations regarding the financial sector were overturned via executive decrees in subsequent months: stoppage tax on interbank transactions was lifted, and taxes on government securities were reduced from 5 to 1 percent. Meanwhile, the financial reform bill was shelved; the TBB, which had trumpeted the need for stronger regulation for some time, kept silent over the issue. The cap on open positions, on the other hand, was circumvented easily via manipulations on balance sheets. It was estimated, for instance, that by early 1999 open positions in the Turkish banking system were around US$15 to 20 billion, or about five to six times what it should have been according to the 30 percent rule (Kumcu 1999). Treasury and Central Bank regulators were well aware of this irregularity, but also politically instructed not to pursue the matter.

Three main factors explain the Turkish government’s lack of teeth vis-à-vis the banking sector. One was a pervasive belief within the economic bureaucracy, especially early in the decade, that a somewhat forgiving attitude toward bankers might indeed help achieve the greater goal of financial deepening.\footnote{Interview, Deputy General Director (Anonymous), the Undersecretariat of Treasury, 23 December 2004.} Just as the DPT protected Turkey’s infant industries under import substitution despite their inefficiencies, so the Treasury and the Central Bank saw little logic in crushing Turkey’s budding banks at a time of growing financial integration. During the 1994 shock, for instance, only three very small banks were taken over by the TMSF, while others in comparable trouble were spared.

A second factor was fear of a repeat of 1994; policymakers were unwilling to take drastic regulatory measures that could alienate foreign asset holders and further limit
Turkish banks’ access to global funds. This reflected a classic ‘race to the bottom’ mentality, which nonetheless would prove utterly wrong in 1999. Still, the level of fiscal exposure to commercial banks was so high, as we will see in the next subsection, that such a fear was not exactly without merit. An important part of this puzzle was the unavoidability of continued fiscal expansion—a subject to be more properly explored in the context of double redistribution.

A third reason for lax regulation was much simpler: a vested interest in the ‘bad governance’ of the sector on the part of some bankers and corrupt politicians. The main issue here was not an absence of rules, but one of rule-following. Consider this instructive passage from Erdal Sağlam (1998a), a top economy columnist well-versed in the intricacies of Turkish financial policymaking:

After becoming the minister responsible for the economy [1991], Çiller and her spouse got too palsy-walsy with the owners of some smaller banks. These bankers used to tell Çiller “what she should do”, and even fax to the Treasury some debt issuance proposals favorable to their position. And because “half her brain” [Tevfik Altnok] was in charge of the Treasury, these proposals that in fact deeply offended the bureaucracy were swallowed. (...) Çiller later became the prime minister [1993]. During that period privileges were granted to certain banks through Y.T. [Yaman Törüner] whom she had placed in the Central Bank [as Governor]. (...) During that period some banks, thanks to the connections of their owners in high places, used to hit the “bulls-eye” in Treasury auctions. Ministers talked to bank bosses, made arrangements for paper [government securities] sales and negotiated interest rates. Other banks would observe what these banks did and decide their market behaviour accordingly [translation mine].

Çiller remained the dominant figure in economic policymaking until 1997, but state-banker relations were not particularly different after her departure. Yılmaz and his economy minister Güneş Taner picked up where she had left. At the height of the policy debates over financial sector reform in 1998, for instance, Yılmaz attended an

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12 Interview, Manager (Anonymous), Banking Regulation and Supervision Agency (BDDK), 14 July 2004.
13 In fact later that year both Yılmaz and Taner would be implicated for irregularities in the sale of small public bank. The scandal also involved connections to mafia bosses, and led to the fall of the ANAP-DSP-DTP coalition via a censure motion, necessitating a minority DSP government until elections were held.
exclusive meeting with the owners of five smaller banks, upon which Taner announced
the government had reached an agreement with the sector (ibid.). Larger banks were
troubled by this covert initiative from smaller banks on such a fundamental matter that
concerned the entire sector. The outcome, though, was favorable, as it would appear it
was during this meeting that the proposal for an independent regulatory agency was
defeated. As Sağlam (1998b) reported a few weeks later,

Banks do not want the rules to be decided by an independent council; they do not want
to be governed by rational rules that apply to everyone equally... [B]anks prefer to do
business through one-on-one relations with those in power, ministers and the Prime
Minister, by occasionally receiving special privileges but in the meantime overlooking
the privileges of their rivals [translation mine].

The dynamic between larger and smaller banks was a function of this general
attitude. Larger banks often accused smaller banks of gaining unfair advantage by relying
on their special political relations to ignore the rules (Sağlam 1997b). And the Turkish
Banks’ Association, dominated by larger banks, closely followed the evolution of new
international norms and made suggestions for improving standards of supervision,
internal control, transparency and credit accounting (e.g. TBB 1997; 1998b; 1998c;
1999). Yet both the association and the directors of the larger banks simply remained
indifferent to the numerous bureaucratic initiatives of the late 1990s that sought precisely
such improvements, and let instead profit-aggressive smaller banks fight technocrats and
a handful of idealist politicians (such as Zekeriya Temizel, DSP’s finance minister)
against the introduction of new rules as well as the full observation of existing ones.

Further compounding this picture was the question of public banks, whose weight
in the system had lessened, but was still considerable throughout the decade. Populist
politicians of the 1990s put public banks in the service of two main tasks that were
equally destructive of their bottom line. The first, and this was an age-old practice, was
resource allocation through Ziraat and Halk in the form of cheap credits toward agriculture and small business, which eventually bore massive ‘duty losses’. Second, and this in itself was an innovation, was to use state-owned banks for domestic borrowing and occasionally for the manipulation of Treasury auctions. “It is true that,” remarked a Treasury official, “when bids [from private commercial banks] were insufficient, public banks were made to intervene. These are things that happened in auctions; they cannot be proven.”14 In this way, public banks operated as a security valve for everyday debt management. Tighter regulation of the sector would have exposed these within-state irregularities; it would also make duty losses much less tolerable, and would thereby severely challenge the social bargains that kept weak governmental coalitions alive.

To conclude, the 1990s was a decade of contrasts for Turkey’s fiscal and financial regimes. On the one hand, there was considerable institutional dynamism, although less than in the reformist 1980s. Much of this dynamism could be traced to the growing market internationalization of Turkey’s financial sector. Innovations from the late 1980s onward aimed at ensuring a smooth integration with global markets; there were also efforts, in particular after 1994, to contain the perceived and realized risks of increased international exposure. On the other hand, what followed out of these efforts were not rigorous regimes of governance, but an institutional cacophony with weakly enforced rules and unsustainable arrangements. The root cause of this failure to build sound institutions should be sought in the domestic politics of that decade, and especially in the augmented political weight of financial interests, reflected first in tacit bargains and then open negotiation. Toward the end, unbreakable fiscal dependence on commercial banks,

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14 Interview, Manager (Anonymous), the Undersecretariat of Treasury, 24 August 2004.
coupled with state capture by smaller finance capital and shady operations of public banks, undermined any attempt at substantive course change.

By now it should also be clear that patterns of reshaping during this period constituted only a loose fit with the *negotiated innovation* type. First of all, there was more innovation and less negotiation before 1994, and more negotiation and less innovation after. Second, while international norms and coalition politics were the main guiding forces behind the shaping of fiscal and financial regimes throughout the entire period, the remaining explanatory variables of the research were still significant. Technocrats were the main architects of earlier innovative efforts, although it is hard to imagine how such insulation would have gone unchallenged by that time had it threatened financial interests and coalition efforts. Perhaps more important, after 1994, pre-existing regimes inherited from neoliberal reformers began to show signs of stickiness. Because financial interests during the 1990s crystallized around the structural weaknesses of the existing framework, they tolerated only a select few types of innovation and update while easily defeating half-hearted attempts at regulatory reform.

*Financial Revolution, Fiscal Collapse*

The discussion has thus far explored the processes and politics of institutional reshaping in Turkey’s financial and fiscal regimes in the 1990s. In this subsection I would like to briefly reflect on the outcomes of these processes, or what precisely was taking place on the ground as far as Turkey’s bankers and fiscal policymakers were concerned. These outcomes are important not only to link changes in institutional forms
to institutional effects, but given the relatively lengthy historical focus of this chapter, to put into perspective the progression of different institutional measures as well.

Let us begin with the hallmark of the 1990s, that is, short-term capital movements channeled through commercial banks. The rapid increase in international capital flows since the 1980s is often considered a main source of fragility for both host countries and the global financial system at large. Critics widely agree that premature capital account liberalization, usually followed by intense exposure to speculative movements, lay at the root of the string of financial crises that engulfed many countries in the semi-periphery in the 1990s, generating new types of risks both decision-makers and domestic market actors were ill-prepared to manage (e.g. Kahler 1998; Rodrik and Velasco 1999; Stiglitz 2000; Griffith-Jones, Montes, and Nasution 2001; Eichengreen 2004).

### Table 5.3

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Short-Term Capital Flows (US$ Millions)</th>
<th>Banks Total Loans (Annual Balance)</th>
<th>Banks Short-Term Loans Received</th>
<th>Banks Short-Term Loan Repayments</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td>3,000</td>
<td>1,245</td>
<td>1,014</td>
<td>N/A</td>
</tr>
<tr>
<td>1991</td>
<td>-3,020</td>
<td>1,199</td>
<td>663</td>
<td>43,186</td>
</tr>
<tr>
<td>1992</td>
<td>1,396</td>
<td>2,411</td>
<td>2,402</td>
<td>64,767</td>
</tr>
<tr>
<td>1993</td>
<td>2,994</td>
<td>3,975</td>
<td>3,782</td>
<td>122,053</td>
</tr>
<tr>
<td>1994</td>
<td>-5,190</td>
<td>-6,883</td>
<td>-6,601</td>
<td>75,439</td>
</tr>
<tr>
<td>1995</td>
<td>3,635</td>
<td>1,074</td>
<td>801</td>
<td>76,427</td>
</tr>
<tr>
<td>1996</td>
<td>2,665</td>
<td>1,815</td>
<td>769</td>
<td>8,824</td>
</tr>
<tr>
<td>1997</td>
<td>-7</td>
<td>2,384</td>
<td>724</td>
<td>19,110</td>
</tr>
<tr>
<td>1998</td>
<td>1,313</td>
<td>892</td>
<td>63</td>
<td>19,288</td>
</tr>
<tr>
<td>1999</td>
<td>1,024</td>
<td>2,187</td>
<td>2,070</td>
<td>122,673</td>
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</table>

**Source:** TCMB Electronic Data Delivery System (EDDS); Biçer and Yeldan (2003, 252).
The consequences of unregulated capital flows figure heavily in analyses of Turkey’s economic maladies in the 1990s. Among the main side effects were currency appreciation and an increase in real interest rates, which in turn diverted credit away from the real sector and damaged export competitiveness. Savings, trade openness, and industrial investment as well as production were all negatively correlated with short-term flows (Balkan and Yeldan 1998; Biçer and Yeldan 2003; Çimenoğlu and Yentürk 2005; Esen 2000; Yentürk 1999). While this is a particularly frustrating record of external financial liberalization, it is also important to emphasize, as seen in Table 5.3, that there was considerable volatility in the magnitude of these flows. This can be followed from the banking sector’s ability to attract short-term foreign loans, ranging from around US$9 billion in 1996 to over US$120 billion in 1993 and 1999, that is, on the eve of the two major financial shocks. Such irregularity in the amount of funds funneled into the Turkish financial system makes sense only in the context of patterns of deficit financing (Table 5.4) and developments in the banking sector (Table 5.5).

The 1990s was a decade of total fiscal collapse. Expenditures and deficit rose rapidly, especially after the 1994 shock. Evidently, the most significant factor was rocketing interest payments which consumed almost 40 percent of the public budget by the end of the decade, overtaking personnel costs that had reached record figures during the populist surge of 1989-1992. There were practical and political limits on the elasticity of public wages and salaries, though; as a result, the expenditure constraint was felt most strongly in the realm of public investments, which simply crumbled by mid-decade. And even though revenues also increased (mainly due to indirect taxation), this was well short of the scale of fiscal expansion (HM 2003, 41).
By far the most dramatic development of the 1990s from a deficit financing viewpoint was the predominance of domestic borrowing. Domestic debt stock rose somewhat slowly given the level of fiscal deterioration, catching up with foreign debt only by 1997. Yet its burden had grown astronomically over the years; in 1996, for instance, when domestic debt stock was still less than public foreign debt, it cost almost seven times as much in interest payments. Such burden is intolerable for the fiscal policymaker, and could be balanced only through further borrowing but at lower interest rates so as to stem the increase in the domestic debt stock. This indeed was the primary reason for the political resistance to dissociating fiscal from monetary policymaking in the early 1990s. Once that battle was lost in 1994, until which time security sales to banks and cash advances from the Central Bank had about equal share in domestic borrowing, the Turkish state fell fully at the mercy of financial markets for managing its deficits.

In turn, the period 1994-1999 constituted the golden years of private commercial banking. Compared to 1992, net profits of private banks doubled by 1995, and almost quadrupled by 1998. What is interesting here is that following the recovery from the 1994 shock, and until the slump of 1999, Turkish banks’ reliance on foreign funds was limited. Surprisingly, the annual average of foreign loans received between 1996 and 1998 was about one-fifth of its level during the 1991-1995 period. As such, less than one-third of security purchases during 1996-1998 were covered by capital flows. It would appear, then, that what was most profitable for private banks was to recycle government debt within the domestic system; its alternative, that is, foreign financing, both came at a hefty country risk premium and exposed banks to severe exchange rate risk.
The fiscal collapse of the Turkish state in the midst of the profit revolution in banking significantly altered the policy preferences of bureaucrats, politicians, and financial as well as non-financial interests. Once the cash advance door was closed, the Treasury had three options left: increase everyday efficiency of debt management, collude with public banks and the Central Bank over interest rates, and try to extend maturity composition by emphasizing bonds rather than T-bills. All three were tried after 1997, with little relief on the debt burden. Banks’ preferences, on the other hand, were quite different. They supported the idea of central bank independence, as this increased their share of deficit financing. They also lobbied for short term maturities in the form of T-bills, which not only ensured extra solvency and thus guarded in part against maturity mismatches vis-à-vis foreign liabilities, but had a much larger secondary market.

Crucial to banks’ position was the changing market structure of the sector. The 1990s saw a proliferation of private domestic banks, from 24 in 1989 to 38 in 1998, but also an increase in the market share of top-5 banks. Outside of this top tier, there was fierce competition to get a bigger piece of the pie, and not without good reason. Despite the predominance of a handful of public and private banks in the system, medium and smaller banks made considerable gains in market share throughout the decade. In 1991, banks that ranked 11th to 20th in assets had a combined market share of only 16 percent of the top-ten; by 1996 they had 34 percent (TBB, Annual Reports). All of these second-tier banks were comparable in size, with assets around $1 to $2 billion.15 Together, they were

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15 Banks in that tier in 1998 included, by market share: Esbank, Finansbank, Tütünbank, Dışbank, Körfezbank, İmar Bankası, İktisat Bankası, Türk Ekonomi Bankası, Etibank and Türk Ticaret Bankası. Among the top ten, banks such as Demirbank, Osmanlı Bankası, Toprakbank, and Interbank were comparable in size, as so were a few in the third tier, such as Sümerbank, Şekerbank and Egebank. Overall, there were about twenty smaller domestic banks which relied heavily on government securities for survival.
Table 5.4  
*Selected Fiscal and Debt Management Indicators (1987-1999)*

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<tbody>
<tr>
<td>Growth (GNP constant prices)</td>
<td>9.8</td>
<td>1.5</td>
<td>1.6</td>
<td>9.4</td>
<td>0.3</td>
<td>6.4</td>
<td>8.1</td>
<td>-6.1</td>
<td>8.0</td>
<td>7.1</td>
<td>8.3</td>
<td>3.9</td>
<td>-6.1</td>
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<tr>
<td>Fiscal Revenue / GNP</td>
<td>13.9</td>
<td>13.6</td>
<td>13.6</td>
<td>13.9</td>
<td>15.3</td>
<td>15.8</td>
<td>17.6</td>
<td>19.2</td>
<td>17.7</td>
<td>18.0</td>
<td>19.6</td>
<td>22.2</td>
<td>24.2</td>
</tr>
<tr>
<td>Fiscal Expenditures / GNP</td>
<td>17.4</td>
<td>16.6</td>
<td>16.9</td>
<td>17.3</td>
<td>20.5</td>
<td>20.1</td>
<td>24.3</td>
<td>23.1</td>
<td>21.8</td>
<td>26.3</td>
<td>27.2</td>
<td>29.1</td>
<td>35.9</td>
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<tr>
<td>PSBR * / GNP</td>
<td>6.08</td>
<td>4.82</td>
<td>5.33</td>
<td>7.38</td>
<td>10.34</td>
<td>10.56</td>
<td>11.71</td>
<td>7.86</td>
<td>7.20</td>
<td>8.95</td>
<td>9.76</td>
<td>9.08</td>
<td>15.13</td>
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**Composition of Fiscal Expenditures**

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<tr>
<td>Interest %</td>
<td>17.37</td>
<td>23.21</td>
<td>21.25</td>
<td>20.38</td>
<td>18.49</td>
<td>18.18</td>
<td>24.01</td>
<td>33.25</td>
<td>33.68</td>
<td>38.00</td>
<td>28.50</td>
<td>39.63</td>
<td>38.17</td>
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<tr>
<td>Foreign Debt</td>
<td>7.71</td>
<td>8.48</td>
<td>8.09</td>
<td>6.35</td>
<td>5.48</td>
<td>4.40</td>
<td>4.94</td>
<td>7.26</td>
<td>5.88</td>
<td>4.27</td>
<td>3.75</td>
<td>3.51</td>
<td>3.19</td>
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<tr>
<td>Domestic Debt</td>
<td>9.66</td>
<td>14.73</td>
<td>13.16</td>
<td>14.03</td>
<td>13.01</td>
<td>13.78</td>
<td>19.07</td>
<td>25.99</td>
<td>27.8</td>
<td>33.73</td>
<td>24.75</td>
<td>36.12</td>
<td>34.98</td>
</tr>
<tr>
<td>Personnel %</td>
<td>22.97</td>
<td>23.56</td>
<td>32.36</td>
<td>38.62</td>
<td>37.84</td>
<td>42.44</td>
<td>34.93</td>
<td>30.43</td>
<td>29.38</td>
<td>24.72</td>
<td>25.94</td>
<td>24.83</td>
<td>24.61</td>
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<tbody>
<tr>
<td>Foreign b</td>
<td>24,340</td>
<td>26,234</td>
<td>27,425</td>
<td>30,416</td>
<td>32,590</td>
<td>33,598</td>
<td>36,237</td>
<td>39,550</td>
<td>39,472</td>
<td>40,036</td>
<td>38,873</td>
<td>39,891</td>
<td>42,381</td>
</tr>
<tr>
<td>Domestic</td>
<td>20,082</td>
<td>19,885</td>
<td>19,763</td>
<td>21,939</td>
<td>23,387</td>
<td>28,255</td>
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<td>29,756</td>
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<td>Domestic Bank Advances</td>
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<td>4,852</td>
<td>5,225</td>
<td>6,945</td>
<td>12,513</td>
<td>17,839</td>
<td>21,974</td>
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<td>Consolidated (long-term)</td>
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<td>3,071</td>
<td>3,967</td>
<td>1,281</td>
<td>545</td>
<td>4,479</td>
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<td>6,241</td>
<td>7,832</td>
<td>8,019</td>
<td>10,966</td>
<td>21,775</td>
<td>29,906</td>
<td>28,246</td>
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<td>56,833</td>
<td>41,165</td>
<td>54,605</td>
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<td>46.1</td>
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<tbody>
<tr>
<td>Bonds % (&gt;1 year)</td>
<td>33</td>
<td>42</td>
<td>54</td>
<td>60</td>
<td>25</td>
<td>49</td>
<td>46</td>
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<td>74</td>
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<tr>
<td>Bills % (&lt;1 year)</td>
<td>67</td>
<td>58</td>
<td>46</td>
<td>40</td>
<td>75</td>
<td>51</td>
<td>54</td>
<td>76</td>
<td>78</td>
<td>75</td>
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<tr>
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<td>-9.4</td>
<td>-4.5</td>
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<td>13.5</td>
<td>16.4</td>
<td>21.5</td>
<td>58.1</td>
<td>28.2</td>
<td>54.8</td>
<td>41</td>
<td>38.5</td>
<td>66.5</td>
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<tr>
<td>vs. Consumer Price Index</td>
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<td>-19.6</td>
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<td>6.8</td>
<td>12.3</td>
<td>12.8</td>
<td>68.9</td>
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<td>41.4</td>
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<td>% Return on Hot Money d</td>
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<td>15.73</td>
<td>17.20</td>
<td>-2.06</td>
<td>46.84</td>
<td>32.40</td>
<td>21.50</td>
<td>29.90</td>
<td>43.55</td>
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Source: HM (2003); DIE (2002; 2003); TCMB EDDS (online); Yentürk (2003: 34). Currency conversions are based on Central Bank average buying rates.

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a PSBR = Public Sector Borrowing Requirement
b Excluding Central Bank.

c Calculated from Yentürk (2003: 34), as T-bill interest rates minus CPI and DIR.
### Table 5.5  Banking Sector: Assets, Credits, Equity, Profits, Market Structure (1987-1999) (US$ Million)

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<tbody>
<tr>
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<tr>
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<tr>
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<td>37.85</td>
<td>44.23</td>
<td>39.47</td>
<td>45.60</td>
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<td>24.32</td>
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<td>33.29</td>
<td>36.21</td>
<td>42.97</td>
<td>39.83</td>
<td>39.78</td>
<td>40.52</td>
<td>37.88</td>
<td>39.11</td>
<td>43.56</td>
<td>44.71</td>
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<tr>
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<td>2.8</td>
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<td><strong>Total Number of Banks</strong></td>
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<tr>
<td>Private Commercial (Domestic)</td>
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<td>25</td>
<td>24</td>
<td>25</td>
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<td>18</td>
<td>18</td>
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<td><strong>5-Bank Concentration (% total assets)</strong></td>
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<td>42.86</td>
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<td>40.00</td>
<td>44.93</td>
<td>45.71</td>
<td>43.28</td>
<td>47.06</td>
<td>47.83</td>
<td>50.00</td>
<td>50.67</td>
<td>38.27</td>
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Source: TBB (1998a); TBB Annual Reports (various years)

a Note that in 1999 several private commercial banks were taken over by the Savings Deposit Insurance Fund (TMSF), which explains the discrepancy in both equity and profit figures for this year.

b Net profits as percentage of average total assets.
during that year. Invariably, it was this second tier of smaller banks that were most interested in state capture through personal political connections. They were the ‘rentier capitalists’ in the full meaning of the word, aggressively seeking both financial and political rents.

It is important to note that almost all of these banks were tied to medium-size real sector groups. Bank proliferation of the 1990s should be seen in that light as well. On the one hand, extending the group activity toward the most profitable sector of the day made good business sense in its own right. On the other hand, such a move was crucial to retain the group’s overall domestic competitiveness: bank resources could be put in the service of group activities; financial profits could be used to offset industrial and commercial losses in an increasingly unstable macroeconomic environment; and bank ownership in itself was a source of market as well as political leverage. It was difficult to dissuade any major Turkish capitalist from pursuing bank ownership in the 1990s.

The problem was in the realm of credit. Özal himself was real sector-minded; he had seen how increased domestic borrowing from the mid-1980s onwards curtailed the growth of industrial credit by absorbing whatever funds Turkey’s shallow financial system could generate, and had hoped capital account liberalization would solve the problem by facilitating financial deepening, which in turn would ease the credit squeeze and in this way reinvigorate the export drive (Ersel 1996). But Özal’s predictions did not materialize. While the influx of foreign funds did lead to financial deepening, this was not matched by comparable increases in credit stock: throughout the 1980s, 42.6 percent of commercial bank assets had been allocated as credit; in the 1990s, this ratio fell to 38 percent (Özatay and Sak 2002a, 9). In fact, the period 1996-2001 witnessed a negative
correlation between financial deepening and growth (Ardıç and Damar 2006). Surprisingly, though, high real interest rates, particularly on government securities, provided a partial compensation for this problem by generating a new source of income for the industrial sector as well. Between 1985 and 1988, non-activity income of the largest 468 industrial firms constituted 24.5 percent of their profits on average; yet from 1989 to 1999, the share of non-activity income in profits, the bulk of which came from government papers, was a remarkable 64 percent (Yeldan 2001, 156). Especially after 1997, with profits falling sharply, the Turkish industry found refuge in financing public debt. In fact, without interest income from government securities, the sector would have recorded a sizeable loss in 1999. The macroeconomic imbalances of the 1990s eventually equalized the preferences of Turkish industrialists, at least for their everyday bottom line, with those of Turkish bankers at a point of continued financial rents.

The dynamic relationship between the two primary forces behind institutional reshaping in finance in the 1990s—between the innovative impulse riding on international norms and the negotiativ e impulse riding on coalition politics—can now be more explicitly formulated. It appears that increased market integration, made possible via innovative efforts earlier in the decade, gave rise to powerful domestic initiatives that not only demanded the continuation of fiscal expansion, but over time crystallized into an ironically anti-innovative alliance. By the late 1990s, the interests of bankers and industrialists, and policy preferences of bureaucrats and politicians, all converged on regulatory forbearance in banking and the persistence of the general status quo in fiscal debt management, and thus came to fundamentally diverge from evolving global norms. Surely there were disagreements on such issues as central bank independence, the weight
of different debt instruments, and the role of public banks, but a crackdown on the sector and a structural overhaul of the fiscal regime were undesirable to all these parties equally. Reinforcing this general policy attitude were the fiscal requisites of the bargains struck with popular interests, most crucially, with Turkey’s smallholder peasantry.

5.3 Agriculture: Negotiated Accommodation

The early stage of reforms in Turkey had seen the conversion of the age-old, populist-corporatist support regime in agriculture from a vehicle for income transfer to the countryside to one that repressed rural incomes in a context of fiscal austerity and demand management. Turkey’s insulated reformers in the 1980s had preserved the interventionist machine, but neutralized its redistributive consequences by policy adjustments, effectively decoupling populism and corporatism.

The intensification of domestic political competition amid opportunities for fiscal expansion after 1987 forced a reversal of this pattern. Populism and corporatism were recoupled, ensuring a full restoration of the redistributive cycle. This constituted a typical instance of negotiated accommodation. The upsurge of rural populism was rooted in a simple political logic, namely, the right-wing strategy to harness peasant support for governmental coalitions. At the same time, and much like in the 1980s, the increasingly marginal significance of agriculture for Turkey’s market integration, combined with feeble policy impulses from outside despite a changing global normative environment, resulted in relatively weak nondomestic constraints upon the subsidy regime. The discussion first examines the politics and the institutional background of populist
backpedaling in support policy, and then looks at the relative absence of international constraints in that process.

Restoration

The restoration of rural populism in Turkey after 1987 is testament to the significance of domestic politics and especially coalition efforts for institutional trajectories under high levels of political competition. Three things made restoration a feasible path. One was the availability of public funds for redistribution, thanks mainly to the medium-term sustainability of fiscal expansion, as analyzed above. Another was policymakers’ access to a well-developed but highly adaptive institutional structure capable of managing a complex system of populist transfers, which comprises the main theme of the discussion below. A third factor was the absence of credible non-domestic challenges against such a blatantly anti-neoliberal, market-distortive policy practice, which will be analyzed in the next subsection.

The return of populism to the Turkish village is a rather simple story compared to the negotiated innovation/continuous adjustments pattern in finance. Its contours can be quite legibly followed from basic support figures for the post-1987 period (Table 5.6). Here two points deserve exposition. First, rural transfers displayed considerable resilience throughout the entire period; in most crops and support items the recovery from the 1994 shock was quick and robust. Second, despite a semblance of institutional stasis, there was indeed notable dynamism on the ground.
The conversion of the support regime in the early 1980s had soured the traditionally cozy relationship between agrarian interests and Turkey’s political establishment. Thus, an important challenge for all political parties ideologically suited to carrying the rural vote, and in most regions this meant any party to the right of center, was to mend the rift between rural interests and policymaking. Ironically, it was the ANAP, the very party of neoliberal reformism, which took the first shot at restoring the redistributive functions of the support regime. The eve of the 1987 general elections marked a surge in support prices in a number of crops. This first attempt at rural populism was a well-calculated one in that it concentrated on crops more widely produced in Western and coastal regions, such as tobacco, cotton and tea, where the party saw a better chance of defeating the DYP, which had stronger support among the grain producers of Central Anatolia. Meanwhile, the highly decentralized character of the subsidy regime ensured that the fiscal burden did not fall immediately on the central budget, but was absorbed by the Central Bank and Ziraat in the short run, freeing up funds for other electoral moves such as salary increases and investment schemes. There had always been an element of indivisibility about Turkey’s redistributive machine, though, and once some parts started moving, others inevitably followed. The late 1980s saw a sharp rise in concessional credits, and the widening of the high price policy to almost all commodities. The share of central transfers in agrarian incomes, represented as a percentage PSE, more than tripled during the second ANAP government of 1987-1991 compared to the first (Table 5.6).

16 In 1987 price inflation was still around 35 percent; support prices were raised by 90 to 100 percent in tea, cotton and tobacco, but only about 25 percent in cereals.
Table 5.6  
*Agricultural Supports (1987-1999) (US$ Million)*

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<td>103.7</td>
<td>21.2</td>
<td>29.3</td>
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<td>547.8</td>
<td>909.5</td>
<td>229.6</td>
<td>147.7</td>
<td>141.0</td>
<td>189.6</td>
<td>841.1</td>
<td>840.3</td>
<td>641.7</td>
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<td>607.1</td>
<td>529.7</td>
<td>534.7</td>
<td>499.5</td>
<td>376.4</td>
<td>390.4</td>
<td>433.7</td>
<td>249.5</td>
<td>386.5</td>
<td>579.4</td>
<td>538.9</td>
<td>607.9</td>
<td>288.2</td>
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<td>765.2</td>
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<td>908.4</td>
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<td>4,537.7</td>
<td>1,917.1</td>
<td>2,073.5</td>
<td>1,937.5</td>
<td>1,955.4</td>
</tr>
<tr>
<td>Other b</td>
<td>92.2</td>
<td>126.8</td>
<td>116.7</td>
<td>209.6</td>
<td>182.4</td>
<td>246.9</td>
<td>155.9</td>
<td>587.0</td>
<td>134.9</td>
<td>269.9</td>
<td>280.5</td>
<td>318.0</td>
<td>214.2</td>
<td>457.7</td>
</tr>
<tr>
<td>Duty Losses</td>
<td>57.8</td>
<td>45.7</td>
<td>155.3</td>
<td>380.0</td>
<td>94.0</td>
<td>1,034.7</td>
<td>89.6</td>
<td>441.3</td>
<td>-</td>
<td>1,532.9</td>
<td>1,198.4</td>
<td>1,368.5</td>
<td>2,607.1</td>
<td>3,005.0</td>
</tr>
<tr>
<td>Total</td>
<td>839.3</td>
<td>1,212.0</td>
<td>1,311.0</td>
<td>1,718.0</td>
<td>1,671.0</td>
<td>2,971.0</td>
<td>2,577.0</td>
<td>2,600.0</td>
<td>1,876.0</td>
<td>6,868.0</td>
<td>4,165.0</td>
<td>5,140.0</td>
<td>6,207.0</td>
<td>6,348.0</td>
</tr>
<tr>
<td>PSE</td>
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<td>2,649.9</td>
<td>4,120.2</td>
<td>6,547.4</td>
<td>8,524.8</td>
<td>7,924.7</td>
<td>7,777.4</td>
<td>3,717.1</td>
<td>4,205.5</td>
<td>5,584.9</td>
<td>8,335.4</td>
<td>10,311.8</td>
<td>7,477.0</td>
</tr>
<tr>
<td>Percentage PSE</td>
<td>6.4 c</td>
<td>20.2</td>
<td>13.3</td>
<td>18.3</td>
<td>20.9</td>
<td>28.9</td>
<td>26.8</td>
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<td>14.1</td>
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<td>16.0</td>
<td>24.9</td>
<td>26.5</td>
<td>22.4</td>
</tr>
<tr>
<td>TSE (% GDP)</td>
<td>N/A</td>
<td>4.8</td>
<td>3.4</td>
<td>4.5</td>
<td>4.7</td>
<td>7.2</td>
<td>5.4</td>
<td>5.2</td>
<td>3.2</td>
<td>3.7</td>
<td>4.4</td>
<td>5.7</td>
<td>7.0</td>
<td>6.4</td>
</tr>
</tbody>
</table>

Source: Kasnakoğlu (1995); Yeni and Dölekoğlu (2003); OECD PSE/CSE Database (online).

- Price support figures, as calculated by Yeni and Dölekoğlu (2003), include cereals, tobacco, sugar beets and cotton only, and is therefore a conservative estimate.
- Other supports include incentive premiums, differential payments, compensations, livestock subsidies, and general service expenditures.
- As calculated by Kasnakoğlu (1995), on the basis of OECD’s Producer Subsidy Equivalent methodology at the time and not its current replacement, the Producer Subsidy Estimate methodology, although both are abbreviated as PSE. All other PSE and TSE (total support estimate) figures are taken from the OECD database. PSE measures all explicit and implicit monetary transfers to farmers; percentage PSE stands for the share of such transfers in total gross farm receipts. TSE is a broader figure, and includes PSE plus general services provided to agriculture as well as transfers from taxpayers to consumers of agricultural commodities.
The reinstatement of peasant populism by the late 1980s had the critical consequence of further shielding the pre-existing organizations of rural market governance from neoliberal policy pressures. In practice this was a major blow to the ANAP’s already sluggish privatization drive, because now not only the biggest bank in the system, Ziraat, but a number of huge non-financial SOEs such as ÇAYKUR (tea), Sugar Factories, and TEKEL (tobacco and alcohol) were also largely off the hook. Yet despite its dramatic backpedaling from orthodox neoliberalism and adoption of a generous subsidy policy, the ANAP failed to retain its hold over rural voters after 1987. Its main rival, the DYP, proved much more adept at securing electoral support in the countryside, which was of pivotal importance in its election victory in 1991.

Two factors explain the DYP’s rural success. First, it was much more aggressive in its commitment to populist redistribution. Upping the ante in the volume of transfers was its simple but effective tactic against the ANAP to reclaim rural votes. “Whatever other parties give, I will give 5,000 liras more [per kilo as support price],” declared Süleyman Demirel infamously before a crowd of Aegean tobacco farmers during his 1991 campaign. Once in power, the party also offered much more favorable credit opportunities along with frequent debt write-offs. Yet the restoration of rural populism was not simply about the amount of funds transferred to the countryside. It was also about restoring the ‘proper’ channels of populist redistribution. Thus, secondly, a significant part of the DYP’s success came from its ability to reach down to peasantry through pre-approved routes of interest intermediation, namely, through agricultural chambers and sales cooperatives. During its 8-year incumbency the ANAP never appreciated the centrality of these corporatist organizations, and thus did not sufficiently
permeate them. Even when it decided to woo the rural vote, it did so from afar and above, that is, at the marketplace and exclusively through a price policy it formulated outside the quasi-public agrobureaucracy. By contrast, building on old school center-right instincts, the DYP was well aware that populist handouts alone would not guarantee electoral loyalty in the long run. Rather, constructing a stable alliance with the peasantry required the reconstitution of the institutionally thick relations between the center and the periphery as in the pre-neoliberal era. It required not occasional deals, but the possibility of constant societal negotiation by bringing peasant representatives and rural elites back into the fold—in other words, a resurrection of the tight chain of patron-clientelism of Menderes during the 1950s and Demirel during the 1960s and 1970s. In most of the 1990s the DYP proved vastly successful in this effort, and fiercely defended its turf against any infiltrations from other parties of the right. In fact, as late as 2002, when both the ANAP and the DYP’s ratings were at free fall in opinion polls, these parties were still busy battling one another at the heart of the corporatist machine, as the DYP-aligned Board of Directors of the Union of Agricultural Chambers (TZOB) sacked the organization’s chairman over accusations of being an ANAP sympathizer.

The persistence of rural populism throughout the decade should be mainly credited to this return of old-style center-periphery politics. The mid-1990s was a time of deep fiscal trouble, but it also represented a dramatic electoral shift to the right, intensifying the party competition for rural votes. Even though the DYP was still ahead of the pack in the countryside, during the 1995 elections it was beaten by both the RP and the ANAP in popular vote and lost considerable ground to the MHP in central regions. More than ever, its electoral fortunes were tied to the continuity of rural transfers. Both
producer and total support estimates recovered quickly in 1996 and 1997, the final years of DYP rule. By then, rural populism was already deeply entrenched within an otherwise liberal policy regime. In addition, so intense was the level of political uncertainty and so imminent was the threat of a snap election after DYP’s ill-fated coalition with RP that the parties that made up the weak ANAP-DSP-DTP government of 1997 to 1999 could not risk cutting down populist side-payments. To the contrary, they tried to seize the DYP’s clientelistic networks in producer cooperatives—the ANAP mostly in the Black Sea region due to its traditional power there and the DSP in the left-leaning Thracia. Consequently, rural transfers continued after the DYP’s departure. As an excellent indicator of the quick recovery from the 1994 shock and persistence of side payments thereafter, prices received by farmers, which had trailed the GDP deflator without exception since 1980, would overtake the deflator by more than 10 percent by the late 1990s (Table 5.7). Trends in commodity PSE (Table 5.8) and the return to high volume support purchases in politically indispensable crops (Table 5.9) confirm this picture.

Table 5.7  
Quick Recovery and Continued Transfers:  
Prices Received by Farmers as Percentage of GDP Deflator (1987=100)

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<tr>
<td></td>
<td>87.71</td>
<td>97.31</td>
<td>100.97</td>
<td>105.40</td>
<td>114.39</td>
<td>111.89</td>
</tr>
</tbody>
</table>

Source: Author’s own calculations from DIE (2003).

Table 5.8  
Quick Recovery and Continued Transfers:  
Percentage PSE in Selected Commodities under DYP and After

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</thead>
<tbody>
<tr>
<td>Wheat</td>
<td>31</td>
<td>23</td>
<td>26</td>
<td>-3</td>
<td>27</td>
<td>33</td>
<td>42</td>
</tr>
<tr>
<td>Sugar</td>
<td>48</td>
<td>40</td>
<td>-16</td>
<td>28</td>
<td>32</td>
<td>56</td>
<td>61</td>
</tr>
<tr>
<td>Beef</td>
<td>39</td>
<td>46</td>
<td>32</td>
<td>58</td>
<td>54</td>
<td>40</td>
<td>48</td>
</tr>
</tbody>
</table>

Source: Çakmak, Kasnakoğlu, and Akder (1999: 65)
Table 5.9  Quick Recovery and Continued Transfers: Support Purchases by Quantity in Selected Commodities (thousand tons) (1990-1998)

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<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>Wheat</td>
<td>5,159</td>
<td>4,453</td>
<td>2,452</td>
<td>2,671</td>
<td>1,356</td>
<td>41</td>
<td>632</td>
<td>3,435</td>
<td>5,212</td>
</tr>
<tr>
<td>Sugar Beet</td>
<td>13,986</td>
<td>14,975</td>
<td>13,101</td>
<td>12,814</td>
<td>10,721</td>
<td>8,820</td>
<td>11,414</td>
<td>14,908</td>
<td>17,619</td>
</tr>
<tr>
<td>Tobacco</td>
<td>184</td>
<td>193</td>
<td>152</td>
<td>217</td>
<td>273</td>
<td>112</td>
<td>105</td>
<td>124</td>
<td>196</td>
</tr>
<tr>
<td>Cotton</td>
<td>440</td>
<td>516</td>
<td>799</td>
<td>427</td>
<td>158</td>
<td>305</td>
<td>282</td>
<td>277</td>
<td>536</td>
</tr>
</tbody>
</table>

Source: Yükseler (1999: 6)

Surely, rural populism of the 1990s was quite similar to populist episodes before 1980; in the final analysis it relied on the same actors (center-right politicians, rural elites, agrobureaucrats), mainly the same instruments (price, input and credit subsidies), and the same organizations (SOEs, cooperatives, interest associations). Nevertheless, there were also differences that are crucial to our analysis. The most striking of these was in the coalitional basis of populist redistribution, which I will explore in the next section. At the institutional level, meanwhile, policymakers tried to accommodate new policy challenges within pre-existing arrangements. This in turn entailed some degree of change and dynamism in institutional forms despite considerable continuity in the main parameters of the support regime. Three such instances of accommodation are noteworthy.

The first was the pronounced role of Ziraat. One cause of this was the natural expansion of demand for smaller credits over time. Between the late 1970s and mid-1990s, the number of local credit cooperatives increased from about 2000 to 2500. But a much more important reason was the fiscal crisis of the Turkish state. A distressed central budget forced politicians to push the financial burden of rural populism incommensurably onto Ziraat. The growth of agricultural credit stock far surpassed the recovery in PSE levels. For instance, between 1980 and 1989, the bank’s concessional loans had averaged US$230 million per year; this figure would shoot up to an annual average of US$1.6
billion between 1990 and 1999 (Yeni and Dölekoğlu 2003, 45). Indeed, by mid-decade credit subsidies became the costliest support item among direct transfers to farmers (Table 5.6). Compounding this problem was the fading of Central Bank credits to the public sector from the early 1990s onwards, which rendered agricultural SOEs and producer cooperatives dependent almost exclusively on Ziraat to finance their ever-growing subsidy bill. As a result, the duty losses of these agencies, once monetized by the Central Bank, came to threaten the bank’s balance sheet as permanent nonperforming loans; they also tended to snowball due to the astronomical interest rates of the period (Table 5.10).\(^{17}\) By the end of the decade, Ziraat was no longer an outlet to compensate for the limitations of price and input schemes, but was itself desperately in need of bailout.

\[\text{Table 5.10} \quad \textit{Duty Losses: Total SOEs vs. Agricultural SOEs (US$ Million)}\]

<table>
<thead>
<tr>
<th></th>
<th>Total SOE Duty Losses</th>
<th>Agricultural SOE Duty Losses</th>
</tr>
</thead>
<tbody>
<tr>
<td>1987</td>
<td>201.8</td>
<td>45.7</td>
</tr>
<tr>
<td>1988</td>
<td>162.1</td>
<td>155.3</td>
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<tr>
<td>1989</td>
<td>285.1</td>
<td>380.0</td>
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<tr>
<td>1990</td>
<td>441.6</td>
<td>94.0</td>
</tr>
<tr>
<td>1991</td>
<td>1,363.0</td>
<td>1,034.7</td>
</tr>
<tr>
<td>1992</td>
<td>2,243.4</td>
<td>89.6</td>
</tr>
<tr>
<td>1993</td>
<td>1,053.3</td>
<td>441.3</td>
</tr>
<tr>
<td>1994</td>
<td>624.2</td>
<td>-</td>
</tr>
<tr>
<td>1995</td>
<td>357.3</td>
<td>1,532.9</td>
</tr>
<tr>
<td>1996</td>
<td>226.2</td>
<td>1,198.4</td>
</tr>
<tr>
<td>1997</td>
<td>352.0</td>
<td>1,368.5</td>
</tr>
<tr>
<td>1998</td>
<td>1,111.1</td>
<td>2,607.1</td>
</tr>
<tr>
<td>1999</td>
<td>1,324.6</td>
<td>3,005.0</td>
</tr>
</tbody>
</table>

\textit{Source:} HM (2003); Yeni and Dölekoğlu (2003: 41)

\(^{17}\) Notice that after 1995 agricultural duty losses greatly surpass total public sector duty losses, indicating that the rest of the public sector, composed mainly of industrial enterprises, was turning a sizeable profit. In fact, a Treasury report (Yener et al. 1996: 38) gives larger figures for agricultural duty losses during the 1989-1995 period, so it is possible this was a decade-wide trend. The report also cites a much larger volume of concessional loans from Ziraat for this period.
Second, active integration of the support machine into an otherwise liberal policy regime exposed interventionist arrangements to pressures for reform. The ANAP had managed to avoid this constraint for a while, but as the fiscal cost of rural populism continued to accumulate, it became politically difficult to defend the support regime in its entirety. Particularly vulnerable were those subsectors in which state agencies encountered direct competition from private initiatives. In 1992, a few enterprises, including the Meat and Fish Organization (EBK), the Milk Industry Organization (SEK) and the Feed Industry, were jettisoned through restructuring and privatization, to be followed by the Agricultural Supply Organization (TZDK) in 1998. State monopolies over the processing of some crops such as tea and sugar were also gradually lifted, and private industry made rapid inroads into these sectors. Furthermore, after the 1994 shock, the number of commodities officially supported was reduced from 26 to 9. In addition, input subsidies, especially in fertilizers, were de-emphasized toward the end of the decade, allowing the private sector to take over. It was also decided producer cooperatives would no longer be ‘assigned’ subsidy-related tasks. Still, Turkey’s standard market price support (MPS) crops remained covered, and as a result the largest and politically most indispensable SOEs also survived, such as TMO, Tekel (tobacco), and Sugar Factories. The basic functioning and organization of cooperatives also remained intact.

Third, while some components of the subsidy regime were discarded, new ones were also introduced. Most notable among these was the use of novel fiscal instruments,

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18 Com Modities eligible for market price support after 1994 included cereals, sugar beets, and tobacco.
19 Writing a few years after the 1994 measures, Akder (1998, 140) notes that “politicians still declare support prices on products for which the sales cooperatives are responsible. [They] promise government credits to the cooperatives in return for high procurement prices.”
such as the Support and Price Stability Fund (DFIF) and the Capacity Utilization Support Fund (KKDF). The former served extensively as a revolving credit line for producer cooperatives after 1994; the latter was used in a more limited capacity to aid the livestock industry during the late 1980s. Like most extra-budgetary funds of the 1990s, their main advantage was to get around the fiscal constraint. There was a marked diversification in policy repertoire as well; new items included incentive premiums in milk and beef, differential payments in cotton and olive oil, and electricity subsidies. These new policy tools were meant not to supplant, but rather supplement primary support instruments, particularly in crops and areas in which state intervention had weakened. Taken together, though, they represented an emergent trend toward better targeted subsidies.

The crucial point here is that, in an increasingly liberal policy macro-environment, restoring the antiquated support machine to its designed function of populist redistribution required some fine-tuning and the addition of a few new parts. If one defines institutional change narrowly as change in institutional forms, then there was a great deal more change involved in the recoupling of populism and corporatism after 1987 than their decoupling through conversion during the early reform stage.\(^\text{20}\) Thus, whereas functional reorientation was sufficient for insulated accommodation (conversion) of the 1980s, negotiated accommodation (restoration) of the 1990s necessitated formal adjustments.

These fundamentally different patterns of institutional reshaping both rode on an important feature of the support regime. Turkey’s age-old arrangements of rural market governance were notorious for their unwieldiness and inefficiencies, but they proved

\(^{20}\) Needless to say, conversion was a more dramatic kind of change as it went directly against the very spirit of the support regime, although it entailed formal stasis.
surprisingly adaptive during both periods, functionally under conversion and formally under restoration. This plasticity of pre-existing institutions provides one explanation for their remarkable persistence in neoliberal times. Corporatist market governance in Turkish agriculture did not survive merely as a bizarre historical accident. To the contrary, it actively nestled in an otherwise liberalized policy environment. At the organizational level, agencies that made up the old interventionist machine made strong attempts, some quite successful, to acclimatize to capitalistic ways. Ziraat continued to lead the banking system, and proved a formidable competitor in ‘client service’; it was quick to adopt new banking instruments and technologies, and aggressive in deposit taking. Likewise, many of the SOEs and producer cooperatives, including TMO, TZDK, SEK, EBK, Tekel, Fiskobirlik (hazelnuts), and Tariş (olives, figs), improved their marketing capabilities, coming up with new brands and extending their retail network along the way. Meanwhile, at the political level, the renewed significance of patron-clientelism within the remaining web of parastate agencies made old-style corporatist co-optation an integral component of the Turkish political landscape in the 1990s. Significantly, these clientelistic networks not only co-existed with, but in part operated through the strongholds of neoliberalism. A good example was the Treasury’s General Directorate of SOEs; most rural side payments had to be disbursed through this unit, causing a great deal of strain between populist rulers and neoliberal bureaucrats who were now partly marginalized. Central politicians faced new challenges as well, such as

21 The notion of institutional and organizational plasticity is developed by Roberto Unger (e.g., Unger 2004). While Unger associates plasticity with the capacity for innovation, the cases I provide here suggest it could also be a source of institutional resilience.

22 In some cases it was the relative success, but also the cost, of such efforts that triggered the downfall of these agencies. SEK and EBK’s privatization followed an urban proliferation of the retail outlets of these organizations; TZDK’s divestiture was preceded by the introduction of a new tractor model that made the firm a viable competitor in a growing market dominated by affiliates of some of Turkey’s largest industrial conglomerates such as Çukurova and Koç.
keeping in check the increasingly powerful labor unions within state agricultural enterprises. In the end, the support regime, writ large, gained further resilience as agencies and actors on its either side learned how to operate from within new environmental realities.

*The Missing Variable: International Constraints*

The adaptability of the support regime was one important factor behind its persistence. Just as crucial was the absence of strong international incentives for change. Our typology already asserts some connection between these two factors: given weak international incentives for sectoral reorganization, policymakers will typically opt for a strategy of accommodation and seek to adapt pre-existing institutions to changing policy priorities. The preceding analysis of Turkish agriculture, spanning almost two decades thus far, provides plenty of evidence for this line of argument. But there is also something of an empirical puzzle here. Simply, in an increasingly liberalized and open economy such as Turkey’s, it is unusual for the governance of a major sector to remain so detached from outside influences for such a long time. In the fourth chapter, I have pointed out two major reasons for this absence of nondomestic incentives for change: first, the declining significance of Turkish agriculture as an exporting sector; and second, the absence of strong policy pressures in favor of sectoral reorganization, which in part stemmed from the absence of well-developed, change-oriented international norms in agriculture. Together, these factors resulted in a general sense of apathy toward the institutional shell
of agricultural supports on the part of both Turkish technocrats and international agencies that played an important role in the country’s reform opening.

Turkish agriculture’s relative insulation from nondomestic constraints took place in a different context in the 1990s, which provides a clearer illustration of how the impact of international norms for institutional pathways depends on wider patterns of market and policy internationalization. For it is in this context that we see a decisive global trend toward less interventionist norms and new, alternative designs in rural market governance; and yet, both sectoral and extra-sectoral dynamics of market integration on the one hand, and the terms of international policy exposure, on the other, shielded populist corporatism from the transformative potential of these new norms and designs.

I begin with a brief account of the normative shift in agricultural governance in the 1990s. The transition out of a state-assistance paradigm in favor of a market-liberal one was strongest in the United States, Canada and Australia (Coleman, Skogstad, and Atkinson 1997). The hallmark of this trend was the US Federal Agricultural Improvement and Reform (FAIR) Act of 1996, which replaced deficiency payments with a direct income support scheme, thereby decoupling payments from production (Orden, Paarlberg, and Roe 1999). Europe, on the other hand, took a more cautious path to the market (Skogstad 1998). The 1992 reform of the Common Agricultural Policy (CAP), generally known as MacSharry reforms, substantially reduced support prices in most commodities; but it also introduced compensatory payments to offset income losses of farmers (Ingersent, Rayner, and Hine 1998; Kay 1998). A second round of reforms approved in 1997 (Agenda 2000) reinforced the MacSharry framework with price competitiveness remaining as the primary policy goal. It also extended the scope of
support policies toward other issues such as rural development and environmental protection (Moyer and Josling 2002, ch. 9; Garzon 2006, ch. 7).

The domestic policy reforms on both sides of the Atlantic proceeded in a context of intense multilateral efforts to liberalize and harmonize the rules of international trade in agricultural goods. The culmination of these efforts was the Uruguay Round Agreement on Agriculture (URAA), which went into effect in 1995. The agreement stipulated the ‘tariffication’ of all nontariff barriers and introduced a system of ‘bound tariffs’; each country declared scheduled reductions on these bound rates over a six-year implementation period. URAA also placed a ban on new export subsidies and required cutbacks on existing ones. Most important, the agreement included reductions in what were considered trade-distorting domestic support instruments, such as market price supports, now classified as ‘amber box’ supports. In their place it encouraged a transition to ‘green box’ instruments such as direct income payments (Josling 1998, ch. 3).23

These changes in global policy trends were surely quite significant. But they had no discernible impact on Turkey’s populist-corporatist subsidy regime, for two reasons. The first was the position of Turkish agriculture in the international economy. Quite simply, because Turkey had increasingly less to gain and more to lose from market integration in agriculture, Turkish policymakers grew insensitive to the trade-driven shift in international norms. During the post-1987 period, the significance of agricultural exports continued to decrease; by the end of the 1990s, the sector contributed less than 10 percent of Turkey’s total export revenue (Table 5.11). Most instructively, this fall in

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23 A third category was ‘blue box’ supports; this included ‘amber box’-style instruments that also had the putative effect of limiting production in traditionally overproduced commodities. For their indirectly trade-enhancing and price-correcting qualities, ‘blue box’ supports are treated as ‘green’. Instruments that fall under this category, such as US deficiency payments and European compensatory payments, were not subject to reduction commitments.
Table 5.11  *Turkish Agriculture: Output and Export Shares (1980-1999)*

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<td><strong>Turkish Agriculture in Turkish Economy</strong></td>
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<tr>
<td>% Turkish GNP</td>
<td>24.2</td>
<td>22.6</td>
<td>22.7</td>
<td>21.6</td>
<td>20.3</td>
<td>19.4</td>
<td>18.8</td>
<td>17.2</td>
<td>18.3</td>
<td>16.6</td>
<td>16.3</td>
<td>16.1</td>
<td>15.8</td>
<td>14.5</td>
<td>15.3</td>
<td>14.4</td>
<td>14</td>
<td>12.7</td>
<td>13.4</td>
<td>13.4</td>
</tr>
<tr>
<td>% Turkish Exports</td>
<td>56.5</td>
<td>46.6</td>
<td>36.5</td>
<td>32.3</td>
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<td>17.4</td>
<td>19.1</td>
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<tr>
<td>Export/Output Ratio</td>
<td>2.3</td>
<td>2.1</td>
<td>1.6</td>
<td>1.5</td>
<td>1.2</td>
<td>1.1</td>
<td>1.3</td>
<td>1.0</td>
<td>1.0</td>
<td>1.2</td>
<td>0.9</td>
<td>1.0</td>
<td>0.8</td>
<td>0.7</td>
<td>0.8</td>
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<td>0.7</td>
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<tr>
<td>% World Agric. Output</td>
<td>2.21</td>
<td>2.15</td>
<td>1.86</td>
<td>1.73</td>
<td>1.62</td>
<td>1.63</td>
<td>1.65</td>
<td>1.62</td>
<td>1.52</td>
<td>1.68</td>
<td>2.22</td>
<td>2.12</td>
<td>2.25</td>
<td>2.68</td>
<td>1.81</td>
<td>2.20</td>
<td>2.38</td>
<td>2.21</td>
<td>2.96</td>
<td>2.44</td>
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<tr>
<td>% World Agric. Exports</td>
<td>0.63</td>
<td>0.90</td>
<td>1.00</td>
<td>0.95</td>
<td>0.91</td>
<td>0.89</td>
<td>0.88</td>
<td>0.84</td>
<td>0.76</td>
<td>0.80</td>
<td>0.93</td>
<td>0.79</td>
<td>0.87</td>
<td>0.85</td>
<td>0.77</td>
<td>0.82</td>
<td>0.92</td>
<td>0.89</td>
<td>0.81</td>
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<tr>
<td>Export/Output Ratio</td>
<td>0.29</td>
<td>0.42</td>
<td>0.54</td>
<td>0.55</td>
<td>0.56</td>
<td>0.55</td>
<td>0.53</td>
<td>0.52</td>
<td>0.56</td>
<td>0.45</td>
<td>0.36</td>
<td>0.44</td>
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<td>0.47</td>
<td>0.35</td>
<td>0.34</td>
<td>0.42</td>
<td>0.30</td>
<td>0.33</td>
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*Source:* DIE (2003) and author’s own calculations from WB-World Development Indicators Online and WTO-Statistics Database (online). Turkish figures are in 1987 constant TL prices; world figures are based on current US$. 

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agriculture’s export share was much faster than the decline in the sector’s income share in Turkish economy. As a result, from 1994 onwards, agriculture began to continually pull less than its weight in exports, becoming an inward-oriented sector in relative terms.\[24\] Comparisons with world agricultural trade data confirm this general trend. Turkey’s share in world agricultural exports had been historically lower than its share in world agricultural output, partly because of the country’s traditional food self-sufficiency. In time, this became a much more pronounced tendency, as what I call the ‘export/output ratio’, that is, the ratio of Turkish agriculture’s share in world exports to its share in world output, slid from an annual average of .50 in the 1980s to .37 in the 1990s.\[25\] Part of that decline could be attributed to a strong lira in much of the 1990s, which not only hampered export competitiveness but translated into larger figures in terms of share in world agricultural output, making stable levels of export share look less impressive.

The commodity composition of international trade matters just as much as its volume in terms of effects on domestic farm policy. For instance, it is often noted that agriculture’s role in Turkey’s trade performance is larger than it appears, for the sector also provides raw materials for a number of export-oriented industrial subsectors, most notably textiles (e.g. Çakmak et al. 2008, 27). This, however, is not particularly relevant for an analysis of the support regime, as market price support for cotton took consistently negative values throughout the 1990s,\[26\] indicating a classic instance of resource transfer from agriculture to industry, and through this from producers to consumers.

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\[24\] Note that agricultural imports were also minimal, typically accounting for less than 5 percent of total imports.

\[25\] For the two case periods, the ratios were .49 for 1980-1986 and .40 for 1987-1999; note that the crisis year of 1980, with a ratio of .28, greatly diminishes this ratio in the rest of the much shorter first period. The average ratio for 1981-1986 is .53.

In fact, even though Turkey’s subsidy regime relied on instruments broadly similar to those in the developed world, it was much more defensively oriented. In Turkey, price interventionism was never really put in the service of achieving export competitiveness; its ethos was confined to the protection of rural incomes against the threat of both the urban bias in domestic policymaking and highly distorted world prices at the border. As a result, crops that were internationally most competitive were also those that were least supported.27 For example, between 1996 and 1999, which represented the height of the restoration of rural populism, fruits and vegetables typically received negative support just as cotton, although they comprised almost two-thirds of Turkey’s agricultural raw commodity exports.28

By contrast, standard market price support items, such as sugar beets and wheat, were internationally uncompetitive. They also employed the largest number of peasant farmers that were most sensitive to price fluctuations. From this followed a simple state strategy of protecting against world prices as much as fiscally possible; throughout the 1990s, support prices on wheat and sugar beets were set on average 20 and 30 percent above world trade prices, respectively (Table 5.12). And most strikingly, among the top ten wheat producers in the world, Turkish farmers received the highest average prices in the 1990s (Table 5.13).

In short, patterns of international market exposure in Turkish agriculture in the 1990s did not create incentives to depart from the pre-existing regime, but validated its redistributive spirit. The effects of economy-wide patterns of integration were no different. The weakened export impetus made repression of domestic demand much less

27 For a crop-specific analysis of Turkey’s agricultural competitiveness, see Çağatay and Güzel (2003).
28 OECD Database (online); Dİ/ETÜK: Exports by Standard International Trade Classification (SITC.Rev.3) (online).
Table 5.12  World Trade Prices vs. Turkish Support Prices: Wheat and Sugar Beets (1990-99) (Current US$/ton)

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<tbody>
<tr>
<td><strong>Wheat (US$$)</strong></td>
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<td></td>
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<tr>
<td>World</td>
<td>167.2</td>
<td>137.3</td>
<td>155.9</td>
<td>149.4</td>
<td>145.4</td>
<td>178.3</td>
<td>209.4</td>
<td>173.5</td>
<td>145.6</td>
<td>130.8</td>
<td>159.3</td>
</tr>
<tr>
<td>Turkey</td>
<td>193.4</td>
<td>180.6</td>
<td>168.2</td>
<td>167.0</td>
<td>118.6</td>
<td>162.5</td>
<td>271.5</td>
<td>231.1</td>
<td>205.2</td>
<td>185.6</td>
<td>188.4</td>
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<tr>
<td><strong>Sugar Beets (US$$)</strong></td>
<td></td>
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<tr>
<td>World</td>
<td>35.7</td>
<td>24.3</td>
<td>38.0</td>
<td>40.0</td>
<td>53.8</td>
<td>42.6</td>
<td>43.8</td>
<td>52.4</td>
<td>82.1</td>
<td>70.4</td>
<td>48.3</td>
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<tr>
<td>Turkey</td>
<td>54.5</td>
<td>52.2</td>
<td>51.8</td>
<td>50.4</td>
<td>34.6</td>
<td>60.1</td>
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<td>79.8</td>
<td>67.8</td>
<td>66.4</td>
<td>57.6</td>
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<tr>
<td><strong>Turkey/World %</strong></td>
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<tr>
<td>Wheat</td>
<td>115.7</td>
<td>131.5</td>
<td>107.9</td>
<td>111.8</td>
<td>81.6</td>
<td>91.1</td>
<td>129.7</td>
<td>133.2</td>
<td>140.9</td>
<td>141.9</td>
<td>+ 18.5%</td>
</tr>
<tr>
<td>Sugar Beets</td>
<td>152.7</td>
<td>214.8</td>
<td>136.3</td>
<td>126.0</td>
<td>64.3</td>
<td>141.1</td>
<td>134.0</td>
<td>152.3</td>
<td>82.6</td>
<td>94.3</td>
<td>+ 29.8%</td>
</tr>
</tbody>
</table>

Source: Author’s own calculations from FAOSTAT-TradeSTAT (online) and DIE (2003). World trade prices are taken as the simple average of world export and import prices in current US$. Note that this differs from the OECD Index of World Prices, which often gives lower figures. Turkish price conversions are based on Central Bank average buying rates per year.

Table 5.13  Top Ten Wheat Producers in the 1990s: Production, Exports, Producer Prices (Annual Averages, 1990-1999)

<table>
<thead>
<tr>
<th></th>
<th>Production (million tons)</th>
<th>Exports (million tons)</th>
<th>Producer Price (US$/ton)</th>
</tr>
</thead>
<tbody>
<tr>
<td>China</td>
<td>106.12</td>
<td>0.03</td>
<td>142.31</td>
</tr>
<tr>
<td>United States</td>
<td>64.45</td>
<td>31.03</td>
<td>128.11</td>
</tr>
<tr>
<td>India</td>
<td>61.26</td>
<td>0.30</td>
<td>149.15</td>
</tr>
<tr>
<td>Russia</td>
<td>36.14</td>
<td>0.32</td>
<td>75.18</td>
</tr>
<tr>
<td>France</td>
<td>33.75</td>
<td>16.04</td>
<td>154.91</td>
</tr>
<tr>
<td>Canada</td>
<td>27.42</td>
<td>19.20</td>
<td>88.57</td>
</tr>
<tr>
<td>Turkey</td>
<td>19.25</td>
<td>1.11</td>
<td>180.98</td>
</tr>
<tr>
<td>Germany</td>
<td>17.60</td>
<td>4.24</td>
<td>159.72</td>
</tr>
<tr>
<td>Australia</td>
<td>17.21</td>
<td>11.53</td>
<td>142.31</td>
</tr>
<tr>
<td>Ukraine</td>
<td>16.49</td>
<td>0.91</td>
<td>72.62</td>
</tr>
</tbody>
</table>


justifiable. Further, no systemic fiscal link existed between subsidy schemes and agriculture-dependent industrial exports. Financial internationalization did not challenge Ziraat’s special position within the banking system either. In the end, there was no discernible non-domestic market constraint working against populist corporatism. In fact,
apart from the fiscal cost of generous subsidies, which had proved controllable during the 1980s, Turkish governments could not find any economic rationale for innovation; yet given the fragile coalitional balance of the decade, they had convincing political reasons to not rakishly jump on the international reform bandwagon.

Another reason for the limited effectiveness of the shift in global norms was the policy channels and terms through which they were transmitted. In the absence of constrictive IFI conditionalities, Turkish policymakers were in a better position to negotiate the terms of their exposure to these novel ideas. The only concrete constraint that emerged out of the new global policy reorientation was the country’s commitment schedules to the WTO under the URAA. In sensitive products that formed the backbone of support schemes, Turkey declared very high base rates of duty and minimum reduction commitments. This included ‘megatariffs’ in a number of commodities, bound at 195 percent in meat, 132 percent in dairy, 161 percent in cereals, 113 percent in sugar, and 150 percent in tobacco. Reduction commitments in these commodities were typically around 10 to 20 percent by 2004 cumulatively, which meant no reduction was necessary over the next few years (Çakmak 1998a, 212ff; Çakmak, Kasnaçoğlu, and Akder 1999, 81ff). Thus, as Akder (1998, 133) aptly noted, “tariff bindings [would] cause little impact on existing policies.” In terms of domestic supports as well, the relatively low volume of rural transfers around the 1994 shock made it possible for Turkey to take advantage of de minimis exemption levels toward ‘amber-box’ supports, set at 10 percent of total agricultural output for developing countries. Here again, no reduction commitment was required. Consequently, despite a changing international policy environment, populist redistribution was off the hook for the rest of the 1990s.
What further cushioned the impact of the paradigm shift in agriculture was Turkey’s special relationship with the EU, with which it signed a Customs Union (CU) agreement in 1996. The agreement did not cover agricultural commodities, however, even though nearly half of Turkey’s agricultural exports were destined for European markets. As such, the future status of agriculture within the CU quickly turned into an important consideration for debates over agricultural reform in Turkey in the latter half of the 1990s. The main issue here was the prospects of full membership that would require Turkey’s inclusion in the CAP. The country’s policy options in terms of adapting to broader normative changes under the WTO regime thus became intricately linked with European efforts in that department (Akder 1998). Arguably, this created crucial ammunition for Turkish policymakers to counteract calls for sweeping reform. The continued predominance of agricultural exceptionalism in Europe, reflected in the EU’s reluctance to fully converge on the more liberal path taken by the US in domestic supports while pushing for more heterodox reform proposals for CAP such as Agenda 2000, translated into a fundamental difference in agricultural policy alternatives between Turkey and most other developing countries, particularly those in Latin America (e.g., Jank 2004). Simply, for Turkey there was no tangible regional pressure against traditional modes of agricultural state interventionism.

In the final analysis, neither patterns of international trade nor external policy influences generated strong incentives to reform Turkey’s age-old regime of rural market governance along emergent international norms. To the contrary, both types of international exposure proved largely indifferent to the support regime, making accommodation, or ‘solutions from within’, a viable medium-term institutional strategy,
which was also politically the most desirable option. And here, just as in the 1980s, the main constraint for policymakers of the 1990s was the problem of fiscal sustainability. This in turn constituted the link between agricultural and financial regimes.

5.4 Double Redistribution: Interests, Coalitions, Institutions

Peasants and bankers were the relative winners during Turkey’s lost decade. Both collective interests benefited from intended and unintended fiscal transfers throughout the 1990s, and in return lent numerical and tactical support to the weak governmental coalitions of the decade. This section first provides the evidence for these twin transfers, which I term ‘double redistribution’, and discusses its fiscal foundations. It then places double redistribution in the context of the fortunes of other elite and mass interests and reflects on its political repercussions. The final part of the section explores the institutional implications of this unusual convergence of interests.

Winners of the Lost Decade

Evidence for double redistribution is fairly strong (Figure 5.1). “Banking on the government”, as Akçay (2003: 169) puts it, proved a very lucrative business for Turkish financiers, with private commercial banks’ annual interest income from securities steadily increasing from under half a billion in 1987 to over US$9 billion by 1999. On average, this income was about twice as big as the net profits of these banks throughout

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29 Turkish data for this period covers interest income from banks’ entire securities portfolio, and does not differentiate between various components of it. Still, a more elaborate classification adopted in 2000 indicates that about 80 to 90 percent of this income accrued from government securities (HM 2003).
the 1990s, putting into perspective their structural dependence on and vested interest in Turkey’s perpetual fiscal crisis. The decade also saw, as already discussed in relative detail, an upsurge in rural transfers, riding on the explosion of credit subsidies and high producer prices vis-à-vis both world prices and the GDP deflator. Total support estimates (TSE) averaged over 5 percent of GDP throughout the decade, more than triple the OECD average. PSE figures were also remarkably high for a developing country, especially for one in grave fiscal trouble. Turkish farmers in the 1990s were supported more than their counterparts in the United States, as much as their fellow farmers in Canada, and two-thirds as much as European farmers.30

Figure 5.1  Double Redistribution: Producer Support Estimate (PSE) vs. Private Commercial Banks' Interest Income on Securities, 1987-1999 (US$ Billions)

Source: OECD PSE/CSE Database (online); HM (2003).

30 Decade averages for PSE, showing the percentage of agricultural income accruing from direct and indirect transfers, was 22 for Turkey, 17 for the US, 23 for Canada, and 35 for the EU (OECD PSE/CSE Database, 1986-2007 [online]).
As obvious from the figure above, the classic phase of double redistribution was the period of 1994-1998. Whereas both peasants and bankers made important gains in the much of the early 1990s, the former appears to have been hard hit by the 1994 shock—although one needs to consider that private banks also recorded a significant drop in net profits that year. After 1994, however, it appears every unit increase in producer support had to be matched by an equal increase in financial rents from public indebtedness. For a few years during the mid-to-late 1990s, agricultural and financial transfers had isomorphic trajectories.

Focusing too much on the magnitude of these transfers could be somewhat misleading. These figures are certainly useful to get a sense of the general direction of the fortunes of peasants and bankers. They do not represent a precise metric, however, and there are important caveats to be made. In finance, one must bear in mind that profitability strictly depended on milking the fiscal debt. Otherwise, high inflation, macroeconomic uncertainty and intensified competition made conventional retail banking a most unrewarding activity. Banks’ interest income from loans, for example, barely covered their interest expenditures on deposits throughout the decade, and fell well short of their non-interest expenditures, primarily due to high losses incurred from foreign exchange transactions. It would thus be difficult to argue that the 1990s constituted an optimal environment for banking as we know it. In fact, the most ardent supporters of the fisco-financial status quo were smaller private banks that were also reluctant to compete with larger ones in conventional banking activities.

In agriculture, too, one must be careful while interpreting the data. PSE and TSE calculations, the current standard in agricultural economics to measure rural transfers,
heavily rely on comparisons of domestic and reference (world) prices; a variable portion of these figures denotes direct fiscal transfers to farmers. Furthermore, in the Turkish case, some fiscal items included in these calculations, such as duty losses, debt write-offs, equity injections and the financing cost of concessional loans, were severely bloated in the latter half of the 1990s due to the jumbo interest rates characteristic of this period. In other words, the high ‘overhead cost’ of running a complex redistributive machine under macroeconomic instability also counted toward subsidy figures. Add to this the traditional flaws in the implementation of the support policy, such as delays in payments to farmers toward state procurement in a high inflation economy, and figures based on standard international calculations suddenly become somewhat less representative of the real life experience of Turkish peasants.31

What double redistribution represented for fiscal trends was far more important than its absolute magnitude. Looking at these twin transfers gives us a clear picture of the locking-in of fiscal expansion in the 1990s (Figure 5.2). The determining factor here was the trajectory of rural transfers. Levels of PSE and public sector borrowing requirement (PSBR) rose and fell in unison from 1987 up until 1998, attesting to a powerful link between rural populism and fiscal expansion. This also confirms the accidental character of financial transfers. The jump in such rents after 1994, and then again after 1997, was not the result of strategic policy choices but largely a function of intensifying macroeconomic instability, which made the financing of fiscal debt progressively more

31 In terms of agricultural support figures there is also the notorious problem of reliability and consistency of data. The disorganization in public finances throughout the 1990s took its toll on figures pertaining to agricultural transfers as well, often leading to different state agencies publishing highly different data for the same transfer category. As a related official from the Treasury remarked, “At times some of these figures were reported with specific goals in mind…as [in order to fall under] blue box, rather than red box [sic.] items, for instance. (…) Exactly how much was transferred to agriculture in the past [1990s]? There exists no healthy inventory of this” (Interview, Undersecretariat of Treasury, 13 December 2004). Note that OECD figures are also based primarily on reports from the Turkish economic bureaucracy.
expensive for the state and lucrative for banks. Isomorphic rural and financial transfers after 1994 now make empirical sense as well; it was the inescapable increase in PSBR that connected the two. Here we also have good evidence for the exhaustion of this overall cycle by 1999. Simply, the sharp hike in PSBR that year could not ensure increased transfers to the countryside; instead, net transfers to financiers finally overtook the sum of all direct and indirect central transfers to farmers. One cannot overemphasize the significance of this threshold: fiscal expansion was now effectively de-linked from populist redistribution. As such, it ran out of political justification.

Figure 5.2  

Source: OECD PSE/CSE Database (online); HM (2003); TCMB EDDS (online).

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For instance, the return on Treasury bills vs. the consumer price index during the period 1987-1993 averaged less than 6 percent; between 1994 and 1994, the average was a surreal 48 percent. See Table 5.4.
Double redistribution also marked the privileged position of peasants and bankers vis-à-vis other mass and elite interests. The first phase of populist upsurge in the early 1990s embraced the totality of popular interests formerly suppressed under technocratic reformism. The coalition partners of this period, DYP and SHP, were direct successors to the main center-right and center-left ruling parties of the 1960s and 1970s. In that sense, the reinstatement of peasant and labor-based populism in a new policy context that genetically favored elite interests symbolized a concerted effort to emulate the broad social compromises of the ISI period. But in comparison to its antecedent, this emulated compromise was devoid of any economic logic of its own. More importantly, now that high levels of border protection in manufactured goods was no longer an option, it offered little incentive to industrialists to bear with rising costs of real wages. Populist redistribution of the early 1990s directly ate into industrial profits; it did not ameliorate, but exacerbated the most fundamental class division of modern times.

The 1994 shock was an important ‘correction’ for industry in that sense, putting an abrupt end to wage increases. The significant decline in real wages in the rest of the decade washed away earlier gains from labor-based populism. By contrast, prices received by farmers, perhaps an even better indicator of rural interests than PSE in the Turkish context, recorded absolute gains after a modest slump in 1994 (Figure 5.3). Thus, of the two types of populist transfers, toward wage earners on the one hand and the peasantry, on the other, the latter not only preceded the former given that rural populism had begun in 1987, but unquestionably outlived it as well. This gives peasant populism a
less conjunctural and more systemic character under high levels of political competition.

And by its very nature, it also accounted for a much larger share of Turkey’s fiscal abyss.

Figure 5.3  *Peasants vs. Workers: Prices Received by Farmers vs. Real Wages in Manufacturing (1993-1999) (1993 = 100)*

![Figure 5.3](image)

*Source:* DIÉ/TÜİK Database (online) and author’s own calculations from DIÉ (2003). Prices received by farmers as percentage of GDP deflator, assuming 1993=100. Original data takes 1987 as base point.

The implications of this wage correction for industry were readily visible from the rapid increase in net profit margins in private manufacturing after 1994 (Figure 5.4). Studies on gross profit margins, that is, markup rates, also emphasize the link between industrial profitability and wage costs in the mid-1990s.\(^{33}\) Post-1994 wage repression did not prove to be a long-term solution for industry, though, as profit margins began to decline once again after 1997. The main culprits here were macroeconomic uncertainty

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\(^{33}\) See Boratav and Yeldan (2000, 30ff), Kepenek and Yentürk (2004, 370ff), and especially Günay, Metin-Özcan, and Yeldan (2005). Markup rates, measuring the relationship between revenues and wage as well as non-wage costs, are often considered a better indicator of profitability in manufacturing, especially in oligopolistic markets. The reader should note that during the wage boom of the early 1990s markup rates continued to increase; wage increases were absorbed by both simultaneous price adjustments and declining non-wage costs as a result of currency overvaluation. It was the devaluation and economic contraction of 1994 that curtailed industry’s capacity to absorb high real wages, thus pitting wage levels directly against gross profit margins. In Figure 5.3 I use net profit margins (the ratio of net profits to revenue) to offer some comparability between private finance and manufacturing.
which created an inopportune investment climate, and currency overvaluation, which hurt competitiveness both in export markets and against cheap imports flooding the domestic market. Equally important was the insatiable appetite of the Turkish state for financial funds, crowding out industrial credits in the process: despite intense interpenetration between finance and industrial capital in large as well as small players in the system, financial deepening did not benefit the real sector. Instead, private commercial banks’ credits to assets ratio dropped substantially after 1997 (see Table 5.5). Bank profitability, however, appeared immune to these shifts.

Figure 5.4  Bankers vs. Industrialists: Net Profit Margins—Private Commercial Banks vs. Private Manufacturing Industry (1993-1999)

Overall, peasants and bankers had better fortunes than other major mass and elite interests in much of the 1990s. To suggest that double redistribution was the outcome of a socially deliberated, strategic coalition would be unrealistic, though. More accurately, it was the residue of the aborted grand compromise of the early 1990s—the consequence of staying the path that had emerged earlier in the decade, minus labor populism. It implied
a fortuitous convergence of financial and rural interests which for a while served as a de facto, pragmatic alliance, according a semblance of everyday political legitimacy to weak governments already unwilling to tackle deep-seated fiscal problems.

The fundamental differences between the interests involved in double redistribution make it both more comprehensible and extraordinary at the same time. Unlike a potential labor-industry alliance, an agro-financial coalition did not require a material compromise of any sort. Not only was there no visible tradeoff involved as far as these interests were concerned, but peasants and bankers did not even truly encounter one another in the national marketplace. Besides, double redistribution did not directly threaten other interests either. This in turn made a politically effortless coalition, constrained only by its fiscal sustainability. Its lack of a political-ideological core, meanwhile, was the main advantage of this tacit alliance; it could be ‘owned’ by any governmental coalition without much justification.

Yet double redistribution was also quite remarkable in that, in essence, it put a poorly regulated but highly internationalized banking sector in the service of extending some security to a stringently regulated and rather autarkic countryside at a time of profound macro-environmental change. It linked together the richest and the poorest segments of Turkish society, the most mobile and the least mobile factors of production in a fast-internationalizing Turkish economy, electorally most conspicuous versus least significant actors in Turkish democracy, and the most liberal and most statist forces in Turkish bureaucracy. Underlying this unusual coalition was an interesting tapestry of relations that involved the international arbitrage-seeker, his domestic counterpart in Istanbul, bureaucratic and political elites in Ankara, and finally the Anatolian peasant. All
these actors differed greatly in their specific goals, but shared the same basic means to achieve them, that is, fiscal expansionism of the Turkish state.

**Complementarity**

The twin transfers of income toward peasants and bankers were made possible by fiscal, financial and agricultural regimes in place. The predominant mode of deficit financing, the rules governing the banking sector, and age-old subsidy schemes were all equally central to the viability of double redistribution. But I will go a step further and argue that, once set in train, simultaneous rural and financial transfers also had the unintended consequence of establishing strong complementarities between these otherwise divergent institutional designs. The particular effects of fiscal, financial and agricultural arrangements were such that each created an inadvertent but continuous demand for the persistence of the other two, which in turn made all three regimes progressively resilient against brewing threats of top-down reformism.

The main pattern here was actually not too complex. It could be readily classified as what Richard Deeg labels “complementarity in the form of synergy”, or “mutually reinforcing effects of compatible incentive structures in different subsystems of an economy” (Deeg 2007, 613).34 The relationship between agricultural support schemes and the regime of public finance was perhaps the most obvious. The capacity of the support regime to transfer resources to the countryside was largely a function of the capacity of the Treasury to sustain an expansionary fiscal policy. In that sense rural populists had a marked preference for the continuity of existing mechanisms of deficit

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34 The other type Deeg (2007) mentions is complementarity in the form of supplementarity.
financing. Also, the murkier and the more convoluted were the public accounts, the easier it was for populist politicians and agrobureaucrats to run the elephantine agricultural machine. Fiscal disorganization and indiscipline provided an ideal platform to accommodate all the bells and whistles of populist corporatism.

Also obvious were the linkages between fiscal and financial regimes. Deficit financing, particularly once the central bank option drew to a close by mid-decade, depended entirely on the commercial banking system, which rendered heavy-handed regulation of the sector an unattractive choice. For banks, meanwhile, and especially for smaller ones, the continuity of the existing mode and levels of public borrowing was about the only path to survival. The system of public financial management and regulatory weaknesses in banking were mutually reinforcing.

Rural and financial transfers were the grease that oiled these relations of complementarity. Moreover, their very fiscal nature formed a not so visible but nonetheless powerful link between agricultural and financial governance. A high-performing support regime, successful at defusing distributive tensions in the countryside via increased rural transfers, exacerbated the fiscal dependence on commercial banks and in this way both fuelled rentier redistribution and contributed to bankers’ cause to escape tighter regulation. At the same time, a loosely regulated financial system riding on high open positions facilitated fiscal expansion and thereby made rural populism that much more feasible in the short run, helping to keep at bay the calls for radical reform of the subsidy regime. It is of course difficult to determine with any precision the role of complementarity in the varying degrees of institutional stability that characterized these arrangements during the classic phase of double redistribution. Still, we can safely argue,
particularly in light of empirical evidence presented so far in this section, that in much of the 1990s there were indeed increasing returns from the persistence of preexisting fiscal, financial and agricultural regimes that carried over well beyond the respective domains they governed. The stability of one regime made life unquestionably easier and more secure for the other two.

The concept of complementarity has lately received considerable attention in the comparative literature on advanced political economies. It is often employed in a somewhat positive light, alongside a family of congruent concepts such as institutional coherence, coevolution, and clustering, and typically as one potential factor behind the resilience of national configurations of capitalist governance (e.g. Amable 2000; Boyer 2004; Hall and Gingerich 2004; Höpner 2004; Crouch et al. 2005). By contrast, the interaction effects that facilitated and were in turn reinforced by double redistribution did not foster the reproduction of a sustainable mode of macro coordination. Rather, the complementarity of fiscal, financial and agricultural regimes via twin transfers represented an institutional knot that only aggravated Turkey’s economic troubles. One could defend rural side-payments on political grounds, yet even the proponents of such transfers had long criticized the inefficiencies of the support machine. In finance, the talk of reform was a fixture of the late 1990s as both the banking community and economic bureaucrats frequently voiced their concerns over fiscal and banking regimes (Cizre-Sakallıoğlu and Yeldan 2000, 503ff), but attempts at meaningful reform, such as in 1998, were quickly smothered. What double redistribution did, then, was to transform a loose, accidental alliance of disparate interests into an impenetrable anti-reformist front by creating multiple and interacting disincentives for change at the institutional level.
The costs of this relative stability were to rise exponentially in time. Nowhere could this be observed more clearly than in Ziraat, where all three regimes intersected at their worst. The critical example here was the notorious story of cotton premiums. In 1993-1994, the bank was ordered to disburse premium payments to cotton farmers on behalf of the Treasury,\textsuperscript{35} which translated into a modest duty loss of US$124 million in its balance sheet. From 1995 onwards, however, astronomical interest rates were applied on this loan, and the bank’s receivable from the Treasury rose to a stunning US$7.7 billion by 1998—representing about 40 percent of the bank’s assets (Yükseler 1999, 13). It is widely agreed that this was ultimately a cosmetic makeover by politicians to cover up the real sources of the bank’s deteriorating balances. The potential culprits here were various. Some were related to Ziraat’s genuine support tasks, namely the accumulated burden of concessional loans to cooperatives until 1996 and to individual farmers throughout the entire period. Others had nothing to do with agriculture, such as the use of bank resources to finance economic packages of the RP-DYP coalition in 1996, the bank’s perpetual losses from its ‘mission’ to drive down interest rates in Treasury auctions, and large scale corruption and other political manipulations in its loan policy, leading to a sharp increase in nonperforming loans (Özkaya et al. 2001, 20ff).

To conclude, the roots of the twin transfers could be found in the strategic policy choices of the early 1990s. But the tacit political alliance these transfers brought forth at the expense of other mass and elite interests, and the institutional entanglement they induced and later relied upon, were largely a historical accident. The extent of fiscal

\textsuperscript{35} Premium payments are a form of compensation particularly preferred in cash and industrial crops. In this system intervention prices are set low in order to allow industry and exporters to meet their raw material needs at a cost close to or below world prices; the farmers are then compensated via direct payments for the difference between this price and a hypothetical subsidized price. This is a standard ‘blue-box’ item whereby cash transfers to farmers have little direct effect, in theory, on market prices.
imbalance and financial fragility Turkish policymakers deemed permissible to sustain the makeshift coalition behind double redistribution set the natural limit of this arrangement—a limit that was to be reached, ultimately, in 1999.

5.5 Necessary Nuances

The principal feature of the 1990s for both financial and agricultural regimes was the decisive influence of domestic politics. Intense party competition lent tremendous leverage to pent-up distributive grievances of the early reform period, forcing an end to technocratic exclusivism and neoliberal austerity. In turn, the weak ruling coalitions of the 1990s took full advantage of the fiscal opportunities presented by financial internationalization in their conciliatory bids toward popular interests. When an attempted grand compromise collapsed by mid-decade, peasants and bankers found themselves as unlikely partners in a loose residual alliance that ensured simultaneous rural and financial transfers and guarded against threats of radical reform in both sectors.

International considerations, in comparison to the domestic conjuncture, had a more subdued and intermittent effect in finance, and almost none in agriculture. Signs of a paradigm shift in the global agricultural policy norms did not pose much of a challenge to the support regime; it emerged well after rural populism was fully reinstated, and its restrictive stipulations embodied in the WTO process were of minimal significance for Turkey given the production and trade profile of the sector. In finance, meanwhile, harmonization with emergent policy and institutional norms continued well into the 1990s as part of a wider strategy of financial integration. But as fiscal dependence on the
banking sector grew, so the innovative appetite of Turkish rulers faded. The latter half of the decade was marked by intense problems of rule-following and utterly failed efforts to bring public financial management and banking regulation up to par with ever-improving international standards.

Three themes in this story deserve elaboration. The first concerns the puzzle of the subdued influence of nondomestic norms upon institutional trajectories despite continued internationalization of the Turkish economy during this period. The second is about the analytical implications of complex patterns of institutional stability in these regimes. The third pertains to the value of sectoral institutional analysis for enhancing our understanding of reform politics.

(a) First of all, we must be careful not to downplay the causal significance of the international factor as a whole. For it was not a lack of internationalization, but the shift in patterns of international exposure that diminished the effects of nondomestic norms over sectoral institutions. At the level of policy pressures, the fact that Turkey was largely outside the purview of the IMF and the World Bank from the late 1980s onwards itself deserves some attention. But the impact of the change in dominant patterns of market integration is more central to our story. Had Turkey gone farther on the manufacturing export-led route rather than sliding into a foreign capital-induced, import-dependent growth path, events could have unfolded much differently in both sectors. It is of course doubtful whether this at all was a viable option for Turkey in the 1990s. So many forces worked against it, from the country’s industrial profile to an increasingly subsidy-unfriendly international trade environment, and from sovereign debt dilemmas to political
limits to demand repression. Still, a simple counterfactual exercise can help us appreciate the importance of this retreat from manufacturing export-orientation.

In finance, sticking with this previous pattern would have nudged sectoral reorganization in a decidedly different direction. The continuation of a policy of undervalued lira—and capital account opening at a later time might have been the precondition of this—would have discouraged speculative inflows by limiting opportunities for arbitrage gains. Coupled with a tight fiscal policy, this would have forced banks to rely more on traditional deposit taking and credit allocation, putting a cap on profits and thus deterring the proliferation of players in the system. All these would likely have made the proper regulation of the sector more indispensable and politically less problematic, as commercial and industrial credits would have been much more central to growth prospects and fiscal dependence on bank funds much less critical. Ironically, then, the sector itself would probably have been less integrated with international markets, but the financial regime would have been more malleable along emergent nondomestic norms. Instead, the switch to finance-driven integration at first reinforced the innovative impulse in banking and intensified non-domestic incentives for sectoral reorganization. But in time, it incalculably generated strong incentives for financial, bureaucratic, and political interests to defend the institutional status quo, inhibiting further innovation. The sector itself was increasingly internationalized, but its governance grew less responsive to normative developments abroad. Under double redistribution, market integration did not bear institutional convergence.

In agriculture, the persistence of manufacturing export-orientation would have meant the continuation of low domestic terms of trade for the sector, and through this,
quite possibly the accelerated dissolution of the peasantry. Besides, a cheap lira would have brought producer prices much closer to world prices, rendering policymaking more receptive of the trade-driven shift in global policy norms about rural market governance. These factors could have made rural populism less expedient and existing support schemes more open to change in the medium run. Functional conversion might very well have been followed by formal transformation. Instead, the switch to finance-led integration reinforced the accommodative pattern in agriculture by throwing a lifeline to redistributive state intervention. It also further insulated the sector from world markets via expensive currency, which not only curtailed export capacity but also fuelled protectionist tendencies in the face of the threat of cheap imports. Consequently, unlike in finance, in agriculture the relative absence of market integration and lack of institutional convergence went together.

The general point here is an affirmation of the earlier argument about the value of a holistic, economy-wide approach to gauging the effects of internationalization over sectoral institutions. A narrow focus on the sector in question alone, either from a policy or market integration standpoint, will provide only partial insight. Instead, we need to look at the big picture, and in a nuanced fashion sensitive to different channels of nondomestic influence.

(b) A second major implication of the preceding analysis is about institutional stability. Studies on sectoral regimes in late developers are not only relatively rare, but they almost exclusively focus on the emergence of new arrangements rather than the

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Note that the share of rural population in total population had plummeted from 55 percent in 1980 to 40 percent in 1990; after the restoration of rural populism, however, it only gradually declined, to 35 percent in 2000. In fact, in absolute terms rural population increased during the 1990s (DIE 2003).
persistence of existing ones.\(^\text{37}\) This is an understandable proclivity given how profoundly liberalizing reforms affected developing economies over the past few decades. But the experience of Turkish finance and agriculture in the 1990s suggests that accounting for relative stability is empirically just as important, and analytically just as challenging. In agriculture, we see the adaptive persistence of old institutions. Finance, on the other hand, witnessed the growing resilience of comparatively new fiscal and banking regimes against threats of substantive reforms from above. It is crucial to stress that in neither sector did institutional stability result from a simple case of bureaucratic inertia. Rather, episodes of relative continuity displayed complex patterns, in which dynamics of internationalization, intricacies of coalition building and maintenance, and unforeseeable interaction effects between configurations in different domains figured prominently.

Furthermore, in neither sector did stability take the form of pure stasis. In finance continuity and change went hand in hand. Although structural reform was avoided, on the banking side the introduction of deposit guarantees and legal limits on open positions, and on the fiscal side steps toward central bank autonomy and more active debt management, all pointed at a degree of openness to change. Nonetheless, these sporadic measures did not make up a whole: change lacked coherence and direction. As such, it was not transformative. Agriculture revealed an even more extreme case, whereby change and novelty not only accompanied but enabled continuity. Behind the survival of intense state interventionism was a remarkable process of institutional adaptation that included selective state divestiture, the use of new financing options, and the emergence of new support instruments. The core of the support regime remained intact, but for this it had to shed some of its bulk and have new elements added. Such clear evidence for the

\(^{37}\) See, for instance, Johnson (1999; 2001); Snyder (2001); Luong and Wienthal (2004); McDermott (2007).
dynamism involved in patterns of institutional stability does not just warn us against the fallacy of overly dichotomous notions of continuity and change. It also suggests that our analytical models should be capable of grasping their expectable coexistence. This in fact is an important emergent theme in institutional analysis, among both economists (Acemoglu and Robinson 2006) and political scientists (Streeck and Thelen 2005; Boas 2007). Sectoral institutions make excellent cases to trace this phenomenon. A more genuine instance of such coexistence of old and new will be presented in the next chapter, in the context of the hybridization of the support regime.

(c) Finally, a sectoral institutional outlook sharpens our understanding of the politics of economic reform. This was not sufficiently clear in the previous chapter, which examined a policy context characterized by political closure. By contrast, the centrality of institutions to the coalition efforts of the 1990s makes institutional analysis much more relevant for gathering new insight into reform politics.

At the micro level, and continuing from the previous point, much strategic action went into ensuring a degree of institutional continuity. This in effect illustrates the affinity between coalition politics and preexisting institutions, a theme I discussed briefly in the second chapter. The connection between the two is explicable even through the crudest of functionalism. Collective actors fought to preserve the arrangements that favored their economic interests, and they fared considerably better in that struggle whenever they were able join forces with other actors seeking compatible goals. Agriculture offers the classic example of this, with negotiated accommodation corresponding precisely to an intersection of coalition efforts and pre-existing institutions. The more voice peasants and agrobureaucrats gained in governing coalitions,
the better they were able to shield corporatist interventionism from technocratic threats. Among financial interests as well, a similarly protective attitude toward preexisting (although much newer) arrangements set in by mid-decade and proved instrumental in thwarting reformist attacks.

Close examination of these strategic efforts, as dictated by a sector-specific focus, helps expose some intra-coalitional dynamics that are not so visible when analysis is narrowly aimed at fleshing out the macro-policy outcomes of political realignments—the typical way in which coalition arguments are employed in the reform politics literature. Looking at the de facto alliance studied in this chapter, one cannot ignore that peasants and bankers diverged significantly in their capabilities. From the time of redemocratization, rural interests acted out of a well-placed persuasion that the continuity of the support regime was the precondition (if not the guarantor, as the early 1980s had taught) of rural side-payments; it was through this regime that the political power of the countryside had historically found economic expression. For bankers, however, this relationship was constructed in reverse order. Their political power was an aftereffect of their economic power, and their improved economic fortunes in turn descended from the contingent workings of institutional arrangements built by insulated technocrats. For this reason, the direction of the causal arrows between political power, economic power, and sectoral institutions becomes somewhat untraceable for bankers after their impromptu inclusion in ruling coalitions by mid-decade. Typical of a dominant class actor, in the case of bankers, economic might bore political influence, and vice versa. And both in turn were deployed to protect existing arrangements, but also benefited from them, and so on. By contrast, for peasants these arrows were still running largely in a single direction,
from political leverage to the support regime to economic fortunes. As a subordinate class actor, peasants could not develop the kind of economic interdependence bankers had with the state. Rather, they overrelied on political leverage and remained all too vulnerable economically, as evidenced during the 1994 shock. Not all partners were created equal.

At a macro-political level, a sectoral institutional focus helps us locate Turkey more tightly within the voluminous literature on the troublesome relationship between democracy and economic liberalization. Turkey constitutes something of an outlier case in that regard. In some countries (most famously in Chile) the quest for popular legitimacy emerged only after the first stage reforms were completed. In scores of others in Latin America and the postsocialist world, liberalization coincided with democratic opening, inspiring the debate over dual transitions. In Turkey, however, reformers relied on the temporary authoritarianism of the post-coup period to enforce a technocratic agenda, but before the first stage reforms were complete, they were sucked into a fierce competition with old school political elites. Lacking public support and stripped of authoritarian protection, ANAP fell back upon populisms of the older kind while trying to appease various private sector interests through novel policy means—an inherently contradictory pattern to be replicated by its successors.

Double redistribution was born out of the generalized failure of these efforts, but it also represented this dual political logic in its purest form. Rather than neutralize losers by bringing together potential winners under a pro-reform coalition, it rallied traditional and new style rent seekers behind an odd political alliance dedicated to reform forestalling and the reinforcement of the emergent institutional status quo. The twin sectoral transfers we have examined provide tremendous insight into some political
puzzles that have characterized Turkish liberalization. On the side of elite interests, it sheds light on the enigma of why big industry, a de facto member in distributional coalitions in most market reformers, was never genuinely incorporated into policymaking. It was politically marginalized during the 1980s, and remained in the shadow of financial interests during the 1990s. On the side of mass interests, the functional restoration of the support regime meant that Turkish populism in the 1990s differed fundamentally from Latin American neoliberal neopopulisms, where neoliberal leaders used populist political strategies to mobilize mass support for painful economic reforms. Özal during his second tenure came close to this pattern (Öniş 2004), but the absence of a solid coalition of winners and the relative weakness of party structures made plain political discourse and singular material rewards insufficient to gain the acquiescence of reform losers. What transpired instead was a return to systemic, old-style economic populism, and not political populism providing cover for economic neoliberalism.
CHAPTER SIX

REFORM AND COUNTERREFORM

The period analyzed in this chapter (2000-2007) portrays a transitional dynamic familiar from the preceding decades in that, it first saw a wave of top-down, IFI-guided reforms, to be followed by attempts to negotiate the terms of change with social forces. But domestic and international contexts were vastly different from the 1980s and the 1990s, and so were the consequences for the institutions in question. The crisis of the Turkish economy coincided with the sea change in the global development wisdom, putting institutions in both sectors on a firm path of externally-inspired innovation. Domestically, meanwhile, what replaced technocratic insulation once the crisis subsided was not a political scrimmage between myopic party elites as in the 1990s, but a strong single-party government that saw the construction of a broad-based coalition as its sole ticket to political survival. The outcome was identical types of institutional reshaping in both finance and agriculture: insulated innovation, followed by negotiated innovation.

In finance, technocratic reforms of the crisis years aimed at a synchronous recasting of fiscal and banking regimes via comprehensive legal-organizational measures. A new law overhauled the system of deficit financing while an autonomous regulatory agency disciplined banks in a most heavy-handed manner. In agriculture, a World Bank-led reform project replaced age-old subsidy instruments with a direct income support (DIS) regime, and severed the formal corporatist links between the state and farmers’ organizations. In both sectors, insulated innovation brought about novel institutions.
The rise of the Justice and Development Party (AKP) to power in late 2002 marked a transition out of this insulated path. Nevertheless, continued fiscal bottlenecks, IFI and EU anchors, increased foreign entry into the Turkish banking system, and most important, an alliance with various segments of the Turkish industry convinced the party to stick with reformist initiatives in finance. In 2005, two core new laws consolidated the emergent fiscal and banking regimes. Agriculture offered a radically different story, in which negotiation and coalition efforts resulted in a partial retreat from subsidy reform. At the first sign of economic recovery and concerned with expanding its popular base, the AKP brought back price supports and input subsidies, while also retaining elements of the novel regime and even introducing whole new ones. By mid-decade, old and new instruments came to operate side by side within a hybrid support regime—an arrangement to be carved in law in 2006. Consequently, out of the same type of reshaping, that is, negotiated innovation, vastly different institutional outcomes followed in different sectors.

The chapter is organized as follows. The first section discusses the rise of reformist initiatives from 1999 onward, paying special attention to the alliance between the IFIs and insulated technocrats, and the AKP’s efforts to partially circumvent the continued restrictions of that alliance by broadening its coalitional base. Sections two and three, which constitute the bulk of the chapter, analyze patterns of institutional innovation in finance and agriculture in relative detail. The final two sections flesh out the broader implications of the material presented. Section four offers a cross-unit comparative perspective to explore why identical types of change generated divergent institutional configurations in these sectors. The fifth section inquires what these highly varied
trajectories of reform in Turkish finance and agriculture can tell us about the practice and outcomes of the recent institutional turn in mainstream development thinking.

6.1 The Political Economy of Crisis and Reform

The recession year of 1999 was a milepost for Turkish economic governance, marking the exhaustion of foreign capital-led growth via unruly financial integration. Fears of systemic collapse muted the chorus of fiscal populists and tilted the balance of power toward IFI-endorsed, reformist technocrats. The realization of that very fear in 2000-2001 only solidified this technocratic turn, crushing the mainstream parties of the lost decade in the process. Rising out of this political vacuum and aided by rapid economic recovery, the AKP from 2003 onward managed to win the acquiescence of diverse collective interests to pursue a heterogeneous reform agenda.

The Second Coming of Technocrats

Turkish economic policymaking around the turn of the century displayed a typical affinity between technocratic reformism and normative exposure to multilateral and supranational organizations. The late 1990s had already witnessed a growing awareness within the upper echelons of the Turkish economic bureaucracy as to the ‘real sources’ of Turkey’s economic problems—hence a barrage of policy papers, design schemes, and discussion pieces on how to overcome these problems, emanating mainly from the neoliberally-oriented research departments of the Treasury, the Central Bank and, to
some extent, the DPT. The failed reform proposals of 1998 were a reflection of this rising technocratic consciousness.

Only in the face of severe trouble did Turkish politicians take heed of these reformist voices—a universal pattern indeed. The accumulated burden of persistent imbalances, compounded by the contagion of Asian and especially Russian crises, pulled Turkey into a deep recession in 1999. Fiscal deficits and interest rates soared, industrial production fell, and the economy shrank by over 6 percent. Amid protests from the real sector, a fresh coalition government, although as patchy as the ones before it, considered the downturn an opportunity to launch a reformist offensive. At the center of these efforts was an IMF-guided, exchange rate-based stabilization program, unveiled in December 1999.

The role of this IMF program in the cataclysm of 2000-2001 remains a contested topic. There is widespread agreement that a decade of unruly financial integration had already made Turkey particularly susceptible to external shocks (Cizre and Yeldan 2005; Öniş 2006b; Özkan 2005). But many also argue that flaws in the design and implementation of the disinflation program were a crucial factor in the outbreak and depth of the crisis. Some blame the IMF and its allies in Turkish bureaucracy for paying insufficient attention to the fiscal and financial weaknesses of the economy (Akyürek 2006; Çapoğlu 2004; Ghoshal 2006), others for exacerbating these very weaknesses through bad design and poor crisis management (Akyüz and Boratav 2003; Alper and Öniş 2003b; Ertuğrul and Yeldan 2003). In any event, the outcome was disastrous. Two waves of capital outflow, in November 2000 and February 2001, precipitated the deepest crisis in modern Turkish history, which recorded a 9.4 percent decline in real GDP.
One may reasonably expect such a major crisis to undermine the legitimacy of the political incumbents and trigger a shift away from the policy path in place; this was the Turkish experience in the late 1970s, and more recently in several Asian countries after 1997, Russia after 1998, and Argentina in 2001. Yet the Turkish meltdown of 2000-2001 had the opposite effect of bolstering technocratic reformism. One reason why was that technocrats directly targeted the policy and institutional status quo of the 1990s, which had been widely perceived as the root cause of the crisis. Just as crucial was the significance of powerful external anchors that gave tremendous leverage to technocratic insulation.

Consequently, the period between late 1999 and late 2002 represented an unbroken episode of extraordinary politics much like the early 1980s. It ushered in a process of top-down structural reorganization in multiple policy areas under the active guidance of the IMF and the World Bank. This in turn had the predictable outcome of shutting out reigning party elites and social forces from the making of economic policy, particularly after February 2001. In hindsight, this second incarnation of technocratic reformism had distinct advantages over its predecessor two decades earlier.

First, it rested on superior foundations in terms of both leadership and bureaucratic capacity. In the midst of the 2001 crisis, the much discredited coalition government invited a current World Bank vice-president, Kemal Derviş, to supervise a sweeping reform program. Accorded with extraordinary ministerial powers but refusing to align with any political party, Derviş emphasized an openly technocratic approach aimed at diminishing the influence of everyday politics over economic policy processes (Cizre and Yeldan 2005, 392ff). Crucially, unlike Özal who still had to answer to
generals, Derviş had a freer hand in drawing up and implementing his program. He also came from a more elite background than Özal, and was internationally better connected given his noted academic and executive credentials. Yet most important, unlike Özal, Derviş did not have to deal with a thick stratum of state-minded bureaucrats. Having to do so had forced Özal to rely on a small inner cabinet handpicked on the basis of personal connections. Rather, two decades of marketization had cultivated a new generation of liberally-oriented state elites. The core agencies of the Turkish economic bureaucracy were ready and willing for a second round of reforms.

Among these agencies, the Treasury was king—a position fortified by Derviş’s arrival. The organization had already served as a “central coordination unit” for the implementation of the post-1999 reform offensive. It certainly had the bureaucratic capability and expertise for such a task, was the natural counterpart of the IFIs as the recipient and within-state disburser of all IMF and World Bank funds, and was also important because the downward spiral that ended up in catastrophe was first and foremost fiscal in nature. Besides, it was the moral hub of neoliberal state elites and home to bureaucrats disgruntled with the irregularities of populist, corrupt politicians they had been forced to accommodate day in and day out since Çiller. Part of the affinity between Treasury technocrats and the IFIs was thus ideological in nature. As an official would put it, “We do not see the IMF staff much different than ourselves. There is a resemblance in attitude.” Derviş placed further emphasis on the agency, making it his reform headquarters. The extreme powers of the Treasury, however, came at the expense of the marginalization of executive (read, spending) ministries as well as of the Ministry of

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1 Interview, Director (Anonymous), Undersecretariat of Treasury, 13 August 2004.
2 Interview, Deputy General Director (Anonymous), Undersecretariat of Treasury, 24 August 2004.
Finance and particularly the DPT in decisionmaking. This intra-state dynamic of the early 2000s had important consequences for AKP’s more heterogeneous and pragmatic approach after 2003.

A second factor that gave an edge to the technocratic reformism of 2000-2002 over its antecedent pertains to the content of the policy advice coming from the IFIs. The crisis of the Turkish economy opened the gates to a new, more intense sort of normative influence from abroad. The IMF and the World Bank were deeply involved in Turkey’s first stage reforms in the early 1980s as well, but back then their main focus was on broad macroeconomic policy guidance, similarly to elsewhere at the time. Yet two decades later, Bank and Fund officials arrived in Turkey with elaborate blueprints for comprehensive micro-regulatory and institutional reforms. This was directly a function of the “institutional turn” in mainstream development circles and, as we shall see later, involved typical instances of “institutional monocropping” (Evans 2004; 2005). Such an institution-oriented reformism had different implications for politicians and bureaucrats. Because the goal here was not a developmental ‘course change’, as had been the case in the 1980s, but a ‘course correction’ aimed at fixing problems that had emerged on a pre-existing path, reforms of the 2000s implied a lighter political burden. At the same time, the scope of legal and organizational change required for that task was so vast that it assigned a heftier workload and much broader responsibilities to bureaucrats. An important upshot was the outbreak of intense infighting at the innards of the Turkish economic bureaucracy, pitting various reformist and traditionalist factions against one another over state reorganization. IFI engagement, both in the form of exerting direct political leverage (Miller 2006) and by according ideational coherence to the reform
process, was crucial in assuring victory for Treasury-based technocrats in most such battles.

Finally, reformers of the 2000s also had the advantage of having a second nondomestic force tipping the balance in favor of structural reform. The recognition of the country’s formal candidacy for EU membership in 1999 brought forth another powerful external anchor for Turkey in the coming decade. The EU anchor supplemented the IFI anchor in two important ways. First, it inflamed the anti-status quo sentiments in Turkish society and polity. With the rhetoric of systemic change an ever powerful political currency, it became increasingly difficult for reform skeptics to establish and act as a unified front. Second, progress toward membership requires considerable transplantation/monocropping in the spirit of the institutional turn. There are striking similarities in content as well. In fact, one might think of the acquis communautaire, the body of EU law candidate countries must adopt and implement, as a much enhanced version of the Washington and Augmented Washington Consensus reform agendas combined. There is significant overlapping between the latter and the European acquis, especially in areas concerning harmonization across property rights regimes, fiscal and financial control, corporate governance, central bank independence, anti-corruption, and social policy. That two separate external anchors urged analogous agendas of change buttressed the hand of Turkish reformers considerably. Particularly after 2003, this condition enabled the use of the more sympathetic EU card in countering opposition to the sort of reforms the IFIs too deemed essential.

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4 Consider also that, at a broader level, the Copenhagen Criteria, by emphasizing democratic governance and a functioning market economy, sets successful completion of dual transition as the main precondition for membership.
I have argued in chapter 5 that the absence of a broad-based reform coalition was one important factor in Turkey’s problematic market transition. Coalition efforts from 1987 onward generated makeshift alliances devoted to reform stalling, and rode invariably on a mix of old-school redistributive populism and new channels of collusion between political and economic elites. The AKP government of 2002-2007 was in that sense a first for Turkey.\(^5\) Below, I discuss how this new party was able to garner broad support for the continuation of the reformist path on many (but not all) policy items.

Let us start from a fundamental difference between the top-down reformism of the 1980s and that of 2000s; that is, the kind of societal insulation technocrats enjoyed. Turkey’s early reformers were insulated from popular pressures thanks to institutional barriers to electoral contestation put in place by coup leaders. Surely the crisis of 1979-1980 had undermined the collective preferences of the ISI period, but it was the prolongation of authoritarian constraints well into the mid-1980s that allowed Özal and the ANAP to deny popular interests the gains of economic recovery while remaining just as unaccountable to the private sector. By contrast, the period 1999-2002 was a time of solid democratic progress for Turkey, which could be credited first and foremost to the EU process and served as the main catalyst behind a series of legal and constitutional amendments extending political and social rights. As such, the autonomy Derviş and neoliberal bureaucrats enjoyed was the result mainly of the narrowing of policy options under economic collapse, with no formal political root. IFI conditionality was the crucial ingredient here. From late 1999 to 2002, the IMF alone poured over US$30 billion into

\(^5\) See Yavuz (2006a) and Cizre (2008) for useful collections on various dimensions of the rise of AKP.
Turkey, demanding in exchange very high levels of primary surplus, expressive of an extremely tight fiscal position. More than anything, it was this lack of fiscal funds for allocation that shut off societal interests from the policy process. This was especially the case for peasants, workers, and the small business, whose main political strategy had long been to extract concessions from the state budget. With the path to democratic contestation widened, governability in the ensuing years would depend on regaining the allegiance of at least some of these numerically indispensable groups. This could not come at the expense of an all-out retreat from the reformist path, though, given severe fiscal trauma, continued external fragility, and strong IFI conditionality. Some common ground had to be found.

Both economic and political factors worked in favor of the AKP in achieving that goal. Unlike the ANAP in the late 1980s, which had faced a similar task of reincorporating collective interests, the AKP inherited a fast recovering economy. This made it easier to sell reform compliance to the electorate while rendering the IFIs and international investors less sensitive to occasional policy slippage. In this way, the party was able to adopt a more pragmatic approach to reforms than Derviş’s technocrats. The political context was just as important. Corruption scandals and economic meltdown wiped out the political establishment of the center-right. As a result, none of the three major right-wing parties of the 1980s and the 1990s (that is, the ANAP, the DYP and the MHP) managed to secure seats in the parliament in the November 2002 elections, allowing the AKP to form the first single-party government in over a decade. Subsequent years saw the complete dissolution of the ANAP and the DYP, leaving the AKP as the uncontested party of the center-right (Açıkel 2003; Coşar and Özman 2004).
One should not confuse this relative lack of party rivalry on the right after 2002 with a categorical lack of political competition. The AKP may not have been dragged into intense party contention of the kind that had characterized the 1990s, but its precarious political position vis-à-vis the military-backed secular establishment created a very powerful incentive to continuously stretch its support base so as not to meet the same end as its predecessor, the RP. The party responded to this challenge in two ways. First, ideologically, it settled on a moderate and heterogeneous stance. Without fully rejecting the party’s Islamist roots, AKP leaders adopted a tolerant, nonbelligerent rhetoric. This move toward the center helped the party not only to avoid direct and potentially fatal confrontations with the secular establishment but to appeal to disenchanted ANAP and DYP voters with great electoral success (Mecham 2004). AKP leaders also embraced a rather colorful mélange of political and economic ideas. The party’s simultaneous commitment to social conservatism and democratic progress, market-driven development and social justice, and international openness and identity-based solidarism inspired comparisons with both European Christian Democrats (Hale 2006) and Third Way social democracy (Öniş 2006a, 210; Patton 2006, 534).

Second, the AKP’s attempts to broaden its support base were greatly aided by a powerful party organization at the local and provincial levels as well as an insatiable appetite to penetrate the bureaucracy. This less noble side story of the party’s ascendancy has so far drawn no recognizable scholarly attention. During both the 2002 and 2007 elections, the AKP relied heavily on its extensive party machinery and resorted to every clientelistic trick in the book to secure votes, including food donations and other material incentives toward poor households—hardly the work of a truly democratic movement.
The party’s strict discretionary attitude in civil service appointments is also widely known. Save for the staunchly secular Turkish military and pockets of resistance within the judiciary, political and religious orientation has become an important criterion for promotions in all quarters of the public bureaucracy. This dual and so far effective logic of actively reaching down to the masses while trying to capture the state brings the AKP closer than any other formation in recent Turkish political history to the few mass-based dominant party experiences in the periphery, such as Mexico’s PRI and Argentina’s JP. This is not so say that the party’s commitment to democracy is a mere façade. Nonetheless, it has strong hegemonic tendencies that frequently contravene its official rhetoric.

The AKP’s partly successful bid for constructing a reform coalition should be seen in this context; that is, not as a reflection of a single-minded dedication to neoliberal restructuring, but as part of a general, evolutionary strategy of political survival. Upon taking office in late 2002, the party faced a dilemma, and was forced to take a gamble. Clearly, AKP leadership had little choice but to accept the reformist constraint as given. The cost of renouncing the IMF program and stopping the restructuring process in its tracks was incalculably high. Growth had just resumed and the economy was yet too fragile to risk losing international prestige and investor confidence. Yet there was also an enormous political carrot at the end of this reform compliance stick—to win the favor of Turkey’s Istanbul-based and industrially-oriented big bourgeoisie, with whom the party had no prior organic connections. The leading association of this dominant class actor, TÜSİAD, had already taken a very active stance in the preceding years and offered immense backing not only for Derviş’s program but for the EU process and the
democratization drive as well (Öniş 2005). The day after the election, the association released a press statement, urging the AKP to honor the “founding principles of the Turkish Republic”, to adhere to the “completion of structural economic reforms” in line with the IMF program, and to commit itself to the “relevant legal and institutional reforms” on the EU membership process (TÜSIAD 2002a). In essence, big business asked the new government to refrain from pursuing a potentially destabilizing political agenda and to maintain the dual external anchors. Given the concerned tone of this statement, the AKP’s performance during its first year in office may have far exceeded the expectations of Istanbul bosses. The government did emphasize political harmony and respected both anchors on the whole, emerging as a fairly acceptable successor to Derviş. Its uncharacteristically conciliatory stance in international affairs (for instance, on the sticky issue of Cyprus) and perceived willingness to move forward with the most contentious elements of the restructuring process, such as privatization and pension reform, helped further close the ranks between the party and the dominant bourgeoisie. This of course was a mutually beneficial arrangement. Given TÜSIAD’s status as the leading civil society organization and the unmistakably secular orientation of its powerful membership, obtaining the approval of the Istanbul bourgeoisie was a rich source of political capital for the AKP. It helped quell the fears of the international community about the party’s Islamist roots and strengthened its hand against the secular establishment. For big business, meanwhile, the AKP as the most pro-EU, pro-democracy, and pro-reform mainstream party was not only the best possible choice among alternatives, but promised the very first government in over two decades of
liberalization efforts that it felt it could influence through institutionalized channels in a way proportionate to its economic might.

At the same time, even though the AKP appeared to be a worthy successor to insulated technocrats from the perspective of big business and the IFIs early on, it was not insulated at all from societal pressures. Aligning itself with an externally imposed reformist agenda, in particular when it could not comfortably fall back on its ideological roots, was a tremendous political gamble for the party. For one thing, the issue of social justice had always been at the core of the party’s message and was central to its electoral success. The AKP “was perceived as ‘hope’ by the lower strata of society” (Aydın and Dalmış 2008, 220), especially by the urban poor, to whom the program offered nothing but more agony in the short run. Furthermore, the party’s traditional support base, small- and medium-sized entrepreneurs of Anatolia, had different priorities than Istanbul capitalists. The umbrella organization of this class, the Independent Industrialists and Businessmen Association (MÜSIAD), was quite critical of the IMF program and was irritated by what it considered an overly strict fiscal and banking reform agenda, especially in the early years of AKP rule (Öniş 2006a, 220ff). Also, reform compliance soured the party’s relationship with organized labor, making it very difficult to harness the loyalty of the working class (Yıldırım 2006). Finally, there was the question of politically unignorable rural interests, whose incorporation into a reform coalition seemed unlikely, given the restrictions of the World Bank-led agricultural reform project.

The AKP’s strategy in dealing with this classic dilemma of a mass party facing mismatched priorities under harsh economic constraints has been a mixture of tactical

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6 See Öniş (1997) and Buğra (2002) for the connection between the rise of political Islam and Anatolia-based medium bourgeoisie; see also Yavuz (2006b) on the special case of AKP.
compliance, cosmetic resistance, and selective subversion. In banking regulation, for instance, the party was able to combine the demands of the IFIs and industrialists with the deep popular disgust toward rentier interests to defeat sporadic opposition from the sector. In other policy areas, and some elements of fiscal reform fall under this category, the party made a few disconcerted attempts to circumvent the reform process in order to give an impression of resistance and signal its true colors to its support base, only to capitulate to technocratic demands in the end and direct its efforts to seek out ways to appease its constituency from within emergent constraints. And yet the party showed stiff resistance to other items on the reform agenda, trying openly to undermine the process and even roll back earlier technocratic advances. The clearest example of the latter is the partial subversion of the emergent agricultural subsidy regime.

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7 Another instance of tactical compliance was in the area of labor market flexibility, where the government did pursue a policy of social dialogue through the Economic and Social Council, but eventually enacted a new Labor Law closer to the demands of the IMF and the private sector, in this case, both TÜSİAD and MÜSİAD (Süral 2005; Yıldırım 2006).

8 Battles over the social security regime offer a parallel example. From the mid-1990s onwards, Turkey’s traditional ‘pay-as-you-go’ (PAYG), defined-benefit system turned into a fiscal ‘black hole’ due to low level of contributions and very high number of primary beneficiaries. A first attempt to tackle the problem was a 1999, IMF-inspired legislation that increased the eligibility age, but some core provisions of the new law were overruled by the Constitutional Court in 2001 (Sayan 2006). Once in office, the AKP at first systematically delayed the matter, but finally succumbed to IMF pressure and passed a reform act in 2006 (Adar 2007). This new law too was quashed by the Constitutional Court, triggering another round of delays amid intense multipartite negotiations over a new draft bill with business associations and labor unions. The outcome of these negotiations was the Social Security and General Health Insurance Law (No. 5434) of April 2008 (Resmi Gazete, 8 May 2008), which involved some compromise between business and labor demands. In the process, the government managed to sneak in significant measures for harmonization across different plans that specifically favored the self-employed, a loyal constituency of the AKP.

9 Reforms regarding anticorruption are another instance of subversion. During its early years in office and under intense pressure from the IMF and the World Bank, the AKP ensured the parliamentary ratification of several international conventions regarding control of corruption, and passed a number of related laws aimed at maximizing accountability in state practice, the most important of which was the Public Procurement Law (No. 4734) that established a Public Procurement Agency to ensure transparency and fairness in public tenders (Tarhan 2005; Bedirhanoğlu 2007). But this strong legal commitment to emerging global norms on anticorruption was hardly representative of everyday political reality. Instead, old-style cronyism resurfaced quickly. The Public Procurement Law has been amended almost 50 times since its enactment in 2003 (Münir 2008). In recent years, the tiny Public Procurement Agency has been at the center of a series of allegations, mostly about favoritism toward contractors close to the government, which included several projects of the Ministry of Energy and the Ministry of Transportation. In 2006 the finance minister faced a censure motion regarding his alleged involvement in port and telecommunications
What we have in Turkey’s record of restructuring after 2003, then, is a nuanced picture that calls for an issue-specific outlook. And contrary to popular perceptions, it also strongly warns against overstating the strength and coherence of the AKP’s reform coalition. The biggest problems facing the economy were on the fiscal and financial fronts; institutional reforms regarding these regimes received the most attention from IFI-backed technocrats. At that level, the AKP was successful in transforming socially insulated initiatives into a powerful, broad-based pro-reform coalition. However, in most other areas of reform, the coalition was either quite narrow and weak, or simply nonexistent. As a reflection of this, the party was unable to directly serve the interests of its classic constituency even though it nurtured the lines of social dialogue with collective interests; and although it remained receptive to IFI demands, it also showed a lack of eagerness toward several reform elements. It is therefore difficult to explain the acquiescence of wide segments of Turkish society as well as the IFIs on the basis of the AKP’s reform performance pound per pound. With the notable exception of agriculture, a much more plausible explanation for the party’s high approval rating was the favorable outcome of the gamble AKP leaders had been forced to take. This outcome was the rapid pace and surprisingly equitable character of Turkey’s economic rebound: between 2002 and 2006, real per capita income grew by over 30 percent; and despite high rates of unemployment and with no concerted strategy of poverty reduction, about 6.5 million privatizations. Apart from these large scale scandals concerning the central authority, it is public knowledge that nepotism and clientelism is rampant in local governments as well, particularly in tenders of the AKP-run Istanbul Metropolitan Municipality. The faltered willingness of Turkey’s postcrisis reformers to combat corruption is also confirmed by international agencies. The country’s ranking in Transparency International’s Corruption Perceptions Index (CPI) deteriorated rapidly in the postcrisis period, from 50th in 2000 to 64th in 2007, whereas its CPI score fell from 3.8 in 2000 to an average of 3.5 for 2001-2007—certainly not to be expected from a country supposedly undergoing intense post-Washington Consensus-style reforms. The IFIs are well-aware of the problem; the World Bank, for instance, speaks of a need to “reignite the initial impetus of [the] administration” and complains that “[u]nfortunately, there is no obvious action plan” (World Bank 2006: 59).
people, or nearly 10 percent of the Turkish population, were lifted out of poverty.\textsuperscript{10} This encouraging economic picture has broadened AKP’s policy options considerably by providing a comfortable short-term cushion against the potential adverse effects of both reform compliance and policy slippage. As such, it gradually diminished the need for a broad and coherent coalition, and convinced a politically more confident AKP leadership to stop trying to harness the active loyalty of diverse social segments and concentrate instead on assuring simple assent, as evidenced toward the end of the party’s first term in office.

The big question here is whether this episode of fast, relatively equitable, and socially harmonious growth that followed the mending of Turkey’s broken market transition is the harbinger of a neoliberal version of the grand class compromises that had characterized the Turkish ISI in the 1960s.\textsuperscript{11} We cannot know the answer to this question yet. But a discussion of how things have turned out for Turkish peasants and bankers under intense pressures for sectoral regime change can provide some interim perspective on the likelihood of that prospect.

\textsuperscript{10} TÜİK (2007) and Turkish Statistical Institute Database (online). Both World Bank’s World Development Indicators (WDI) Database and the IMF’s World Economic Outlook (WEO) Database give comparable figures of cumulative per capita GDP growth, 33.1 percent and 32.7 percent, respectively. On the poverty front, Turkish figures indicate a sharp decline in poverty rate, from around 27 percent of the total population in 2002 to less than 18 percent in 2006. During the same period, the ratio of people living under US$4.3 a day dropped from 30 to 13 percent. Other important characteristics of this period were low inflation settling at single-digit levels for the first time since the 1960s, record levels of foreign direct investment, and an astounding overall internationalization of the economy, which saw both imports and exports almost triple in 5 years. Critics, meanwhile, point to a sticky unemployment rate of around 10 percent, galloping current account deficits, high levels of public indebtedness inherited from the 2001 crisis, and growing foreign debt of the private sector as important risk factors that threaten both the pace and the quality of growth. On a different note, there are yet no conclusive studies as to how much of this economic record could be attributed to Turkey’s domestic, post-Washington Consensus-style reforms, and how much of it is explicable through some fortuitous nondomestic factors instead, such as a favorable world financial and trade conjuncture and the EU process. A reasonable hypothesis would be one of synergy, with domestic reforms allowing Turkey to reap the benefits of advantageous external conditions, which in turn reinforce the reform process in some crucial areas.

\textsuperscript{11} Öniş (2006a, 229), for instance, links AKP’s electoral success to its “ability to move beyond class-based politics and to forge a broad cross-class coalition that incorporates both the winners and losers of neoliberal globalization.”
6.2 Finance: Permanent Reform

A fundamental problem with Turkey’s public and private finances throughout the 1980s and the 1990s was the reproduction of some pre-liberal patterns of dependency under new guises and in much more destructive ways. In the public realm, the anomaly was not that the allocation of fiscal funds remained central to the fortunes of various social groups, for this is always so under any policy regime, but that this most basic of state functions could not be carried out in a responsible fashion. Once export-oriented growth began to falter and democratic competition intensified, the challenge of brewing distributive tensions could only be met by relying on unabated fiscal expansion, although via novel channels. Herein lay the paradox of Turkey’s bank-based financial system as well. The sector was increasingly liberalized and open, and yet in time banks grew addicted to financing the deficits of the national state as the sole source of high profitability. In this way, their livelihood became tied to the willingness of Turkish governments to intervene on behalf of the losers of market transition—hence double redistribution. Consequently, despite systemic transformations in both spheres, fiscal expansion remained a most important determinant of electoral success, and public policy in other realms remained a most important determinant of bank profits.

Turkey’s post-1999 reformers were committed, first and foremost, to eliminate the much maligned incentive structures that allowed these dependencies to take root in neoliberal times: fiscal disarray and financial underregulation. Institutional reforms of this period initially relied on strong cooperation between liberal bureaucrats and IFIs. And when technocratic insulation could no longer be maintained, other initiatives
coalesced around that reformist kernel to pre-empt major subversions and help consolidate new arrangements, with enormous consequences for both realms.

*Insulated Innovation: Novel Institutions*

Our goal in this subsection is to document the top-down restructuring of fiscal and banking regimes during the height of technocratic reformism. Fiscal reforms emphasized brand new rules and operating procedures, mainly following a pattern of innovation I have identified in chapter four as ‘rule-based reorganization’. In banking, capacity building entailed a different pattern: the creation of a new stand-alone agency, which also, over time, revised and improved the rules along paths that had opened earlier. I begin with banking.

The main flaw of Turkey’s banking regime, as detailed in the previous chapter, was not so much an absence of rules as one of rule-following and enforcement. Liberalization and increased openness, along with lucrative avenues for rentier gain, encouraged the proliferation of actors in the system while at the same time exposing banks to novel, unfamiliar risk factors. Governments of the 1990s acknowledged these new risks, but fell short of utilizing cautionary mechanisms already in place. Despite clear provisions regarding credit exposure to affiliated firms, excessive levels of connected lending were widespread (Denizer et al. 2000, 12ff). There were legal limits on open positions, yet their pandemic transgression was widely ignored (Kaplan 2002). Banks did report detailed balance sheets on the basis of a uniform chart of accounts, but cosmetic touch-ups and exploitation of loopholes were common.
This underregulation of the sector had two root causes. First, bank regulators lacked bureaucratic capacity. The tasks of monitoring and supervising the system were divided between relatively small departments under the Treasury and the Central Bank—a structure inherited from the ISI days of crude financial repression. Second, and far more important, regulators lacked autonomy. Even when a bank was in open breach of rules, it was the prerogative of the minister responsible for the Treasury to order punitive action (Alper and Öniş 2002, 12-3). At that level, fears of scaring off foreign creditors, the shaky position of public banks themselves, and finally, widespread collusion between politicians and bank owners together constituted a built-in political disincentive against proper enforcement.

The Banks Law No. 4389 of June 1999 attempted to eliminate both causes of underregulation in a single move, by establishing a capacious and autonomous Banking Regulation and Supervision Agency (BDDK) (Resmi Gazete, 18 June 1999). It also set stricter lending criteria and reporting standards than the 1985 legislation that it replaced. Most crucially, it made it easier for private banks in breach of these regulations to be placed under TMSF receivership, and introduced harsh punitive measures against shareholders and bank executives. But while the new law closely mirrored technocratic sentiments that had been gaining ground for some years, its implementation was slow, reflecting the typical risk-aversiveness of governmental coalitions of the decade. The necessary impetus came only from outside, in the context of the IMF program. Turkey’s Letter of Intent to the Fund, dated 9 December 1999, cited the full operation of the BDDK by end-August 2000 as a structural performance criterion. Less than two weeks

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later, and on the very day the first installment of the stand-by credit was approved (December 22), five insolvent banks were brought under TMSF management.\textsuperscript{12}

The creation of the new banking agency itself was a relatively smooth process. Some 30 personnel each were transferred from relevant departments of the Treasury and the Central Bank. With recruits from outside the bureaucracy, the number of specialist personnel quickly topped 100.\textsuperscript{13} Problems emerged, though, in the appointment of the agency’s chairman and the governing board due mainly to intense turf wars between coalition partners. Nonetheless, with program benchmarks hanging over the government, a resolution was found, and the agency began its operations in August 2000. Its first important move was to transfer two more banks, Etibank and Bank Kapital, to the TMSF in late October. Shortly thereafter, the agency warned all banks to quickly reduce their open positions to conform to legal limits by year end.

Given that banks had known for over a year that a more stringent regulatory environment was dawning, it is surprising many were caught so badly off guard. The problem here was one of reckless greed compounded by an underestimation of regulators’ determination to clean up the system. In a context of real appreciation of the lira under currency peg, a domestic lending boom, declining but still generous interest rates, and finally investor optimism thanks to the government’s broad commitment to the IMF program, private banks enjoyed a rapid influx of foreign capital. Many in turn relied on these short-term foreign funds to aggressively buy into lira-denominated government papers with much longer maturities so as to maximize arbitrage gains before a projected

\textsuperscript{12} These banks were Egebank, Yurtbank, Sümerbank, Esbank and Yaşarbank. By comparison, only three banks were taken over between 1997 and 1999 (Türk Ticaret, Bank Ekspres, and Interbank), but these cases were triggered mainly by large-scale corruption scandals.

\textsuperscript{13} Interview, BDDK (Anonymous Director), 30 December 2004.
fall in public yields. In this way, in less than a year into the IMF program, the Turkish banking system grew much more vulnerable to capital flight. Record-high open positions by early fall indicated unusually severe currency and maturity mismatches.

Much criticism has been leveled against the IMF and the Turkish authorities both for failing to size up the gravity of this growing systemic risk and for mismanaging the crisis itself. But a more specific line of attack concerned the BDDK. Accustomed to two decades of laxity, banks did not anticipate too radical a reversal in regulatory attitude. The agency proved them wrong. Its swift move against problem banks and resolute enforcement of the new law reportedly caused “profound anxiety in the sector” (Tunç 2003, 45). The apogee of this uncompromising posture was the prosecution of ex-owners of banks placed under receivership. Deemed untouchable just months before, many such figures were now jailed on charges of fraud and even organized crime (Akçay 2003, 181). On the flipside, this meant the agency was every bit as Turkey’s technocratic reformers expected, starting life with a powerful display of both bureaucratic capacity and political autonomy.

14 In mid-November, a highly leveraged mid-size market maker, Demirbank, faced insolveney. Cut off from the interbank market, it began dumping its massive securities portfolio at a loss, which eroded whatever little confidence left in the system and triggered the first wave of capital reversal. Many observers find the Central Bank’s stubborn defense of the currency peg and inconsistent approach in injecting liquidity into the system during these early days of the crisis as one aggravating factor; the IMF is also blamed variously for its poor diagnosis of the problems of the sector, playing along with Turkish authorities rather than taking a more proactive role, and simply for not extending sufficient funds when most needed (Akyüz and Boratav 2003; Alper and Öniş 2003b; Öniş 2003; Miller 2006).

15 The highest profile case was Murat Demirel, the nephew of Süleyman Demirel, easily the most dominant figure in Turkish politics in postwar decades; nephew Demirel was jailed in October 2000 on charges of fraud and embezzlement related to Egebank. Not all prosecuted were involved in such transparent personalistic corruption, though. Case in point was Ali Balkaner, the ex-owner of one of the most troubled of all banks transferred to the TMSF, Yurtbank. In this instance, the problem was not the direct siphoning of bank resources, but the squandering of the bank’s capital in bad investment deals, especially in the real estate market. Regulators believe at most one percent of the bank’s loss had found its way into Balkaner’s pocket (Interview, BDDK (anonymous), 23 December 2004). Yurtbank in that sense was a classic case of a real sector group having jumped the bank ownership bandwagon in the alluring 1990s primarily to expand and support non-financial group operations.
The first wave of capital outflow in November 2000 was caused by international investors’ growing misgivings about the open positions and associated exchange rate risks faced by private banks. In contrast, what triggered the February 2001 crisis were the liquidity problems of public banks, which, as discovered by the agency, carried severe interest rate risks due to gargantuan duty losses in their balance sheets (Özatay and Sak 2002b). This revelation led to widespread perceptions that Turkey’s sizeable sovereign debt might not be as sustainable as the IMF and Turkish authorities wanted to believe. The ensuing mass exit was to pull the plug on an already comatose financial system.

The meltdown exposed the novel agency to a much different agenda. In less than six months after starting operations, it faced not merely a task of rule enforcement but a much more strenuous one of rehabilitating the entire sector. A comprehensive “Banking Sector Restructuring Program” was announced in May 2001, built on four pillars: restructuring of public banks; restructuring and resolution of banks taken over by the TMSF; strengthening of the private commercial banking system; and improving the regulatory, monitoring and the supervisory framework (BDDK 2001b).

The urgent chore was to put out the fire. In June, the BDDK negotiated a debt swap between the Treasury and private banks that replaced their lira-denominated bonds stocks with FX-denominated ones, thus effectively resolving the problem of open positions. Around the same time, the devastated balance sheets of public banks were repaired via massive capital injections in the form of Treasury bills. The agency also merged Emlak, the fourth public bank in the system, with Ziraat, appointed a common board of directors for the remaining three public banks (now Ziraat, Halk and Vakıfbank).

16 BDDK (2001a; 2001b; 2002; 2003a; and Banking Sector Restructuring Program Progress Reports). See also Akçay (2003, 182ff); Steinherr, Tükel, and Üçer (2004, 5ff); Pazarbaşıoğlu (2005, 162-4); Dinçer (2006, 97ff); and Tükel, Üçer, and van Rijckeghem (2008, 282ff) for standard accounts of the program.
only), and revoked all regulations allowing duty losses. This was followed, in July, by the
takeover of five small private banks.\textsuperscript{17} The public financial burden of this system rescue
operation was enormous: some US$22 billion for fixing the public banks, and another
US$16 billion for private banks transferred to the TMSF since 1999.\textsuperscript{18}

Having eliminated the immediate risk factors in the sector, the BDDK turned its
attention to the equity structures of private banks and the regulatory environment. The
“Bank Capital Strengthening Program”, announced in February 2002, called for an
emergency triple audit (two by independent auditors, one by the agency) of all banks in
the system. Capital adequacy standards were revised both to include a market risk
component that reflected the Basel I update of 1996 and a consolidated framework
following the emergent EU norm, forcing most banks to raise their paid-up capital.
Around the same time, an initiative was launched to address the problem of non-
performing loans (NPL). Dubbed the “Istanbul Approach”, it sought to restructure the
outstanding obligations of real sector firms adversely affected by the 2001 crisis.\textsuperscript{19} In
addition, the agency pushed forward a chain of new rules concerning balance sheets,
internal accounting standards, and disclosure procedures. These measures aimed at
institutionalizing maximum transparency within the sector in line with evolving
international norms of prudential regulation. The mutual obligations of the agency and
the actors in the system were also detailed out, enabling a continuous flow of information
to bolster the quality of monitoring and supervision (BDDK 2003b, 60ff).

\textsuperscript{17} These banks were Tari\phi\textsuperscript{\textoe} bank, Bayindirbank, Kentbank, EGSBank and Sitebank. Earlier, Ulusal Bank was
taken over in February, and Iktisat Bankasi in March.
\textsuperscript{18} It is calculated that the total cost of the banking crisis to the Turkish economy was in the order of US$53
billion, or about 36 percent of the Turkish GDP in 2001 (Steinherr, T\textlivl, and \textlivl\textcute 2004, 5).
\textsuperscript{19} As of September 2003, some 200 large firms along with about 100 small and medium-size enterprises
benefited from the program; the total amount restructured was over $5 billion (BDDK 2003b, 50).
A striking feature of this episode of postcrisis restructuring was that it was by and large a top-down affair. As in the early 1980s, banks were excluded from all major policy decisions regarding the governance of the sector. The Turkish Banks Association (TBB), although founded upon an alliance of public banks and the largest private banks, was furious. Ersin Özince, the chairman of the Association and head of İş Bankası, a top private bank with exceptional historic links to the state, felt that private banks were singled out for summary punishment. He called for leniency, warning the government during a BDDK panel meeting in July 2002 that the agency’s heavy-handed approach would jeopardize economic recovery at large:

While the public sector and [real sector] firms are at the start of their reform process, the demand to complete this private bank-centered process in the banking sector in such a short period of time will only choke credit markets. The clog in the banking system, the decline in credit supply will…delay the resumption of economic growth and prevent innovations…in the industrial sector necessary to attain sustainable growth (Özince 2002, translation mine).

A couple of weeks later, and seeing that his remarks had fallen on deaf ears, Özince went further and blamed the critics of the sector with “sadomasochism”.

The growing disenchantment of bankers with the program in the summer of 2002 was the result partly of the events surrounding the takeover of Pamukbank in mid-June. Although Pamukbank’s troubles were widely known, many considered it too big for the BBDK to take down. It was the seventh largest bank in the system and fifth among private banks; on top, it was owned by Turkey’s third largest conglomerate, the Çukurova

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20 About the only exception was the Istanbul Approach mentioned above, which nonetheless constituted a minor and temporary part of the process.

21 Recall that in the late 1990s TBB had pursued a calculating tactic. On the one hand the association was well aware of the growing risks in the sector and frequently expressed the need for tighter regulation; on the other hand it refrained from lending active support to any measures toward strengthening the regulatory environment and stood by as bureaucratic initiatives to that effect failed one after another under relentless attacks from politically-connected smaller banks.

Group. The decision came days after Çukurova’s attempt to salvage the bank by filing a proposal to merge it with the other group bank, Yapı Kredi, the second largest private player. By taking over Pamukbank the BDDK not only refused this merger, which it believed would have destabilized the system, but gained control over Yapı Kredi as well, since many Pamukbank shareholders and executives whose banking licenses were now revoked also happened to be affiliated with Yapı Kredi—among them, Mehmet Emin Karamehmet, head of Çukurova. In their place, the BDDK appointed public managers. This tricky operation was testament to the political autonomy and determination of the new Agency, and it was greeted by the IMF with great enthusiasm. Meanwhile, the industry-controlled TÜSİAD, which had lent unconditional support to Derviş, chose to remain silent on the issue. A few days later, Özince resigned from TÜSİAD’s Board of Directors, where he had represented the banking community. The Pamukbank affair helped expose the deepening cleavages between financial and dominant real sector interests over the recovery program.

Bankers were not unjustified in complaining about the comparatively slow pace of restructuring in other areas, in particular the public sector. The trajectory of the fiscal regime was proof of this. The 2000 program promised fiscal discipline in the form of a sizeable primary surplus (3.7 percent of the GDP), but it pursued a pragmatic approach to that end that emphasized the usual expenditure cuts and tax increases rather than

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23 With two major banks in the system, Çukurova had best of both worlds, using Pamukbank to support the group’s industrial activities by excessive connected lending while the much bigger Yapı Kredi remained the group’s profit-oriented flagship retail bank. According to BDDK, by the time of takeover Pamukbank had a capital shortage of US$2 billion. If the merger had gone through the new bank would have become the largest private bank in the system and the second largest player overall, after Ziraat.

24 “IMF’den BDDK Kararlarına Destek,” Hürriyet, June 20, 2002. In fact, the government delayed its letter of intent to the IMF for the upcoming tranche release until the operation was complete.
comprehensive reforms (Emil and Yılmaz 2003, 43ff). The government’s first Letter of Intent to the IMF in December 1999 conceded this point openly:

Many of the measures in the 2000 fiscal package are of a one-off nature. This has been necessary given the magnitude of the adjustment with respect to the trend. Further measures of a permanent nature will be introduced in 2001, when we also expect a stronger contribution from the structural reforms…

About the only change that could be considered institutional in nature before the 2001 crisis was the elimination of most extra-budgetary funds (EBFs), a move that essentially corrected a contingent anomaly.

With the February meltdown, the institutional reform of ‘state finances’, writ large, picked up steam. The battle was fought on three fronts that concerned three core branches of the economic bureaucracy: central bank independence, which obviously was about the TCMB; the reorganization of debt management, which was a Treasury-centered initiative; and reform of the public finance regime, which mainly targeted the Ministry of Finance. The first two, discussed below, were relatively straightforward and proved achievable under technocratic insulation. The third was organizationally (and culturally) much more demanding and time-consuming; thus, even though there was a comprehensive plan in works, implementation would have to take place under the more negotiative AKP rule. It is therefore analyzed separately in the next subsection.

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26 As discussed in the fourth chapter, EBFs were special allowance mechanisms devised in the 1980s by neoliberal reformers to circumvent the operational rigidities of Turkish public finance. They mushroomed very quickly and many reached monstrous proportions during the expansionary 1990s, turning into a major nuisance for fiscal planners. During the period 1990-1994, for instance, the Treasury’s disbursements toward EBFs averaged about US$8.5 billion per year, even though most indirect taxes also passed through the EBF system (HM 2003). With little accountability to central authority, EBFs’ operations were hard to track down. From 1996 onwards most EBFs were brought into the central budget. But the term itself survived, with two new classifications, budgetary funds vs. nonbudgetary funds comprising two parts of the EBF system. By 1999, there were approximately 75 EBFs, some inactive. The liquidation of EBFs began in May 2000 with Law No. 4568, and continued until end-2001, at which point 69 funds were eliminated. 6 funds, deemed strategically important, remained: Support and Price Stability Fund, Social Aid and Solidarity Incentive Fund, Defense Industry Support Fund, Promotion and Publicity Fund, Savings Deposit Insurance Fund, and Privatization Fund.
In the late 1990s, Turkey was already moving toward dissociating monetary from fiscal policy, the main premise behind the idea of central bank independence, which had gained normative acceptance among inflation-conscious neoliberal economists since the late 1980s (e.g., Alesina 1988). A 1995 legislation had shut the door on short-term Central Bank advances to the Treasury, and the practice was completely abandoned by 1997. While this certainly was an important step, it did not cure the problem of systemic collusion between the Treasury, Central Bank and public banks in the financing of fiscal deficits, specifically in the process of debt issuance. The bank’s interest rate policy, for instance, continued to be heavily influenced by the Treasury’s borrowing schedule.

Central Bank independence is the kind of institutional reform that is seldom demanding from a legal-organizational standpoint, and yet it has the potential to deliver considerable and immediate international prestige (Maxfield 1997). No wonder, then, that it was the first item on the list of Turkey’s postcrisis reformers. In April 2001, Law No. 4651 amended the original Central Bank Law No. 1211, and established the full autonomy of the bank (Resmi Gazete, 25 April 2001). The bank’s primary objective was now redefined as the provision and maintenance of price stability, for which it had the sole authority over the monetary policy and the exchange rate regime. The 4th article of the act stipulated that “[t]he Bank shall enjoy absolute autonomy in exercising the powers and carrying out the duties granted by this Law” (emphasis added). To strengthen this principle, the new law also set up a Monetary Policy Committee within which the Treasury had no voting rights. Furthermore, the law explicitly revoked previous

27 Assuming, of course, that there is an institutionally well-endowed Central Bank in operation, which certainly was the case for Turkey. One also needs to bear in mind that the exchange-rate based disinflation program of 2000 had already put CBRT in a special, relatively autonomous position, and the Bank had exercised that autonomy in its much criticized strategy to fiercely defend the peg up until the February meltdown.
legislations on advances to the Treasury and forbid any bank loans to public institutions (articles 50 and 51). Its purpose, then, was not only to sever the organizational linkages between monetary decision-making and the regime of public finance, but pre-empt their future re-emergence as much as possible.

The reorganization of debt management was a slightly more difficult item, but it could not be delayed given the gravity of the situation. The crisis tore asunder all presumptions about debt sustainability. With skyrocketing real interest rates, the immense burden of bailing out the banking system, and a shrinking national income, Turkey’s sovereign debt to GDP ratio jumped by almost two-thirds in a single year, from a manageable 57 percent in 2000 to an unprecedented 92 percent in 2001, and at much shorter term maturities as well. Conditions called for radical action, and reformers’ response was the Law on the Regulation of Public Finance and Debt Management (No. 4749), enacted in March 2002. The new act was revolutionary in its redefinition of the fundamentals of public borrowing as well as debt management (Resmi Gazete, 28 March 2002). Its main provisions centered on principles of discipline, accountability, and transparency, and its language borrowed a great deal from the New Public Management (NPM) approach briefly introduced in the second chapter. First, all state and quasi-state organizations were now subject to a single, unifying framework of borrowing, bringing all public debt into the budget. Second, the law set strict limits to total borrowing, based on the projected incomes and expenditures in the annual Budget Law. Third, it re-regulated the operating principles and restricted the scope of Treasury-guaranteed borrowing by any public organization. Fourth, it set the principles for cash, debt and risk management and established a risk management unit (what Treasury officials call a
‘middle office’) under the General Directorate of Public Finance. The law also made it mandatory for the Treasury to publish comprehensive quarterly reports on debt management.

Both banking reform, whereby the attainment of regulatory capacity rested on the creation of a novel public agency, and central bank and debt management reforms, whereby rules and relations were redrawn in a context of organizational continuity, constituted clear instances of insulated innovation. In both, change-oriented, liberally-minded technocratic teams displayed a remarkable capacity to reform institutional domains in accordance with evolving international norms. Problems were well-known, and solutions had been widely discussed for some time, as was evident from the defeated financial sector reform bill of 1998 in banking, and various policy papers in circulation on public finance (e.g., Atiyas et al. 1999). In both fiscal and financial domains, international market and policy incentives for reorganization played a crucial role. At the level of market integration, there is great truth in the popular argument that much of Turkey’s economic misfortunes in the 1990s were related to its unruly financial internationalization (Öniş and Aysan 2000; Öniş 2006b; Cizre and Yeldan 2005). Given this sour outcome, making the playing field safer for existing actors was the proximate driver of institutional overhaul. Yet there was also a longer term motive behind this will to transform. Public overseers not only wanted to fix the problems of the day. They also desired to change the rules and their enforcement in such a way as to open the door to entirely new game combinations: a banking sector not driven by a multitude of small actors wrestling one another for the parasitic milking of fiscal sins, but by larger and more serious domestic and international players that turn sustained profits from financing
a stable, well-functioning, globalized market economy; a fiscal environment marked not by layer upon layer of political patronage and rent distribution whereby bloated expenditures are clumsily swept under a nebulous carpet of public accounts, but one in which funds are accountably put in the service of a narrow, well-targeted set of long-term goals in an increasingly open economic sphere. Put crudely, the deeper promise of institutional reform was to make finance-led globalization work.

At a policy level, the IFIs had been true believers in that deeper promise since the mid-1990s, and their support and pressure were crucial for Turkey’s liberal bureaucrats to carry through the reform process. Here, the usual division of labor between the IMF and the World Bank applied. The fund was most influential in assuring reform compliance by twisting the arms of reluctant politicians at the right moments. The bank, on the other hand, worked closely with bureaucrats and offered plenty of guidance and technical assistance. Its renewed and much expanded role in Turkish political economy (Table 6.1) is therefore more important for our analysis.

Fisco-financial transformation constituted a special, particularly effective instance of World Bank influence within a pattern of insulated innovation, for two reasons. First, on the innovation side, bank assistance and strategy were built on the rapid consolidation of coherent, novel global norms in finance—a clear advantage over some other areas of reform. In the 1990s, a near-consensus emerged among neoliberal economists on the virtues of central bank independence (e.g. Maxfield 1997; Forder 2005; Polillo and Guillén 2005). In banking, evolving BIS standards of prudential regulation and supervision have been the hallmark of policy convergence (e.g. Hall 2003; Barth, Caprio, and Levine 2008; Rochet 2008). Fiscal discipline was an old idea for liberal economists,
but the spread of NPM principles of transparent, accountable public financial management provided much stronger ammunition for bureaucratic reformers (e.g. Guthrie et al. 2005). These normative developments in finance, writ large, which emerged in response to troubles and failures of marketization and neoliberal globalization in various parts of the world, comprise an integral part of the institutional turn in development thinking. For instance, four of the ten items on Rodrik’s (2006, 978) list of “Augmented Washington Consensus” are distinctly financial in nature: financial codes and standards, prudent capital account-opening, non-intermediate exchange-rate regimes, and independent central banks/inflation targeting. And two (corporate governance and WTO agreements) are tightly related.

Table 6.1    Turkey and the World Bank: 1980s, 1990s, 2000s

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<tr>
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<tbody>
<tr>
<td>Number of Projects</td>
<td>60</td>
<td>33</td>
<td>35</td>
</tr>
<tr>
<td>Total Loan Amount (US$ Million)</td>
<td>7,893.8</td>
<td>4,011.03</td>
<td>12,910.08</td>
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Source: World Bank (online). “Total Loan Amount” refers to the sum of loan amounts stated in loan agreements and not actual disbursement figures. 2008 data is as of August.

These intellectual currents provided the inspiration for the most important World Bank projects during Turkey’s technocrat-led postcrisis restructuring. The Economic Reform Loan of May 2000 (US$759.6 million) kick-started the dissolution of the EBF system and called for limits on Treasury guarantees on public borrowing (World Bank 2000a). The Financial Sector Adjustment Loan (FSAL) of December 2000 (US$777.8 million) emphasized prudential reforms in banking with specific clauses regarding BDDK operations and legal improvements in the regulatory framework (World Bank 2000a).
The Programmatic Financial and Public Sector Adjustment Loan (PFPSAL) of July 2001 (US$ 1.1 billion) followed up on banking restructuring, but now also included conditions regarding public expenditure reform and the borrowing regime (World Bank 2001a). Finally, the second PFPSAL of April 2002 (US$1.35 billion) was almost identical to the first one in its simultaneous engagement of banking and public sector reforms (World Bank 2002b).

Second, and on the insulation side, finance constitutes a rather special case for IFI-led institutional reforms also because of the issues and the actors involved. Banking is one area in which the World Bank does not have to tip-toe around the ‘best practice’ vs. ‘good fit’ rhetoric (World Bank 2003a, 18ff) or praise the virtues of designing new institutions in ways that “complement what exists” (World Bank 2002a, 10ff). BIS standards are not the least bit about good fit but precisely about best practice and across the board harmonization via transplantation of blueprints. And in finance there is little point in trying to complement endogenous structures, since these are often the sort of arrangements countries are encouraged to get rid of in the first place. The stakes are simply too high for that sort of political correctness. Furthermore, promoting capital adequacy requirements, harmonized charts of accounts, or compulsory disclosure principles is predominantly a ‘state vs. bankers’ affair distanced from ‘the people’, so there is no real-world grassroots approach to it. Similar considerations apply to the restructuring of fiscal governance as well. There is nothing objectionable about reforming an obsolescent, disorganized public expenditure regime, a weak tax bureaucracy, or an undisciplined debt management framework. Here again, potential enemies of reform are

28 Insider transactions and the politicized nature of corporate lending in Asian financial systems offer a good example, which many observers believe to have created a deep moral hazard inviting the 1997 crisis; see, for instance, Haggard (2000, 24ff).
seldom a respectable bunch: populist politicians, traditional bureaucrats, financial
rentiers, and so on. For these reasons, technocratic insulation is easier to achieve in fis-co-
financial reform and, when strict insulation becomes unfeasible over time, one can still
expect the burden of negotiation to be much lighter than in other areas of reform.

Negotiated Innovation: Consolidation

From late 1999 to late 2002, Turkey’s second generation neoliberal reformers
made good use of a relatively closed decision-making environment to re-engineer
banking and debt management regimes. AKP leaders did not enjoy such generous
insulation. They faced, instead, a more competitive environment open to societal
negotiation and political coalitions. But even though reform resistance came from many
quarters, including the party itself, it proved weak and disorganized, and in the presence
of continuing international constraints and strong reformist support from dominant
collective interests, was defeated with minor concessions. By mid-decade, novel fiscal
and financial arrangements were largely consolidated.

Let us begin with the reform of the public expenditure regime, which, because of
the colossal undertaking it involved, could not be completed under the brief episode of
technocratic insulation. Turkey’s fiscal problems were partly rooted in an expenditure
regime inherited from the early days of the republic. The system was governed by Law
No. 1050 of General Accounts, dating back to 1927 with numerous subsequent
modifications. This framework was too awkward to meet the flexible needs of a
liberalized policy environment. The preferred fiscal coding, dubbed as ‘program-based

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budgeting’, created severe problems of classification and planning over time, obscuring the relationship between resources and spending. The law was also notorious for its strict though cumbersome mechanisms of budgetary control. They became the main motive for early neoliberal reformers to eschew ‘fiscal spending’ altogether by relying on EBFs.29

As in other areas of reform, attempts at restructuring this regime too preceded the 2001 crisis. In 1999, during the preparation of the Eighth Five-Year Development Plan, a special commission convened to identify the problems of public financial management and design a program for reorganization (DPT 2000). The commission brought top bureaucrats from the Treasury, the Ministry of Finance, the Central Bank, and the Court of Accounts together with academics as well as representatives from some civil society organizations. The findings and suggestions of the commission report served as the basis for a subsequent World Bank project in 2000-2001, the Public Expenditure and Institutional Review (PEIR) (World Bank 2001b). This document, hailed by the IMF, proposed replacing the age old principle of ‘program-based’ budgeting with a ‘performance-based’ design, introducing a new and unified system of codification for all public accounts, and strengthening external auditing mechanisms.30 Thus, by the time the crisis hit, a comprehensive road map for modernizing Turkey’s public accounts in line with international norms was already on the table.

The culmination of these efforts was the Public Financial Management and Control Law No. 5018 (Resmi Gazete, 24 December 2003). Drafted in the NPM spirit of building capacity through increased transparency and accountability, and clearly modeled on the World Bank PEIR, the law replaced the antiquated Law No. 1050 mentioned

29 Interview, Department Head (Anonymous), the Ministry of Finance, 3 August 2004.
30 See also Kiziltaş (2001).
earlier. The new framework harmonized Turkey’s public accounts with international standards, adopting the GFS (Government Finance Statistics) system and introducing a new codification. In line with the principle of performance-based budgeting proposed in 1999, it emphasized strategic management, medium-term planning, and both pre- and post-spending control mechanisms based on functional performance. It also placed a larger legal responsibility on fiscal authorities at all levels.\(^{31}\)

The reform was not without its contenders. The law was enacted in late 2003, but it went into effect only by the 2006 fiscal year. The main reason for this delay was opposition from both the traditionalist bureaucracy and within the AKP itself. The bill was attacked for bringing principles of IMF-inspired ‘corporate governance’ into the realm of state finances and sacrificing too much of the authority of the ‘center’ in favor of local and external elements.\(^{32}\) It also came under heavy criticism from lower level civil servants for passing too much responsibility upon them without offering comparable means of legal and professional protection.\(^{33}\) A second challenge came from the government. Strong economic recovery after 2002 triggered pressures from within the AKP to circumvent fiscal austerity. Public expenditure reform, taken in the context of high primary surplus requirements set by the IMF, was a significant obstacle to satisfy such pressures. In early 2005, several bills were submitted to the parliament that contravened the new regime. One granted amnesty to outstanding social security payments by small businessmen and the self-employed. Another introduced a generous

\(^{31}\) See BUMKO (2004) for an exhaustive comparative analysis of the new regime.

\(^{32}\) Dikmen (2003), for instance, charged that the bill was part of “an operation to subjugate the last strongholds of the public bureaucracy to the international system. International standards will serve as an important instrument of this. (…) [T]he Ministry of Finance and Court of Accounts bureaucrats will by and large lose their institutional tradition” (translation mine, emphasis added). For another critique along similar lines, see Oyan (2003).

\(^{33}\) See Karagöz (2003). The author is the chief public financial manager in a small Central Anatolian town.
scheme of industrial support to underdeveloped regions. Upon heated public debate and negotiations with the IMF, these and other bills were shelved. The normative content of the institutional reform agenda in public finance proved to be too thick to be easily perforated by old-style bureaucratic or populist impulses. Instead, reforms were expanded toward the reorganization of the extractive arm of the Turkish state. In 2006 a semiautonomous Revenue Administration was established within the Ministry of Finance to replace a highly politicized general directorate notorious for its inefficiency.

The story of public expenditure reform is emblematic of a certain pattern repeated in other areas of fiscal-financial restructuring under AKP rule. On the one hand, there emerged sporadic resistance to reforms, at times from within the bureaucracy, at other times from various social groups, some close to the party’s traditional base. Driven by classic center-right populist instincts, the AKP was at first receptive to such protests, and did not refrain from testing the resolve of the technocrat-IFI alliance via assorted moves to slow down or partially reverse the process. More than a genuine commitment to democracy, it was this political calculation to widen its coalitional base that inspired the party’s openness to social deliberation.

On the other hand, and midway through the party’s first term in office, attempts to appease reform skeptics lost their appeal. By late 2005 a critical threshold was passed in reform compliance. There were two related processes at work here. The first was growing private sector support for restructuring. Following the 2002 elections, dominant industrial interests, represented by TÜSİAD, began to throw their weight much more decidedly behind IFI-led reforms to pre-empt a potential backpedaling under the new government. The association endorsed reforms not only through private consultations with AKP

34 The major exception to this is the gradual subversion of the Public Procurement Reform. See fn.9.
leaders and frequent public statements, but also by commissioning various comprehensive reports on specific areas of institutional restructuring, often prepared by leading liberal-minded scholars in each field.\(^{35}\) Initially, TÜSİAD’s enthusiasm for reforms was not shared by smaller bourgeoisie, AKP’s classic support base. But a spectacular economic performance in 2004, which saw a record-high real GDP growth of over 8 percent, would lead to a fundamental change in reform perceptions among these social segments. The Union of Chambers (TOBB), the umbrella organization of the private sector biased toward commercial interests and smaller industrialists, emboldened its support for reforms (TOBB 2005). Even MÜSİAD, the representative of smaller Anatolian capitalists and a key ally of the AKP, softened its critique of the IMF program and began calling for a ‘deepening’ of micro-regulatory reforms, continued restructuring of the public finance regime, and accelerated adoption of new Basle standards in banking (MÜSİAD 2005, 62ff). By 2005, a broad private sector coalition emerged around fiscal and financial restructuring.

Second, counterreform also lost its appeal because of the continued strength of external anchors. To begin with, the AKP had already inherited, very unwillingly, a new and highly restrictive IMF agreement. The third PFPSAL with the World Bank in April 2004 could be considered a by-product of this persistent IMF constraint. It included strong conditions regarding fiscal discipline and monetary rigor, and placed special emphasis on the deepening of public financial reforms (World Bank 2004a). However,\(^{35}\) One important report was about the role of autonomous regulatory agencies, and paid special attention to BDDK (TÜSİAD 2002b). This was followed by a joint TÜSİAD-OECD comprehensive study on Turkey’s regulatory reforms (TÜSİAD-OECD 2003). In banking, the association’s main policy paper was very much supportive of BDDK’s position (TÜSİAD 2003a); other studies discussed improving relations between financial institutions and the real sector (TÜSİAD 2005a) and restructuring of capital markets (TÜSİAD 2005b). Apart from these, TÜSİAD commissioned one major project on public sector reform as a whole (TÜSİAD 2002c) and two reports on public sector performance and reorganization of the public income regime (TÜSİAD 2003b; 2003c).
with a high performing economy in one hand, and stronger private sector support for reforms in the other, the AKP’s original reservations about the IFI anchor dissipated, and the party did not object to a new, US$10 billion stand-by agreement with the IMF in May 2005. The start of membership negotiations with the EU in October 2005 further stoked the reform fire, with the attention of financial and public sector reformers now turning toward harmonization with European norms several notches above what IMF and World Bank deemed good enough for developing countries. Given this rise of the institutional reform bar, and upon the successful completion of three consecutive PFPSALs, it was not hard for the government to digest a new World Bank facility in June 2006. This time it was a Programmatic Public Sector Development Policy Loan (PPDPL) that focused on pension and health care reforms as well as overall improvements in public sector governance (World Bank 2006).

The consolidation of banking, Central Bank and Treasury reforms in 2005-2006 should be viewed in that general context of strengthened domestic support and continued external anchors. The Central Bank’s newfound independence would be tested on three separate occasions, none of which succeeded in a backpedaling from the principle. First, Treasury officials were quick to realize that the bank’s autonomy had important negative implications for debt management. Their main criticism was that lack of coordination (read, collusion) between these two agencies, specifically in the area of interest rates, and the bank’s weight in secondary markets for public securities, led to suboptimal Treasury decisions in the timing and amount of debt issuance. Even then, such within-state discomfort was ignored. Second, the rapid overvaluation of the lira after 2003 led to widespread disenchantment with the floating exchange rate regime among exporters,

36 Interview, Deputy General Director (anonymous), the Undersecretariat of Treasury, 24 August 2004.
generating calls for Central Bank intervention to ensure price competitiveness in international markets. Yet, the desirable side-effects of expensive currency and the absence of clear evidence for its export-damaging outcomes meant the devaluation lobby failed to harness sufficient social and policy support to pressure the bank to relax its monetary stance. Finally, Central Bank reform was tested one last time in the spring of 2006 when, upon the retirement of the bank’s much-revered Governor, Süreyya Serdengeçi, the government attempted to replace him with an outsider known to have close ties to the AKP. Yet faced with a presidential veto followed by mounting criticism from TÜSİAD and the IMF, the government did not insist on its candidate and picked instead an insider veteran for the job. Notice that all three instances marked impulsive reactions to the recent path change in monetary governance. In none of these instances were political stakes high enough for the government to undermine seriously the bank’s autonomy and thereby endanger the hard-found stability at home and the prestige abroad.

The consolidation of Treasury and banking reforms offered a more colorful picture. In these areas as well, novel arrangements appeared to have quickly accumulated a certain degree of resiliency that made sharp reversals unfeasible in the short run. In both, policy pressures in the form of IFI conditionality and the EU anchor were a crucially important factor. Yet more interesting was the way domestic political considerations and, in the case of banking, market integration reinforced emergent institutional arrangements.

Overvalued currency helped ameliorate the foreign debt problem of both the public and the private sector and facilitated the domestic demand-driven growth dynamic of the Turkish economy by making consumer imports cheaper. And the expensive lira was never proven to damage export performance, partly because most manufacturing exports were also heavily dependent on the import of intermediate goods; if anything, Turkish exports were exceptionally strong during the 2004-2007 period.
The main challenge in Treasury reform was within-state political struggles. As discussed earlier, both before and under Kemal Derviş, the undersecretariat served as a super-agency that coordinated top-down restructuring efforts in all areas in close cooperation with the IMF. The 2002 debt management law further empowered the agency. This privileged status of the undersecretariat caused resentment in other branches of the economic bureaucracy, and most notably in the DPT and the Ministry of Finance—the two agencies normally responsible for the budget. The AKP’s rise to power was a major boost for these traditionalist elements. Unlike most other executive departments, the AKP found it difficult to permeate the Treasury, which for two generations had remained the stronghold of Western-minded, liberal-secular technocratic elites, dubbed as the ‘White Turks’. The constraint here was one of structural dependence. The AKP had a sizeable following within the state, but neither inside the Treasury nor elsewhere within the bureaucracy did it have the cadres that could replace the well-educated, technically adept management of the agency. Furthermore, the powers of the Treasury, given its semi-autonomous character, exponentially increased the IFI constraint on almost every aspect of economic policymaking, and therefore were perceived with suspicion during the party’s initial years in office. In such a context, rather than try to capture the agency, the AKP strategy concentrated on undermining its authority through an alliance with traditional bureaucratic elements. Throughout 2003 and 2004, the Treasury was gradually toppled from the throne of economic governance, and the center of gravity in reform coordination shifted toward the DPT, within which the party was able to find (and implant) more sympathizers.\(^{38}\) In fact, the AKP was willing to

\(^{38}\) The rise of the DPT was a theme that cropped up repeatedly during my interviews at the Undersecretariat of Treasury in July-August and December of 2004. I was offered two explanations. The first was intra-
go much further. There were strong rumors that the government was actually planning to abolish the undersecretariat altogether, and regroup its various departments to form a general directorate that would operate under the wings of the Ministry of Finance, as had been the case before 1983 (Sağlam 2005). This strategy would have transferred the Treasury’s extensive discretion over public borrowing to a politically more manipulable state organ. Even though this plan never saw the daylight, it was indicative of the deep intra-state tensions that could no longer be suppressed when technocratic insulation came to an end.

These struggles over the Treasury provoked an opportunistic coalition between the ruling party and the traditionalist bureaucracy, but had virtually no effect on the novel debt management regime. As in the case of central bank independence, Turkey had gone too far down the reformist path. The main players were too invested in emergent arrangements to make a radical reversal. Besides, lighter coordinative responsibilities freed up Treasury resources to concentrate better on its primary tasks and gave it a more compact organizational and policy turf to defend. The outcome was growing institutional capacity and continued innovations in debt management along reformist lines. Despite resurfacing expenditure pressures (and the main burden here came from the deficits of the social security system but also increased agricultural supports), the ‘total borrowing limit’ bureaucratic vengeance. Under the DSP-MHP-ANAP coalition that launched the reform drive and later faced the 2001 meltdown, the DPT was controlled by the ultra-nationalist MHP wing of the government, which did not have a strong economic policy agenda. As a result, the organization was very much marginalized during the design of the recovery program. Eager to restore their influence, DPT managers did not hesitate to accommodate the AKP’s desire to break the tyranny of the Treasury, and established close relations with party ministers. The second factor that brought the DPT to the fore was the EU process. The organization was given full responsibility to design and implement a national program for EU integration. Presumably, the influence of the DPT increased as the ultimate object of structural reforms shifted from IFI-led recovery in 2001-2002 to harmonization with European norms by mid-decade. In other words, the EU process tilted the intra-state balance of power in a direction strategically preferred by the AKP. This perhaps constitutes a small piece of the bigger puzzle of AKP’s pro-EU stance despite its Islamist roots.
proved a tightly enforced, unbreakable rule. The ‘market maker’ system, whereby a select
number of commercial banks were given special rights and obligations as ‘primary
dealers’ in Treasury actions, was revamped and reintroduced. Debt instruments were
diversified to suit specific borrower and investor needs, and now included zero-coupon
and floating rate notes as well as price index-linked and foreign exchange-denominated
bonds. The newly established risk management unit (‘middle office’) quickly became the
most crucial Treasury department, overseeing the borrowing and rollover strategy via
continuous sustainability projections and sensitivity analyses. Meanwhile, quarterly debt
management reports and advance disclosure of borrowing strategy and the auction
calendar improved transparency and predictability.  

Banking reform offered a parallel example of consolidation, but here political
battles were more intense and more public. The 1999 Banks Law No. 4389, which had
established the BDDK, was routinely criticized for its poor legal technique; there was a
general consensus that too many of its stipulations were compressed into too few articles
in a convoluted fashion. The law was also amended numerous times over the years in line
with new BDDK regulations: full deposit insurance was replaced with partial insurance to
target only small clients; stringent rules were adopted to facilitate collections from
shareholders of failed banks; the TMSF was separated from the BDDK. Work on new
legislation accelerated in 2003, and a bill, dubbed Credit Institutions Law, was made
public in the spring of 2004. It was followed by another draft, now entitled Financial
Services Law. The political debate around that time concentrated, first, on the weight of
sworn auditors in the BDDK, an important matter for intra-organizational balances; and

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39 Undersecretariat of Treasury, Debt Management Reports (various issues). See also Cangöz (2008) for an
outline of the borrowing strategy in recent years; the author is the Treasury’s Director General of Public
Finance.
second, on what to do with failed banks, that is, whether to retain the option of TMSF receivership or to opt for automatic resolution so as to avoid costly public bailouts. Otherwise, both bills were built on the general principles introduced in the 1999 law and subsequent amendments and regulations.

Bankers were opposed to these drafts from the very beginning. They had already found the 1999 law too constrictive, BDDK regulations too heavy-handed, and the TMSF’s method of dealing with failed banks too ruthless. They considered the proposed legislation as the solidification of this general attitude. Ersin Özince, still the chairman of the TBB, charged before a BDDK panel that “the regulations that are practiced and planned are impulsive in nature”, and represent “an excessively controlling and punitive approach” (Özince 2004). The bill, he argued, put the sector under the yoke of some ‘extraordinary’ measures devised under crisis circumstances.

But over a year of intense lobbying by banks bore no fruit. A last draft, very much along the same lines as the previous two, was announced in April 2005, under the more conventional name, the Banking Law. The TBB fought hard to change this draft as well, proposing a comprehensive list of amendments (TBB 2005). It demanded more liberal loan limits toward affiliated risk groups, leniency in the criminal and financial responsibility of shareholders and executives, and lesser TMSF powers in collections from owners of failed banks. The BDDK stood behind the strict stipulations of the bill; “the easiest way to rob a bank is to own it”, declared its chairman, Tevfik Bilgin, countering TBB pressure. Bankers’ last hope, the parliamentary commission debates in late June, was no help either.

40 Similar concerns were voiced by liberally-oriented observers in the media; see, for instance, İlkorur (2004) and Tuncer (2004).
The new Banking Law No. 5411, enacted in October, is an evolutionary step over its predecessor (Resmi Gazete, 1 November 2005). A fairly long document heavy in legal definition and regulatory scope, it comprises 194 articles as opposed to 27 of the 1999 law. Its stipulations regarding the establishment and operating principles of banks and other financial institutions are exhaustive. The respective roles of the BDDK and the TMSF are also painstakingly elaborated. Finally, while retaining the option of public takeover, it also extends the time clause and the scope of shareholder and executive responsibility with increased fines and penalties for all fraud and misconduct, consistent with the measures put in place after 2000. Just as the TBB feared, what the law represents in essence is a detailed codification of the emergent regulatory framework.

Apart from the IMF and EU anchors, two factors help explain the ease with which the government was able to bypass pungent opposition from bankers over the new law. First, bankers failed to garner support for their cause from other business interests and were left to fend against the law on their own. As discussed before, by 2005 not only Istanbul-based big industry, but less affluent and numerically more significant segments of the private sector were also rallying behind IFI-led restructuring. With the popularity of the reform process at its peak, bankers lacked any potential partners to strike a counter-coalition.42 Second, and perhaps more crucially for long-run considerations, was

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42 It is interesting to note that the traditionally high degree of interpenetration between Turkey’s financial and industrial capital did not make a difference at that level. The overwhelming majority of the actors targeted by the BDDK were small banks associated with mid-size conglomerates. The country’s two largest conglomerates, Koç and Sabancı, were not implicated in the banking crisis. Koç had a small though very sound bank. Sabancı, on the other hand, had one of the largest retail banks, Akbank, which was prudently managed and was unaffected by systemic troubles. In quelling the opposition to sectoral restructuring and establishing autonomy vis-à-vis financial interests, Turkey’s reformers relied on the complacency of these largest conglomerates. About the only problem was Yapı Kredi Bank of the Çukurova group, over which the BDDK had gained control after the Pamukbank incident discussed earlier. Once the battle over the new Banking Law was won, the Koç Group, which had fervently supported the reregulatory reform agenda,
increased foreign entry into the Turkish banking system. This second factor made the streamlining of the regulatory framework along evolving international norms not only more acceptable but also vital—a fundamentally important point I shall discuss in the next section, along with other outcomes of fisco-financial restructuring.

_A Cautious New World_

The promise of institutional reform is that careful manipulation of the rules of the game, by ushering in new constraints and incentives for collective players, will alter the outcomes of the game itself in a direction deemed more desirable by reformers. Seen this way, Turkey’s fisco-financial reforms delivered nicely on that promise. What emerged out of this process was a new world, but not a brave one—for it was actors’ excessive boldness in advancing their short-term interests that brought the old world to a painful end. By contrast, the new world is built on a sense of fear and mutual distrust. It values prudence, risk-aversion, and self-control, and shuns any opportunistic hardiness of heart that eventually destroyed populist politicians and rentier capitalists of the 1990s. But in this cautious new world there also appears to exist, at least so far, a potential for growth and security.

Table 6.2 shows the scale of fiscal damage incurred during the crisis and the dramatic pace of recovery thereafter. Fiscal deficit, PSBR, and the ratio of public debt to GNP all rose to previously untested levels in 2000-2001, but then steadily fell from 2002 onward. The debt stock continued to increase, and total borrowing seemed high even purchased the bank in partnership with Italian Unicredito, becoming a serious competitor in retail banking to its historic rival, Sabanci.
after 2005, but this was mainly due to the rollover of existing debt. More significant is the halving of debt to GNP ratio and the tripling of maturities from 2001 to 2006. In fact, in 2006 and 2007 net borrowing was negligible and foreign debt stock remained unchanged. And even though real interest rates are still high, this is a problem endemic to the rest of the economy—note that from 2004 onward, yield on government securities has indeed fallen behind bank deposit rates. Thanks to sustained fiscal discipline and prudent management of public debt, the Turkish state seems to be largely out of the woods.

Table 6.2  Selected Fiscal and Debt Management Indicators (2000-2007)

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Growth (GNP constant prices)</td>
<td>6.3</td>
<td>-9.5</td>
<td>7.9</td>
<td>5.9</td>
<td>9.9</td>
<td>7.6</td>
<td>6.0</td>
<td>4.6</td>
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<tr>
<td>Fiscal Revenue / GNP (%)</td>
<td>22.9</td>
<td>24.3</td>
<td>22.7</td>
<td>22.2</td>
<td>22.0</td>
<td>23.5</td>
<td>22.9</td>
<td>22.1</td>
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<td>Fiscal Expenditures / GNP (%)</td>
<td>30.8</td>
<td>36.2</td>
<td>34.1</td>
<td>31.1</td>
<td>27.2</td>
<td>24.6</td>
<td>23.5</td>
<td>23.8</td>
</tr>
<tr>
<td>Fiscal Deficit / GNP (%)</td>
<td>-7.9</td>
<td>-11.9</td>
<td>-11.5</td>
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<td>-5.2</td>
<td>-1.1</td>
<td>-0.6</td>
<td>-1.6</td>
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<tr>
<td>PSBR / GNP (%)</td>
<td>11.8</td>
<td>16.4</td>
<td>12.7</td>
<td>9.3</td>
<td>4.7</td>
<td>-0.4</td>
<td>-3.0</td>
<td>0</td>
</tr>
<tr>
<td>Primary Surplus / GNP (%)</td>
<td>4.4</td>
<td>5.2</td>
<td>3.3</td>
<td>4.0</td>
<td>4.9</td>
<td>6.0</td>
<td>5.4</td>
<td>4.1</td>
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Composition of Fiscal Expenditures

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<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest %</td>
<td>39.8</td>
<td>47.2</td>
<td>43.2</td>
<td>41.4</td>
<td>37.1</td>
<td>28.6</td>
<td>25.8</td>
<td>23.9</td>
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<tr>
<td>Personnel %</td>
<td>18.7</td>
<td>16.7</td>
<td>18.4</td>
<td>20.4</td>
<td>22.1</td>
<td>23.4</td>
<td>24.1</td>
<td>24.3</td>
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</table>

Public Debt Stock (US$ Million)

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Foreign</td>
<td>40,514</td>
<td>38,729</td>
<td>56,773</td>
<td>63,346</td>
<td>68,583</td>
<td>64,643</td>
<td>66,576</td>
<td>67,120</td>
</tr>
<tr>
<td>Domestic (Net)</td>
<td>54,216</td>
<td>84,857</td>
<td>91,691</td>
<td>139,262</td>
<td>167,262</td>
<td>182,428</td>
<td>178,906</td>
<td>219,200</td>
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<tr>
<td>Public Debt Stock / GNP (old series) (%)</td>
<td>56.5</td>
<td>90.4</td>
<td>78.4</td>
<td>70.3</td>
<td>64.0</td>
<td>55.5</td>
<td>45.1</td>
<td>N/A</td>
</tr>
<tr>
<td>Public Debt Stock / GNP (new series) (%)</td>
<td>42.9</td>
<td>66.3</td>
<td>61.4</td>
<td>55.1</td>
<td>49.0</td>
<td>41.6</td>
<td>34.0</td>
<td>29.0</td>
</tr>
</tbody>
</table>

Total Domestic Borrowing (US$ Million)

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Banks / Total Borrowing (%)</td>
<td>75.9</td>
<td>74.5</td>
<td>79.8</td>
<td>75.5</td>
<td>85.8</td>
<td>88.3</td>
<td>88.5</td>
<td>82.1</td>
</tr>
<tr>
<td>Average Maturity (Months)</td>
<td>..</td>
<td>9</td>
<td>11,5</td>
<td>14.7</td>
<td>27.4</td>
<td>28</td>
<td>34</td>
<td></td>
</tr>
<tr>
<td>Net Domestic Borrowing (US$ Million)</td>
<td>21,646</td>
<td>69,966</td>
<td>18,403</td>
<td>29,816</td>
<td>21,160</td>
<td>15,140</td>
<td>4,673</td>
<td>2,950</td>
</tr>
</tbody>
</table>

% Return on Government Securities

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>vs. Consumer Price Index</td>
<td>-14.3</td>
<td>43.1</td>
<td>13</td>
<td>20.7</td>
<td>16.1</td>
<td>8.1</td>
<td>9</td>
<td>10</td>
</tr>
<tr>
<td>vs. Deposit Interest Rates (1 year)</td>
<td>-5.65</td>
<td>34.5</td>
<td>9.8</td>
<td>17.4</td>
<td>3.6</td>
<td>-4.1</td>
<td>-5.1</td>
<td>-2.6</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance, General Directorate of Budget and Financial Control (online); HM Public Debt Management Reports (various); Turkish Statistical Institute (online); TCMB EDDS (online); TBB Annual Reports (various).

43 The overvaluation of the lira also makes total domestic borrowing look high in dollar terms. Controlling for price inflation, total borrowing in 2007 was in fact about half the 2004 level in lira terms.
Table 6.3  
Banking Sector: Assets, Credits, Equity, Profits, Market Structure  
(2000-2007) (US$ Million)

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public Commercial</td>
<td>53,154</td>
<td>37,211</td>
<td>45,046</td>
<td>55,680</td>
<td>75,160</td>
<td>92,845</td>
<td>100,176</td>
<td>125,689</td>
</tr>
<tr>
<td>Private Commercial</td>
<td>73,540</td>
<td>64,752</td>
<td>79,339</td>
<td>95,288</td>
<td>123,695</td>
<td>176,793</td>
<td>185,601</td>
<td>225,530</td>
</tr>
<tr>
<td>Foreign</td>
<td>8,403</td>
<td>3,493</td>
<td>4,399</td>
<td>4,650</td>
<td>7,274</td>
<td>15,451</td>
<td>41,453</td>
<td>64,798</td>
</tr>
<tr>
<td>Credits</td>
<td>50,919</td>
<td>28,329</td>
<td>37,434</td>
<td>46,877</td>
<td>72,585</td>
<td>114,156</td>
<td>152,374</td>
<td>215,483</td>
</tr>
<tr>
<td>Public Commercial</td>
<td>13,727</td>
<td>6,086</td>
<td>6,215</td>
<td>8,527</td>
<td>15,142</td>
<td>23,530</td>
<td>32,883</td>
<td>48,555</td>
</tr>
<tr>
<td>Private Commercial</td>
<td>27,742</td>
<td>17,274</td>
<td>24,438</td>
<td>31,454</td>
<td>48,949</td>
<td>77,048</td>
<td>89,232</td>
<td>117,588</td>
</tr>
<tr>
<td>Foreign</td>
<td>1,438</td>
<td>937</td>
<td>1,493</td>
<td>3,397</td>
<td>3,397</td>
<td>7,811</td>
<td>23,334</td>
<td>40,549</td>
</tr>
<tr>
<td>Credits / Assets</td>
<td>32.86</td>
<td>24.63</td>
<td>26.50</td>
<td>28.02</td>
<td>33.69</td>
<td>38.56</td>
<td>44.97</td>
<td>49.98</td>
</tr>
<tr>
<td>Public Commercial</td>
<td>25.82</td>
<td>16.36</td>
<td>13.80</td>
<td>15.31</td>
<td>20.15</td>
<td>25.34</td>
<td>32.83</td>
<td>38.63</td>
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<tr>
<td>Private Commercial</td>
<td>37.72</td>
<td>26.68</td>
<td>30.80</td>
<td>33.01</td>
<td>39.57</td>
<td>43.58</td>
<td>48.08</td>
<td>52.14</td>
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<tr>
<td>Foreign</td>
<td>17.11</td>
<td>26.83</td>
<td>33.94</td>
<td>39.94</td>
<td>46.30</td>
<td>50.55</td>
<td>56.29</td>
<td>62.58</td>
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<tr>
<td>Owner’s Equity</td>
<td>7,514</td>
<td>6,727</td>
<td>17,066</td>
<td>23,802</td>
<td>32,315</td>
<td>40,078</td>
<td>40,512</td>
<td>56,462</td>
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<tr>
<td>Public Commercial</td>
<td>1,450</td>
<td>2,757</td>
<td>4,841</td>
<td>7,078</td>
<td>9,885</td>
<td>10,374</td>
<td>12,929</td>
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<tr>
<td>Private Commercial</td>
<td>7,867</td>
<td>3,001</td>
<td>10,090</td>
<td>14,037</td>
<td>19,263</td>
<td>21,924</td>
<td>27,580</td>
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<td>Foreign</td>
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<td>380</td>
<td>922</td>
<td>1,116</td>
<td>1,464</td>
<td>2,461</td>
<td>4,971</td>
<td>8,563</td>
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<tr>
<td>Net Profits (sector)</td>
<td>-4,689</td>
<td>-3,570</td>
<td>-1,914</td>
<td>3,758</td>
<td>4,539</td>
<td>4,262</td>
<td>7,673</td>
<td>11,011</td>
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<tr>
<td>Public Commercial</td>
<td>-276</td>
<td>-14</td>
<td>701</td>
<td>1,199</td>
<td>1,886</td>
<td>2,140</td>
<td>2,600</td>
<td>3,467</td>
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<tr>
<td>Private Commercial</td>
<td>-594</td>
<td>-2,312</td>
<td>1,600</td>
<td>1,954</td>
<td>1,986</td>
<td>1,037</td>
<td>3,254</td>
<td>5,497</td>
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<td>Foreign</td>
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<td>54</td>
<td>125</td>
<td>174</td>
<td>383</td>
<td>1,021</td>
<td>1,303</td>
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<td>Profitability (% Assets)</td>
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<td>-6.6</td>
<td>1.1</td>
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<tr>
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<td>Total Number of Banks</td>
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<tr>
<td>Total Deposits</td>
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</tbody>
</table>

Source: TBB Annual Reports. Currency conversions are based on Central Bank average buying rates per year.

In banking as well, we encounter radically different conditions from the 1990s. The substantial sectoral reorganization can be traced at four levels (Table 6.3). The first relates to what might be termed a healthy growth of system fundamentals: from 2000 to
2007, assets tripled and equity rose by seven times. Perhaps most positively, the credit squeeze that stifled growth in the 1990s seems to be over, with credits quadrupling during this period and their ratio to assets almost doubling from a low of 25 percent in 2001.

Second, the income and profit structure has also changed. Although profits resumed after 2001 and were particularly strong in 2006-2007, profitability, measured relative to assets, could never catch the fat figures of the previous decade. Particularly dramatic has been the decline in the profitability of private commercial banks: from an average of 5.5 percent in 1995-1999, during the classic phase of double redistribution, to less than one-third of that level during the recovery years of 2003-2007. Table 6.4 sheds some light on the income structure of these banks. Rather surprisingly, interest income from securities (and over 90 percent of this comes from government securities) is still quite important for banks’ balance sheets. The problem, however, is that the persistently high income from this source in recent years was largely the result of the maturation of previously existing stock. This stock has kept dwindling since 2003, and its renewed portion is in longer maturities and carries lower yields. Unless in the unlikely event of a fiscal collapse, this development suggests that a sharp drop in securities income is inevitable for private commercial banks in the near future. A second inevitability appears to be the return of traditional banking activities as the main source of commercial bank profits. Here, just as important as the rise in credit income is the growth of non-interest income, mainly as a consequence of the expansion of fee-based activities. The focus of competition is now retail clients as banks keep diversifying their services.
Table 6.4  
*Private Commercial Banks:  

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Gov. Securities Held</strong></td>
<td>4,431</td>
<td>6,024</td>
<td>7,819</td>
<td>9,957</td>
<td>6,325</td>
<td>7,137</td>
<td>5,582</td>
<td>4,664</td>
</tr>
<tr>
<td><strong>Interest Income</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Securities</td>
<td>3,495</td>
<td>5,509</td>
<td>5,788</td>
<td>5,205</td>
<td>6,369</td>
<td>6,284</td>
<td>6,468</td>
<td>8,198</td>
</tr>
<tr>
<td>Credits</td>
<td>7,429</td>
<td>7,993</td>
<td>4,901</td>
<td>5,082</td>
<td>7,862</td>
<td>10,344</td>
<td>11,771</td>
<td>16,491</td>
</tr>
<tr>
<td><strong>Non-Interest Income</strong></td>
<td>1,454</td>
<td>-3,834</td>
<td>2,775</td>
<td>5,277</td>
<td>3,827</td>
<td>4,629</td>
<td>4,585</td>
<td>6,924</td>
</tr>
</tbody>
</table>

*Source:* TBB Annual Reports

Third, changing rules and conditions have triggered a change in players. This change is manifested at two levels: consolidation and foreign entry. The small ‘group banks’ of the 1990s, which represented the worst of rentier capitalism with their utmost reliance on fiscal expansion, reckless exposure to affiliated firms, shady political connections, and built-in resistance to regulatory oversight, have all but disappeared. Some 20 of these banks were taken over by the TMSF between 1999 and 2003; survivors found it difficult to compete in the new playing field and many merged with bigger players.44 In the end, from a high of 38 private commercial banks in 1998, there remained only 11 in 2007.

On the other hand, the very conditions that destroyed Turkey’s nascent rentier class also encouraged the mass entrance of a new type of actor into the system—large foreign players. Turkey did not have legal barriers to foreign entry in the 1990s, but the 20 or so foreign banks operating in Turkey had a miniscule weight in the system, with around 3-4 percent of total assets. Many of these were boutique banks with a single branch. Thus, even though the sector was highly internationalized in operations, ownership was overwhelmingly domestic. This picture has changed dramatically since

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44 Some notable mergers included Körfezbank-Osmanlı-Garanti; Bank Ekspres-Tekfenbank; Sümerbank-Oyakbank; and Denizbank-Tarişbank.
2001. Regulatory improvements created both a fairer competitive environment for larger foreign players and meant more tolerable country risks. Besides, Turkey was a relatively untapped market with low levels of per capita bank assets, and the decline in the financial dominance of public instruments, the fast pace of its economic growth, and its rising EU prospects made it look very alluring to investors. The result was a rush of foreign entry, especially in the retail market (Table 6.5). By 2008, foreign presence in the sector, including minority shares, reached around 45 percent. And only four commercial banks in the system, the three remaining public banks (Ziraat, Halk, Vakıf) plus the quasi-public İş Bankası, have no foreign ties whatsoever.

**Table 6.5**  *Mass Foreign Entry into the Turkish Banking System*

<table>
<thead>
<tr>
<th>Year</th>
<th>Bank</th>
<th>Share (%)</th>
<th>Foreign Entrant</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>Demirbank</td>
<td>100</td>
<td>HSBC</td>
</tr>
<tr>
<td>2004</td>
<td>Koç Yatırım</td>
<td>50</td>
<td>Unicredito Italiano</td>
</tr>
<tr>
<td>2005</td>
<td>Yapı Kredi</td>
<td>57</td>
<td>Koç-Unicredito</td>
</tr>
<tr>
<td></td>
<td>Garanti</td>
<td>26</td>
<td>GE Capital Corporation</td>
</tr>
<tr>
<td></td>
<td>Dişbank</td>
<td>89</td>
<td>Fortis</td>
</tr>
<tr>
<td></td>
<td>Türk Ekonomi</td>
<td>50</td>
<td>Bank Paribas</td>
</tr>
<tr>
<td>2006</td>
<td>Finansbank</td>
<td>46</td>
<td>National Bank of Greece</td>
</tr>
<tr>
<td></td>
<td>Denizbank</td>
<td>75</td>
<td>Dexia Participation Belgique</td>
</tr>
<tr>
<td></td>
<td>Şekerbank</td>
<td>34</td>
<td>Bank Turan-Alem</td>
</tr>
<tr>
<td></td>
<td>Tat Yatırım</td>
<td>99</td>
<td>Merrill Lynch European</td>
</tr>
<tr>
<td></td>
<td>Bankpozitif</td>
<td>58</td>
<td>Bank Hapoalim BM</td>
</tr>
<tr>
<td>2007</td>
<td>Akbank</td>
<td>20</td>
<td>Citigroup</td>
</tr>
<tr>
<td></td>
<td>Oyak Bank</td>
<td>100</td>
<td>ING</td>
</tr>
<tr>
<td></td>
<td>Tekfenbank</td>
<td>70</td>
<td>Eurobank EFG</td>
</tr>
<tr>
<td></td>
<td>MNG Bank</td>
<td>91</td>
<td>Bank Med</td>
</tr>
</tbody>
</table>

*Source: TBB Annual Reports*

Finally, the nature of foreign exposure and risk has changed. In the 1990s many Turkish commercial banks were arbitrage-oriented; they relied on relatively low interest, short-term foreign flows to take advantage of high interest but longer-maturity
government papers. After the crisis, the BDDK’s rigid enforcement of open position limits and the much longer maturities as well as lower yields of public securities prohibited that option. Given that structural restraint, and with increased investor confidence in Turkish markets, commercial banks turned from short-term to long-term foreign loans, especially from 2004 onwards (Table 6.6). But a quick glance at Turkey’s financial account provides other important clues about the recent transformation of Turkey’s financial integration. First, even though foreign capital still seems to be significant for the country’s growth prospects, the weight has now shifted from speculative inflows to foreign direct investment and longer-term loans. Second, banks no longer seem to be the engine of financial integration; “other sectors” (that is, commerce and particularly industry) managed to draw three times as much foreign capital than banks in 2006, and nearly five-times as much in 2007. Much of this influx is based on long-term loans, but even then, it appears the main risk factor due to foreign financial exposure in Turkey is no longer the banking sector per se. Furthermore, it is widely known that it is the big industry which grabs the lion’s share of this increased availability of foreign funds, which in turn diminishes its reliance on the domestic system that lends at higher rates. This development is cause for concern for the whole sector, and given the projected fall in securities income, it further stokes the competition for patronage of small and medium size enterprises and individual clients.

This structural transformation of Turkey’s banking sector was not unexpected. What is important for the purposes of this study is that it was by and large the outcome of

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45 Consider these remarkably accurate predictions of Alper, Berüment and Malatyali (2001, 93), written during the crest of the crisis: “With the successful completion of the currently revised stabilization program, investment horizons will be lengthened; arbitrage gains and high net interest margins will be eliminated. Banks will have to switch to noninterest income-related activities and have to generate
sweeping institutional innovations designed by insulated technocrats and later successfully defended by politicians despite a more negotiative environment. In the end, incentive structures for market behavior changed and actors were forced to adapt. International considerations were the guiding force in that process at multiple points. It was an unfeasible pattern of integration that brought the system to its knees, and yet salvation came in the form of strict adoption of emergent global norms and practices through cooperation with and compulsion from international agencies. A few years after the crisis, the synergy between novel institutions and nondomestic considerations is stronger than ever. Since 2004 BDDK pushes for the adoption of Basel II principles; a road map for transition was published in 2005 (BDDK 2005), and particularly after the EU’s Basel II-based Capital Requirements Directive (CRD) in 2006, work on harmonization with new standards has accelerated in consultation with sector representatives. Meanwhile rapid foreign entry into the system has entailed regulatory

sustainable sources of fee-based income. Compared to the environment when public sector borrowing requirement was high and the existing banks did not have to compete with each other for asset management, economies of scale will be an important issue. Consolidation within the sector will be taking place and small banks will not be able to survive. Foreign banks will also need to grow in size to be able to compete with large banks in retail banking through, most probably, mergers and acquisitions.”

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vigilance. BDDK had to oversee numerous mergers and acquisitions, and with increasingly complex capital structures and banking operations it now has to fortify its organizational capacity to be able to enforce evolving rules, ensure a level playing field for all actors, and manage risks to the rest of the economy. As such, a retreat from the institutional path that opened up after 2001 remains immeasurably unlikely.

### 6.3 Agriculture: Transplantation and Subversion

I have argued in chapters four and five that the persistence of preliberal forms of market governance in Turkish agriculture rested on two distinct and dynamic types of institutional accommodation. *Insulated accommodation* of the early 1980s dissociated corporatist state intervention from rural populism. Under neoliberal austerity, the antiquated support regime ceased to serve as an instrument of income transfer to the countryside; instead, it was redeployed as a tool for income repression. This was followed, from the late 1980s onward and throughout the 1990s, by a pattern of *negotiated accommodation* through which populism and corporatism were recoupled. Intense democratic competition entailed the restoration of the original redistributive functions of the support regime and turned around the fortunes of the Turkish peasant.

What made accommodation a feasible strategy for both the technocratic reformers of the 1980s and the populist politicians of the 1990s was the absence of strong nondomestic incentives for sectoral reorganization. The crisis changed that picture radically. With the rise of a new generation of insulated technocrats came an impetus for sweeping institutional innovation in the spirit of emergent global norms of agricultural
governance. But negotiati ve constraints and distributive pressures after 2003 precipitated a partial retreat from this reformist path. Before novel institutions could consolidate, older arrangements resurfaced. Turkish policymakers have since settled on a hybrid support regime that blends older and newer elements.

**Insulated Innovation: Novel Institutions**

Of the three cases of insulated innovation explored in this study, the reform of the support regime constitutes the most radical example of that type. We have seen in the previous chapter that, even though reforms in the US and the EU in the 1990s made Turkey’s age-old support regime look increasingly out of date, this normative shift had no tangible impact, given the significance of domestic distributive concerns during that decade, the successful adaptation of corporatist interventionism to neoliberal policy constraints, but most important, due to the limited repercussions of the Uruguay Round Agreement on Agriculture (URAA) for Turkey’s support policy and the weight of less liberal EU markets in the international exposure of the sector. Yet, the less reversible the shift in the international policy wisdom in agriculture appeared, the stronger and more coherent the neoliberal-technocratic opposition to old support instruments became. While critics of the support regime in the mid-1990s were still focused on ways to improve the system from within (e.g., Yener at al. 1996), in a few short years there emerged a broad consensus on the need for brand new institutional designs, such as direct payments (e.g., Yükseler 1999). All the fiscally-conscious, efficiency-oriented neoliberal bureaucrats needed to move in on populist corporatism was a reformist window of opportunity.
As in the case of finance, it was the IMF-led stabilization program that provided such an opening. The December 1999 Letter of Intent placed special emphasis on the dismantling of prevailing subsidy schemes. During the same month, an Agricultural Restructuring and Support Council was formed, involving representatives from some half dozen public agencies, plus the TZOB. Yet, to be expected, it was the Treasury, through its small but highly influential Directorate of Agriculture, that took the lead in devising a master plan for replacing the existing support framework with a new, fiscally sustainable regime. In that massive undertaking it received generous technical, and eventually financial, assistance from the World Bank. The Agricultural Reform Implementation Project (ARIP) of the bank, announced in June 2000, was designed to help the Turkish government meet its goal of “dramatically reducing artificial incentives and government subsidies” (World Bank 2001c, 4). The bank staff reported that “the reforms to be implemented [were] necessary for fiscal stabilization” (ibid.), and endorsed the project with a US$600 million loan.

ARIP had four components. First, in the place of support purchases and input subsidies that were now being phased out, and primarily as a transitory social safety net, a Direct Income Support (DIS) regime was instituted. DIS payments would be allocated on a per hectare basis (roughly about $80/ha in its first year), and were introduced as ‘decoupled’ from the crop or the yield. To facilitate the precise targeting of payments, the project also called for putting together a farmers’ registry system. Second, in order to combat overproduction in some cash crops (most notably in hazelnuts and tobacco) the project endorsed one-time payments to encourage farmers’ transition to alternative crops. Among the crops promoted were corn, oilseeds and feedcrops. Third, ARIP proposed a
sweeping organizational reform of the agrobureaucracy. This included the privatization of the remaining agricultural state enterprises and the restructuring of regional sales cooperatives. Finally, the project had a support services component, which also involved a public information campaign to garner social support for reform.

This radical reform initiative was the epitome of what Peter Evans (2004) has called “institutional monocropping.” It attempted to transplant a system of US-style direct payments as a temporary substitute for the entire range of classic support mechanisms. It pressed for replacing the cultivation of regionally well-established crops with alien ones on the basis of pure market rationality. And it attacked the very foundation of rural corporatism by proposing to sever the historic ties between the political center and the network of farmers’ organizations.

While implementation started via pilot projects in 2000, the reformist tide that followed the 2001 crisis provided an even more opportune environment for top-down transplantation. In 2001-2002, the DIS regime gained regularity. Input and credit subsidies were slashed. All direct transfers, although severely curtailed, were now covered in the general public budget. Sugar Law in 2001 and Tobacco Law in 2002 formed market-friendly regulatory agencies in these two key industrial crops that had represented the traditional strongholds of state intervention. In order to compensate for marketing problems that could arise from the withdrawal of state procurement, grain exchange boards were emphasized. Meanwhile, a number of agricultural SOEs were enlisted for privatization, and cooperatives, made ‘autonomous’ by a 2000 law, received capital injections against past losses for a fresh start.
From reformers’ perspective, initial results were promising. An interim World Bank report evaluating the implementation results of 2000-2002 declared that “[t]he agricultural subsidy reform program significantly contributed to fiscal stabilization”, meeting the most important objective of the plan (World Bank 2004b, x). Subsidy reform managed to cut fiscal outlays on agricultural transfers by US$ 5.5 billion, or about 2.7 percent of GDP. The authors of the report argued that the 13 percent decline in real agricultural prices (22 percent in comparison to non-agricultural prices) had to be interpreted as a major benefit for consumers. And although fertilizer prices increased sharply and real interest rates on agricultural credit rose from about -20 percent in the 1990s to +30 percent in 2001-2002, the DIS payments compensated for almost half the income loss incurred by farmers (ibid., xii). According to the study, Producer Support Estimate (PSE) declined from about 25 per cent in 1999 to 10 per cent in 2001—revised OECD data would set this figure further below, at a mere 4 percent.

But even at its early stages of inception, top-down reform ran into serious difficulties. One set of issues stemmed directly from design and implementation. First, the DIS regime lacked the necessary control mechanisms and thus was open to abuse. Most large landowners quickly devised ways to cheat the system, while some small farmers could not benefit from payments.46 Second, it created unanticipated consequences for the agricultural land and labor markets. Since payments were based on farm size, the regime at first pushed up land prices in some regions, with important social

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46 Landholders were eligible for DIS payments up to 50 hectares. Among those who own more, a widely known method of cheating the system was to re-register their land in the name of the members of the extended family at parcels under 50 hectares. It is also reported that some small owners found it difficult to enter the system because application fees often exceeded the payments for smaller farms (TKB 2004: 336).
implications. Third, some aspects of the alternative crop project were a textbook case of modernist failure with its disregard of the basic intertwining of social structures and production patterns. For instance, reforms promoted a switch from hazelnut farming to corn and soybeans in the Black Sea region. What the designers of the project did not take into account was that most hazelnut farmers were in fact urban dwellers in nearby towns and cities, visiting their land only a few times a year, mainly for inspection, maintenance, and harvesting purposes. The production cycles of the promoted crops, however, required that the farmer live on land. Farmers were not thrilled and did not follow up.

More important, agricultural reform met with intense suspicion and political resistance. From the day of its conception, ARIP never received tangible civic or political support, and was labeled as a predominantly technocratic initiative imposed from abroad (Çakmak and Akder 2005, 67). Elite commitment to reform remained thin even among the most vocal critics of economic populism. Farmers’ organizations had difficulty in adjusting to the new legal framework and attempted to continue operating in their usual politicized patterns, while also attacking the program publicly. Quasi-corporatist professional associations were at the forefront of public criticism. TZOB charged that “the abandoning of all supports and the transition to DIS is to consent to the destruction of the sector” (TZOB 2003, 262), while the head of ZMO argued that the new regime

47 The DIS system favors land-intensive crops, such as cereals, in which larger farms collect larger payments. There are strong indications that this caused severe problems especially in Eastern and Southeastern Anatolia where sharecropping arrangements were common. Reportedly, many big landowners broke tenancy contracts to benefit from cash payments themselves rather than letting sharecroppers become eligible (Interview at the TZOB with anonymous director, 12 August 2004).

48 Interview, General Director (Anonymous), the Ministry of Agriculture and Rural Affairs, 20 August 2004. By 2003, a mere 580 hectares of about 550,000 hectares of the total hazelnut area made the switch, and only 452 producers were eligible for payments. The official explanation for this failure of the transition program was farmers’ concerns about price volatility due to the restructuring of the regional hazelnut cooperative (Fiskobirlik). Ironically, the 2008 World Development Report cites Turkey’s failed farmers’ transition program as a potentially viable measure to assist production shifts (2007, 114).
would “aggravate the misery of producers” (Günaydın 2002, 63). There was ‘sub-rosa resistance’ (Allina-Pisano 2004) from within the state as well, revealing just how deep were the mental fissures between the core organizations of economic governance and the agricultural machine operating in the background. For instance, the Ministry of Agriculture at first protested the project, but later returned to the bargaining table with proposals to rush the reform process, probably expecting to expose its faults in its infancy. The Ministry of Industry and Trade, on the other hand, conducted tough negotiations with the Treasury to preserve its hold over cooperatives and expand its influence within the new regulatory boards. The project was a major source of bureaucratic infighting.

With insulated, technocratic reformism in high gear, neither problems of implementation, nor societal opposition and intra-state reluctance mattered. The government’s resolve to see through agricultural subsidy reform was repeated in all twelve IMF Letters of Intent between December 1999 and the summer of 2002. Most of these documents involved stipulations regarding the legislative and organizational timetable for the reform process and made clear commitments about support prices and the fate of other subsidy instruments in accordance with fiscal projections. By the time the AKP came to power, and in terms of the extent of institutional change effected, the Treasury- and World Bank-led agricultural reform had made at least as much progress as banking reform, and was several steps ahead of public financial restructuring.

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49 Interview, Director (Anonymous), the Undersecretariat of Treasury, 24 August 2004.
Despite various hurdles, agricultural reform pushed forward without major setbacks in its early years. The November 2002 elections put an end to this prelude. The AKP’s approach to subsidy reform reflected a strategy of opportunistic dualism. On the one hand, the party, whose ranks already abounded in reform skeptics, would find it vital to dilute the process and bring back older instruments as part of its global effort to expand its support base from urban to rural poor. On the other hand, it did so slowly and cautiously, with continuous bargains with the IFIs and without putting the fiscal balance at risk. Most crucial, rather than a radical repudiation of novel arrangements, reform subversion took the form of tactical compromises between older and newer instruments. The outcome has been a hybrid institutional regime, granting policymakers access to an enhanced, flexible policy repertoire, which is also open to further innovations due to its simultaneous exposure to both societal pressures and international norms.

The fast pace of economic recovery in 2003 and the approaching local elections of 2004 were the immediate catalysts for the AKP to reconsider the support policy. Good yield in grains in 2004 provided a good excuse for sizeable state procurement, up from around 700 thousand tons in 2002 and 600 in 2003 to over 2 million tons, bringing the wheat stocks of the Turkish Grain Board (TMO) to three million tons. The backpedaling from the founding principles of the subsidy reform only accelerated in 2005. Grain procurement reached 4.8 million tons that year, a record since 1999 and close to the 1990s’ average. Furthermore, the government introduced fertilizer and diesel fuel subsidies. A debt write-off scheme took effect against interest accumulated on

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50 Interview, Department Head (Anonymous), the Undersecretariat of Treasury, 22 December 2004.
Table 6.7  Agricultural Supports (2000-2007) (US$ Millions)

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market Price Support</td>
<td>5,365.7</td>
<td>-14.8</td>
<td>4,357.7</td>
<td>8,739.6</td>
<td>9,010.0</td>
<td>9,623.6</td>
<td>6,780.2</td>
<td>8,665.2</td>
</tr>
<tr>
<td>Payments Based on Output</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cotton Premium</td>
<td>273.8</td>
<td>195.6</td>
<td>92.9</td>
<td>116.5</td>
<td>157.3</td>
<td>340.9</td>
<td>395.4</td>
<td>635.9</td>
</tr>
<tr>
<td>Wheat Premium</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>138.1</td>
<td>329.5</td>
<td>466.8</td>
</tr>
<tr>
<td>Payments Based on Input Use</td>
<td>823.9</td>
<td>242.3</td>
<td>215.7</td>
<td>222.0</td>
<td>321.8</td>
<td>401.5</td>
<td>888.4</td>
<td>1,023.0</td>
</tr>
<tr>
<td>Concessional Loans</td>
<td>463.4</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
<td>7.0</td>
<td>26.9</td>
<td>102.0</td>
<td>172.9</td>
</tr>
<tr>
<td>Fixed Capital Formation</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Livestock improvement</td>
<td>6.0</td>
<td>33.5</td>
<td>45.8</td>
<td>44.9</td>
<td>60.5</td>
<td>104.4</td>
<td>312.3</td>
<td>365.7</td>
</tr>
<tr>
<td>Livestock development project</td>
<td>19.2</td>
<td>33.5</td>
<td>45.8</td>
<td>45.5</td>
<td>66.8</td>
<td>133.5</td>
<td>361.3</td>
<td>404.1</td>
</tr>
<tr>
<td>Direct Income Support</td>
<td>0.0</td>
<td>68.3</td>
<td>1,246.2</td>
<td>1,560.3</td>
<td>1,743.8</td>
<td>1,755.1</td>
<td>1,879.7</td>
<td>1,955.4</td>
</tr>
<tr>
<td>Marketing and Promotion</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Duty Losses</td>
<td>1,937.3</td>
<td>1,645.7</td>
<td>365.1</td>
<td>198.4</td>
<td>133.5</td>
<td>106.7</td>
<td>130.0</td>
<td>178.3</td>
</tr>
<tr>
<td>Debt Write-Off</td>
<td>1,106.3</td>
<td>910.7</td>
<td>1,410.5</td>
<td>435.3</td>
<td>123.7</td>
<td>1,206.0</td>
<td>136.3</td>
<td>132.2</td>
</tr>
<tr>
<td>Equity Injections</td>
<td>245.3</td>
<td>252.2</td>
<td>71.7</td>
<td>128.6</td>
<td>76.6</td>
<td>41.8</td>
<td>1,087.3</td>
<td>46.1</td>
</tr>
<tr>
<td>Transfers to ASCUs</td>
<td>360.7</td>
<td>288.9</td>
<td>87.7</td>
<td>96.4</td>
<td>193.3</td>
<td>202.1</td>
<td>150.2</td>
<td>163.7</td>
</tr>
<tr>
<td>PSE</td>
<td>6,565.5</td>
<td>770.6</td>
<td>5,958.5</td>
<td>10,750.7</td>
<td>11,396.6</td>
<td>12,614.9</td>
<td>10,810.2</td>
<td>13,438.0</td>
</tr>
<tr>
<td>Percentage PSE</td>
<td>20.2</td>
<td>3.5</td>
<td>21.7</td>
<td>28.4</td>
<td>26.1</td>
<td>25.3</td>
<td>20.3</td>
<td>21.5</td>
</tr>
<tr>
<td>TSE (% GDP)</td>
<td>5.2</td>
<td>2.7</td>
<td>4.4</td>
<td>4.9</td>
<td>4.0</td>
<td>3.9</td>
<td>3.1</td>
<td>2.8</td>
</tr>
</tbody>
</table>

Source: OECD Producer and Consumer Support Estimates Database (online)
default credits and unpaid electricity. Concessional loans resumed. Cotton premiums were doubled. And for the first time, premium payments on grains were announced, in addition to both existing support purchases and the now regularized DIS payments. After a few years of experimentation, old support instruments, albeit in bits and pieces, were back in the village, operating side by side with a novel institutional framework.

Table 6.7 illustrates the outcomes of reform reversal. Most striking here is the quick recovery of market price supports (MPS). The sharp increase in PSE levels after 2002, but especially from 2003 onward, seems to have ridden largely on this one instrument that is considered the most market-distortive. Much of that increase has stemmed from standard MPS commodities, including wheat, sugar beets, and beef, as shown in Table 6.8. The substantive price effect of this trend can be traced from Table 6.9. Compared to the previous record year of 1998 which represented the peak of rural populism, prices received by farmers relative to GDP deflator slumped by some 15 percentage points as of 2001, but quickly climbed thereafter to reach new record levels in 2003 and 2004. The rural price depression of the second round of neoliberal reforms was thus shorter-lived.

Table 6.8  
*Fall and Rise of Support: Single Commodity Transfers (STCs) as Percentage of Value of Production (2000-2007)*

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wheat</td>
<td>18</td>
<td>-6</td>
<td>12</td>
<td>39</td>
<td>21</td>
<td>33</td>
<td>25</td>
<td>31</td>
</tr>
<tr>
<td>Sugar</td>
<td>55</td>
<td>28</td>
<td>48</td>
<td>61</td>
<td>63</td>
<td>56</td>
<td>25</td>
<td>55</td>
</tr>
<tr>
<td>Beef</td>
<td>52</td>
<td>44</td>
<td>53</td>
<td>61</td>
<td>53</td>
<td>51</td>
<td>44</td>
<td>46</td>
</tr>
</tbody>
</table>

*Source: OECD Producer and Consumer Support Estimates Database (online)*
Table 6.9  
Fall and Rise of Prices: Prices Received by Farmers as Percentage of GDP Deflator (1998 = 100)

<table>
<thead>
<tr>
<th>Year</th>
<th>1998</th>
<th>1999</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>100</td>
<td>97.81</td>
<td>92.95</td>
<td>84.68</td>
<td>91.07</td>
<td>101.15</td>
<td>103.06</td>
</tr>
</tbody>
</table>

Source: Author’s own calculations from TÜİK (2007). Original data takes 1987 as benchmark.

It is important not to confuse this resurfacing of old support instruments with the pattern of ‘restoration’ that characterized the 1990s. While restoration involved a functional return to populism with some adjustments to institutional forms in place, the AKP’s counterreform has been more acceptive of emergent instruments and principles. The new DIS regime appeared to have found a stable niche by mid-decade. Price supports were no longer financed through duty losses, even though there were sizeable operational costs. There has been more emphasis on comparatively ‘modern’ support instruments such as ‘payments based on output’, essentially, ‘coupled’ deficiency payments. Meanwhile, generous livestock supports of recent years reflect a policy strategy aimed at correcting the grain-producer bias of rural populism in the previous decades. In short, while rural redistribution has resumed, novel arrangements have also gained ground.

Finally, the Agricultural Law of 2006 sealed the transition to a hybrid support regime (Resmi Gazete, 25 April 2006). The law represented a compromise between old and new support instruments and introduced a framework flexible enough to accommodate a variety of policy needs. On the one hand, it cast the DIS system into law by making it the primary support instrument. It also set a low minimum support ratio for

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51 The problem in 2005 was extensive debt write-offs mentioned earlier, and in 2006 it was the collapse of Fiskobirlik, the hazelnut cooperative, to be introduced briefly later.
starters—no less than one percent of the GNP. On the other hand, it adopted a much more diversified support framework, including the European-style deficiency and compensatory payments as well as livestock, insurance, and rural development supports. It also officially brought back older subsidy instruments under a separate article on “other support payments”, which as stipulated could be used toward any input and marketing supports. In essence, the law symbolizes the unwillingness of the government to limit the scope of its policy repertoire by over-commitment to any one paradigm of support.

How are we to account for the hybridization of the support regime? Like other instances of institutional reshaping analyzed thus far, hybridization too involves a certain balance between domestic and international considerations. On the domestic side, it represents the culmination of a spirit of *negotiation* with societal interests and intra-state actors. This in turn has implications for both rural populism and the design of market intervention. On the international side, it represents a rather problematic openness to *innovation*. Here, unlike in finance, patterns of market integration and exposure to evolving global and regional norms pull in opposite directions.

The partial defeat of agricultural reform could be viewed in the context of a renewed appreciation in policy circles of an old belief—that the overwhelming majority of Turkey’s rural producers cannot meaningfully partake in the political system unless they are at the receiving end of a generous system of side-payments. When democratic channels are open, the ‘populist contract’ easily reasserts its attractiveness. With around 30 percent of the workforce still employed in agriculture, distributive concerns continue to carry considerable political weight. Besides, the sector contributes less than 10 percent of the GDP today. Double or even triple the current legal minimum support ratio (that is,
two to three percent of the GDP) is not fiscally far-fetched. Consider, for instance, the sharp contrast between PSE and TSE levels: from 2000 to 2007 producer transfers doubled, from around US$6.5 billion to over US$13 billion, and yet total support estimate, measured in GDP terms, was nearly halved, from 5.2 to 2.8 percent. In short, not only does rural populism remain politically enticing, but it is now economically much more feasible. No democratic, negotiative political project can ignore this point.

Things are different for rural corporatism. Here, the web of politically-supervised interest associations operating in tandem with large state enterprises had proved an adaptive institutional formula for rural market governance. There are growing constraints, however. For many crops, the main historic factor of resilience behind rural corporatism, that is, market engendering, is no longer as justified. The shedding of some enterprises in the 1990s and the legal ‘autonomization’ of cooperatives under ARIP have also weakened the immediate hold of the political center over some parts of the sector. Thus, the will to stick with the corporatist machine is strong, but its scope is irrevocably narrowing down, and some of the organic linkages it used to embody between different actors now need to be reconstructed, perhaps at a more informal level.

An interesting example that illustrates the difficulties of rearranging the state’s role in agricultural markets is the collapse of the hazelnut cooperative, Fiskobirlik. Turkey accounts for around 70 percent of world hazelnut production each year, and an estimated 400,000 families, exclusively in the Black Sea region, rely on this strategic crop that contributes about 30 percent of Turkey’s agricultural exports. As in almost all other industrial and cash crops, hazelnut farmers too were organized under a quasi-public sales cooperative, Fiskobirlik, which had executed the government’s support policy
through a thick agrobureaucratic network since 1938. Prices were administered centrally, and given Turkey’s dominant position in world markets and with millions of votes at stake, they had been inflated for decades. This attracted more farmers into the subsector and triggered an expansion of the hazelnut area, in time leading to persistent overproduction. This structural problem was the driving force behind the inclusion of hazelnut in the alternative crop project.

The architects of ARIP had expected that the ‘autonomization’ of Fiskobirlik with the 2000 Cooperatives Law would lead to a market-based rationalization of hazelnut production. They assumed state withdrawal would curtail central political incentives for high prices, and the market would self-adjust, with a slight nudge from the alternative crop project, for overproduction. Instead, Fiskobirlik executives, now freed from government control and eager to please their member base, pushed up prices and began amassing debts to Ziraat and other banks. Finally, in 2006, the cooperative went bankrupt and was unable to pay farmers toward past years’ purchases. Faced with growing and at times violent social unrest in the region, the government reluctantly stepped in and assigned the TMO, the state enterprise for grains, with hazelnut procurement by using Fiskobirlik’s extensive infrastructure. In short, the attempt to eliminate indirect state control over the subsector produced a crisis that could only be resolved through introducing direct state control. Even when providers of rural side payments are willing to change the rules of the game (and this is not to say that the AKP or any other party would not wish to wield influence in these organizations, perhaps through informal channels of patron-clientelism), it is uncertain how ready and willing the historic
recipients and interlocutors of these payments are to remodel their market behavior and policy expectations on a novel, alien vision of the world.

Table 6.10  
*Turkish Agriculture: Output and Export Shares (2000-2007)*

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Turkish Agriculture in Turkish Economy</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>% Turkish GNP</td>
<td>12.2</td>
<td>11.9</td>
<td>12.2</td>
<td>11.4</td>
<td>10.7</td>
<td>10.6</td>
<td>10.0</td>
<td>8.9</td>
</tr>
<tr>
<td>% Turkish Exports</td>
<td>6.0</td>
<td>6.3</td>
<td>4.9</td>
<td>4.5</td>
<td>4.2</td>
<td>4.7</td>
<td>4.2</td>
<td>3.6</td>
</tr>
<tr>
<td>Export Share/Output Share</td>
<td>0.49</td>
<td>0.53</td>
<td>0.40</td>
<td>0.39</td>
<td>0.39</td>
<td>0.45</td>
<td>0.42</td>
<td>0.40</td>
</tr>
<tr>
<td><strong>Turkish Agriculture in World Agriculture</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>% World Agr. Output</td>
<td>2.47</td>
<td>1.55</td>
<td>1.87</td>
<td>2.19</td>
<td>2.33</td>
<td>2.42</td>
<td>2.22</td>
<td>n/a</td>
</tr>
<tr>
<td>% World Agr. Exports</td>
<td>0.69</td>
<td>0.77</td>
<td>0.67</td>
<td>0.75</td>
<td>0.80</td>
<td>0.95</td>
<td>0.92</td>
<td>n/a</td>
</tr>
<tr>
<td>Export Share/Output Share</td>
<td>0.28</td>
<td>0.50</td>
<td>0.36</td>
<td>0.34</td>
<td>0.34</td>
<td>0.39</td>
<td>0.41</td>
<td>n/a</td>
</tr>
</tbody>
</table>

*Source:* TÜİK (online) and author’s own calculations from WB-World Development Indicators Online and WTO-Statistics Database (online). Turkish figures are at 1998 constant TL prices; world figures are based on current US$.

This brings us to the other dimension of hybridization, that is, its innovative content driven mainly by international considerations. At that level, and as was the case for Turkish finance during the late 1990s, the market and policy dimensions of the process pull in different directions. Trends have not changed much in terms of market exposure. The decline in the export significance of the sector continues apace, and so does the traditional imbalance in its share in world exports compared to its share in world output (Table 6.10). And after a few years of relative convergence on international prices around crisis years, high domestic prices are back. The OECD has calculated that in 2004-2006 prices received by Turkish farmers were on average 28 percent higher than world prices (2007, 223). The situation is worse in standard market price support commodities that concern the largest number of peasant farmers, with prices for sugar
beets in 2005 and wheat in 2007 realizing at a whopping 60 percent above world prices (Table 6.11). Thus, as was the case in the 1980s and the 1990s, Turkey’s defensive position in international markets provides little, if any, incentive for change in the governance of its agriculture. Once the single most important source of the country’s foreign exchange earnings, the sector is now verging on autarky relative to industry and finance.

Table 6.11  World Prices vs. Turkish Support Prices: Wheat and Sugar Beets (2000-2007) (Current US$ / ton)

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Wheat</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>World Export Price (FAO)</td>
<td>120.9</td>
<td>126.8</td>
<td>127.1</td>
<td>146.5</td>
<td>162.4</td>
<td>146.5</td>
<td>n/a</td>
<td>n/a</td>
</tr>
<tr>
<td>World Price (OECD)</td>
<td>126.6</td>
<td>125.2</td>
<td>160.0</td>
<td>155.6</td>
<td>151.2</td>
<td>168.2</td>
<td>204.0</td>
<td>204.5</td>
</tr>
<tr>
<td>Turkey Support Price</td>
<td>163.5</td>
<td>133.8</td>
<td>152.7</td>
<td>217.7</td>
<td>260.5</td>
<td>261.0</td>
<td>262.0</td>
<td>326.5</td>
</tr>
<tr>
<td><strong>Sugar Beet</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>World Export Price (FAO)</td>
<td>89.6</td>
<td>62.2</td>
<td>65.9</td>
<td>54.0</td>
<td>60.4</td>
<td>47.8</td>
<td>n/a</td>
<td>n/a</td>
</tr>
<tr>
<td>Turkey Support Price</td>
<td>57.4</td>
<td>40.3</td>
<td>52.1</td>
<td>63.5</td>
<td>75.5</td>
<td>76.8</td>
<td>n/a</td>
<td>n/a</td>
</tr>
</tbody>
</table>

Source: FAOSTAT (online); OECD.Stat (online); TÜİK (2007).

Whatever innovative impulse exists today, then, comes neither from domestic political projects nor from patterns of market integration, but from exposure to external policy pressures that reflect evolving international norms. While populist corporatism can still connect together mass and elite, political and economic, and central and peripheral interests involved in Turkish agriculture around a time-honored redistributive ethos, it is increasingly challenged by dominant global ideas as to what rural market governance should look like. For instance, both the OECD and the EU have already expressed
concern about the revival of classic support schemes.\textsuperscript{52} Of particular concern is that the re-institutionalization of rural populism generates MPS levels well beyond Turkey’s 10 percent \textit{de minimis} commitment to the WTO in a number of strategic crops. While breaching that commitment and effectively moving toward ‘amber box’ supports in recent years, Turkish policymakers have been taking advantage of the current impasse in agricultural trade talks. Whether such high support levels via old instruments could be sustained in the event of an agreement is highly doubtful. The preservation of some components of reform as part of the wider policy repertoire, especially of the decoupled DIS regime, therefore emerges as an immoveable design constraint for Turkish agricultural governance in the medium run.

The EU process further complicates the normative picture.\textsuperscript{53} On the one hand, piggybacking on the EU’s comparatively less enthusiastic stance on agricultural liberalization expands Turkey’s options in domestic support policy. Unlike Mexico vis-à-vis American corn, the Turkish market is not threatened by cheap wheat imports from France or Germany; in staples its relation to European markets is closer to South Korea’s relation to Japanese markets, and is governed by a strong principle of ‘mutually assured survival’ for domestic producers. On the other hand, prospects of EU integration also fuel the demand for change. For instance, the government’s Agricultural Strategy Document for 2006-2010, which formed the basis for the 2006 law, places special emphasis on harmonization with EU legislation. The formidable challenge here is not the level of support, but to reorient the scope of the institutional framework from a narrow focus on

\textsuperscript{52} See the 2006 OECD Country Survey of Turkey (OECD 2006, 17ff) and the EU Progress Report of November 2007 (Commission of the European Communities 2007, 44).

\textsuperscript{53} On the agricultural implications of Turkey’s potential EU accession, see Çakmak (2004); Çakmak and Akder (2005); Togan, Bayaner, and Nash (2005); and in particular the collection by Burrell and Oskam (2005).
price incentives and cash transfers to include a broader range of issues such as insurance schemes, organic farming, health and sanitary standards, environmental protection, and rural development. These are policy areas with which Turkey’s agricultural bureaucrats are not sufficiently familiar and where there is very little institutional capacity. This pressing need to diversify the support regime has had implications for the World Bank constraint as well. Once the battle over unalloyed reform compliance was lost, ARIP was amended in 2005 to redirect its remaining funds to finance a rural development program that involved land consolidation, strengthening of cooperatives, and village-based participatory investment (World Bank 2005b). This expansion of support objectives also requires substantial bureaucratic reorganization, which in itself is a source of innovation.

The support budget, for example, has now shifted out of the Treasury and been tied directly to the Ministry of Agriculture. This is a major boost for the organization, but it also empowers a more technical, project-oriented policy agenda rather than an overemphasis on conventional side-payments. Likewise, in the context of institutional harmonization with the CAP, there is a master plan in progress to restructure the TMO as a payment agency to single-handedly coordinate all state intervention in agricultural markets. Meanwhile private companies, domestic and foreign, continue to move into subsectors that have been partly or fully vacated by state agencies, creating a need for regulatory improvements, again along EU lines, to address new phenomena such as contract production. In brief, the ‘governance’ of the sector is getting increasingly complex, and populist corporatism, in its conventional forms, is hardly up to that task. A more proactive approach and a commitment to novelty are indispensable.
This perhaps should be our principal conclusion as to the institutional significance of top-down reform and its partial subversion in Turkish agriculture. Certainly conversion and restoration also involved both formal and functional changes in the support regime. But transplantation and hybridization, as a result of the innovative content of both patterns of reshaping, have created an environment of dynamism comparable only to the early years of Turkish ISI. Within that general context of institutional malleability there is room for both further retreat from the reformist path but more so for further innovations. And unlike in finance where both fiscal and banking governance appears to have settled on rigid principles of fear-based restraint and institutional isomorphism, in agriculture the urge to reconcile the historic political charm of rural populism with the global drive toward broader goals and better targeted instruments makes bold institutional adventures more likely.

### 6.4 Discordant Pathways, Redux

In chapters 4 and 5, we have seen how Turkey’s financial and agricultural regimes were reshaped along discordant paths throughout the 1980s and the 1990s. Innovative imperatives in finance and accommodative ones in agriculture generated different institutional outcomes in each sector. Postcrisis reforms appeared to have eliminated this basic sectoral variance: insulated technocrats imposed novel institutions upon both peasants and bankers. Yet the resumption of political competition after 2002 put an abrupt end to that common trajectory. New arrangements were rapidly consolidated in finance, whereas under similar constraints of competitive politics and exposure to
innovation-friendly international norms, agricultural reforms were partially repelled and old support instruments resurfaced. Why did insulated innovation lead to analogous institutional outcomes in these sectors but negotiated innovation to divergent ones?

The answer to this question lies in the sector-specific manifestation of the variables that make up these types of reshaping. For insulated innovation, the crisis of 2000-2001 appears to be an important intervening factor, which in both sectors amplified the salience of the two dominant variables behind this type: technocratic engineering and international norms. The practical bankruptcy of the Turkish state made the squabbling over the distribution of public largesse, which had formed the basis of coalition efforts of the 1990s, meaningless. By putting party rivalry over the allocation of public resources on hold, the crisis paved the way for heightened technocratic influence under lower levels of domestic political competition.

At the same time, the crisis provoked stronger external market and policy incentives for innovation along emergent sectoral norms. In finance, it not only exposed the dangers of unruly integration with international markets in full fashion, but also closed, at least temporarily, the Turkish market off to speculative inflows, thereby cutting the lifeblood of anti-reformist smaller and medium-sized banks. With every bank failure the status quo coalition lost an irreplaceable member and technocrats won a political victory. In agriculture, currency devaluation brought Turkish prices closer to world prices for a couple of years, undermining the legitimacy of market-distortive subsidy instruments. In terms of policy exposure as well, economic meltdown created an extreme dependence on the IMF and the World Bank, and tipped the scales in favor of externally-
inspired innovation via IFI-friendly technocrats. As such, the crisis revealed the potential synergy between international norms and technocratic reformism in its clearest form.

Yet the real puzzle is the varied outcome of negotiated innovation, under which the AKP government tried to reconcile the continued nondomestic incentives for innovation with the emergent political exigency to expand its coalitional base. Let us commence with the dynamics of coalition politics after 2003, which invariably favored peasants and disfavored bankers. It is analytically useful to distinguish between the intra-state versus the state-societal dimensions of this process.

Intra-state struggles are an important part of coalition politics in liberalizing countries. Many, including Turkey, have a long history of state-led development that nurtured a large segment of old-school bureaucrats. Under market reforms, the battle lines within the state are often drawn between traditional bureaucrats and the more liberally-oriented technocratic elements. In the Turkish context of 2000s, it was clear any infighting over fiscal and financial matters would be won by this latter group. Finance, writ large, constituted the natural turf of liberal, Western-minded bureaucrats who had long dominated the core organizations of the economic bureaucracy: the SPK, the Central Bank, and most important of all, the Treasury. Their position was further reinforced by the creation of another large agency with likewise leanings, the BDDK.

As mentioned in the discussion of Treasury reforms, the AKP emphasized the more traditionalist Ministry of Finance and the DPT over the liberal bureaucracy as part of its global effort to permeate the state machinery. While this move exacerbated pre-existing bureaucratic cleavages, it would have no discernible effect on institutional outcomes. For one, by 2003 both these organizations had moved toward a more or less
reformist outlook: the DPT took its task of coordinating the EU process very seriously, and the Ministry of Finance, at least its upper bureaucracy, rallied behind public expenditure reform. As the ideological rift between the two camps narrowed, the object of bureaucratic infighting shifted from the wider direction of change to a simpler one of expanding or defending existing organizational authority under innovative constraints. In the course of fisco-financial reforms, the bulk of bureaucratic conflicts of the post-2003 period concerned such matters as the status of sworn bank auditors in the BDDK, the role of budget specialists versus public auditors in the Ministry of Finance, the powers of the Treasury’s newly formed middle office, and so on. Intra-state cleavages, in short, were not of a type that could be exploited by bankers to escape tighter regulation. The entire Turkish economic bureaucracy, and at that point traditionalists perhaps even more so than liberals, were bent on reining in the unruly bankers.

Bureaucratic infighting was much more consequential for the remaking of the support regime. In agriculture, the ranks of liberal bureaucrats were extremely thin: a tiny Directorate of Agriculture within the Treasury, and some half-hearted support from the DPT. On the other side of the frontline were two huge spending ministries highly skeptical of the reform process, the Ministry of Agriculture and Rural Affairs (TKB) and the Ministry of Industry and Trade (STB). Unlike in finance, the ideational differences between these traditionalist and reformist camps in agriculture could not be reconciled. The head of Treasury’s Directorate of Agriculture, where ARIP was designed, felt that the Treasury staff did not “speak the same language” with their counterparts in these executive ministries, and could not even “agree on basic definitions and concepts.”

Meanwhile, a senior TKB bureaucrat would contend, “the ARIP stuff did not go… They

54 Interview, Department Head (Anonymous), the Undersecretariat of Treasury, 22 December 2004.
[Treasury bureaucrats] did not know what was involved." It is thus no coincidence that the accelerated resurfacing of old arrangements in 2005 followed the transfer of the support budget from the Treasury to the TKB. In sum, because bureaucratic struggles in agriculture concentrated on the general viability of reforms, their outcomes weighed heavily on institutional outcomes. Persistent intra-state opposition from the TKB and, to a lesser extent, the STB resulted in the dilution of reforms from above, which would then intersect with societal opposition from below to ensure partial reform subversion.

In terms of the state-societal dimension of coalition politics as well, rural and financial interests varied in their capacity to manipulate the direction of reforms under competitive politics. Part of this variation stemmed from the preferences of other actors, notably, the industry. Badly stung by the banking crises of 2000-2001, both big industry, organized within TÜSİAD, and smaller industrialists and commercial interests, organized within MÜSİAD and TOBB, emerged as strong supporters of banking restructuring. Bankers thus not only failed to find allies for the counterreformist cause among other elite interests, but faced forthright opposition. Rural transfers, however, were at best an indirect concern for these powerful groups. They did like the fiscal implications of the idea of subsidy reform and TÜSİAD even commissioned reports on agriculture; but when the AKP brought back older subsidies, and seeing the fiscally benign nature of this move, industrialists did not react at all.

Much more important for the varied effect of coalition politics for peasants and bankers was the intra-sectoral composition and political articulation of these interests. Rural interests have been well-organized, and acted as a unified front against agricultural

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55 Interview, General Director (Anonymous), the Ministry of Agriculture and Rural Affairs, 20 August 2004.
reform. They also managed, due to their electoral salience, to construct more direct relations with the AKP.\textsuperscript{56} At that level, there is a mix of old-style patron-clientelism and genuinely democratic interest group politics. Most members of the TZOB’s executive board, for instance, are pro-AKP and have strong parliamentary ties, but the 4-million member strong organization remains critical of the government’s position to stick even with a diluted form of ARIP, supporting opposition (including intra-party opposition) views instead. In the meantime, the Chamber of Agricultural Experts (ZMO), a very active left-leaning civil society organization with some 300,000 members, is staunchly anti-AKP and anti-ARIP. The AKP, as would any other mass party in its place, could not ignore this coordinated, grassroots counterreformism in agriculture. Besides, peasants make excellent partners in any political coalition; they deliver massively in votes, and demand comparatively little in return, which is not hard to accommodate with some fiscal care, especially today.

Here again, bankers have been at a political disadvantage and suffered classic collective action problems. The meltdown of 2000-2001 destroyed the center-right political establishment of the 1990s, and thereby washed away the hard-earned political privileges of the nascent financier class. Bankers tried to reassert themselves politically both during and after the crisis, but these efforts first hit the BDDK wall and then were

\textsuperscript{56} An interesting example was the debate over the new Union of Chambers of Agriculture (TZOB) Law. TZOB is Turkey’s largest professional and civil society organization with close to 4 million members. Historically it was the nerve center of rural corporatism; membership was mandatory for all farmers and the Union was tightly controlled by MARA. The bill, disclosed in 2003, granted autonomy to the Union in the spirit of ARIP, but it also provided it with new, generous sources of income: 0.3 percent of all grain board incomes, a 0.1 percent tax on all agricultural commodity transactions, and 0.25 percent of all DIS payments. From late 2003 to June 2004 when the bill was finally enacted, TZOB, which had opposed ARIP all along, adopted a much softer line and appeared to have supported AKP’s proposals to re-orient agricultural reform. Once the bill passed, however, it rapidly re-escalated its critical tone, and began attacking the AKP for pursuing the IMF line in its subsidy policy. The party took this as a major betrayal, and quickly amended the new TZOB Law, punishing the Union by taking away some of its new sources of income. It also redoubled its efforts to capture the local branches of the Union through its party network so as to bring in a more trustworthy leadership (Interview, TZOB, 12 August 2004).
largely ignored by the AKP, which picked its allies from the real sector. Even then, the TBB fought fiercely against both the TMSF’s harsh treatment of failed banks and the consolidation of banking reforms through the new law. But exactly how much organic support did it have from its membership? Public banks still had considerable weight in the system and, regardless of the potential discontent of their executives, could not go against the government. Meanwhile, some of the largest private commercial banks, such as Akbank and Garanti, were not particularly unhappy to see their smaller competitors with shady political connections wiped out by the crisis. And then there was the Koç factor, Turkey’s largest industrial group, which had openly endorsed postcrisis restructuring in its entirety and was entering the system in great style by gobbling up Çukurova’s failed Yapı Kredi with an Italian partner. Blatantly opposing the new law could sour this historic deal. Finally, for foreign banks entering a market that was yet recovering from a major crisis, a well-regulated environment was not exactly a deterrent. Consequently, even though all these different actors would in principle prefer a lower regulatory threshold, in the short run they could not unite behind that ‘collective good’ given their conjunctural interests. The TBB’s opposition received considerable public attention, but it is hard to imagine individual banks to have fought a comparably tough battle against the government and the BDDK behind the doors. Banks had not only lost much of their leverage within the political establishment and lacked any supporters within the bureaucracy, but they could not stand as a genuinely united force against reform consolidation either.

If the outcome of coalition politics affected institutional reforms in finance and agriculture differently, so did international norms, the second dominant force behind
negotiated innovation, both in their transmission into the domestic policy scene and their very character. A first intervening factor was patterns of market integration. As discussed extensively before, regulatory reforms in banking were seen as essential to mitigate the risks of further integration and also as a way to lure longer-term, non-speculative finance capital into the country. Agriculture continued to be lightly integrated with international markets, and protecting domestic producers against artificially low world prices remained an important function of the support regime.

A second factor was reform legacies (rather than institutional legacies) and technocratic preparedness. In finance, there was a strong legacy of externally-inspired reform, whereas in agriculture there was none. The 1990s, despite grave institutional failings, were also marked by various attempts to refurbish banking, central bank and capital market regimes in response to emergent challenges due to increased internationalization and often in line with evolving global norms—a process I have labeled ‘continuous adjustments’ in the fifth chapter. There was, then, an openness to innovation and an accumulation of reform experience within the financial bureaucracy. As a result, nondomestic incentives for reorganization, coming from market or policy pressures, were assessed at once and forcefully translated into policy. In sharp contrast, ideas for structural reform in agriculture were relatively new and there was no reform legacy whatsoever.\footnote{In fact, serious debate over structural reform in agriculture commenced only in the very late 1990s, in part as a result of the livened efforts of TKB’s Agricultural Economics Research Institute (AERI).} Agricultural reformers were inexperienced; they were receptive to institutional transplantation, but they were not prepared to withstand societal and intra-state opposition to reforms, especially when these were endorsed by the IFIs. Novel international ideas about rural market governance were transmitted, but could not be
successfully translated into the Turkish political-economic landscape.\textsuperscript{58} Given the lack of a legacy of change, internalizing the reformist impulse in agriculture proved an insurmountable challenge.

Finally, there is a fundamental difference between the nature of international policy and institutional norms to which Turkish agriculture and finance have been exposed. In finance, norms are highly cohesive and well-established. Central bank independence, NPM-inspired public expenditure management, and prudential regulatory and supervisory standards in banking have gained widespread acceptance among policymakers around the world. In this case, the IMF and World Bank have served as agents for the customized implementation of the type of reforms Turkey’s economic bureaucrats had long supported and international investors held in high regard. In agriculture, however, ideas of market-friendly rural governance are relatively new, and there is more confusion than consensus over their translation into policy and institutional frameworks, as exemplified by the continued stalemate in agricultural trade talks. As such, harmonization is limited, and apart from a loose emphasis on direct income supports, there are few ‘best practices’ to emulate. Furthermore, the Turkish position on the matter is by and large indexed to the European position, which not only represents a relatively cautious agenda of liberalization but also involves much broader targets than the conventional preoccupation with commodity prices, and in turn features an increasingly complex subsidy framework. Therefore, whereas the global norms that guide financial reforms are particularly strong, coherent, and enforceable by governments within the domestic economy, those that guide the reform of the support regime are more

\textsuperscript{58} See my discussion of the notion of institutional translation, referring to Campbell (2004), in the opening section of the second chapter.
diffuse and fluid, and often require active political enforcement upon governments at the international level, e.g. through the WTO’s dispute settlement mechanism.

To conclude, negotiated innovation led to different institutional outcomes for the postcrisis reshaping of Turkey’s financial and agricultural regimes, because the dominant forces behind that pattern, that is, coalition politics and international norms, had different implications for these sectors. The nature of intra-bureaucratic rivalry and a permissive sociopolitical context for interest articulation facilitated rural producers’ ability to manipulate the AKP’s coalition efforts in the way to give more voice to counterreformist initiatives; in finance, these very factors hampered bankers’ capacity to resist institutional restructuring. Likewise, the requisites of market integration and a strong technocratic legacy of institutional reform endorsed the emergence and consolidation of novel institutions in finance along nondomestic alternative designs inspired by highly cohesive and enforceable global norms; yet different values of these factors created a more tolerant atmosphere for the survival and re-emergence of old arrangements in agriculture.

The analytic implication, one that was mentioned before, must be clear. The typology does offer an explanation for institutional pathways, but not for resultant configurations. For this second task, one needs to go back to the founding variables of the given type and trace their context-specific values, manifestations and interactions in bringing about concrete institutional outcomes.
6.5 Building Institutions from Above

The postcrisis restructuring of the Turkish economy has been largely an IFI-led process. With a combined loan portfolio of more than US$50 billion since 1999, Turkey has been one of the biggest clients of the IMF and the World Bank in the 2000s. With such deep financial exposure came acute policy and normative exposure. Turkey’s recent reform efforts have closely mirrored the evolving development wisdom over the past decade, the hallmark of which is a preoccupation with institution building under an emergent “Post-” or “Augmented” Washington Consensus. Throughout this chapter, we have seen how intensely this revised, institution-centric framework impacted the reshaping of fiscal, banking, and agricultural regimes—via direct conditionality, but also by customizing and actively promoting novel ideas of sectoral governance in cooperation with Turkey’s willing technocratic reformers. In closing, we can ask what this reform experience could tell us about the practice and potential outcomes of this neoliberal institutionalist agenda.

Let us begin on a few positive notes. There is nothing defensible about an awkward, obsolete expenditure regime that precludes transparency in state finances, a system of debt management that prohibits long-term strategizing of deficit financing, or an underregulated financial sector that aggravates the vulnerability of the entire economy to external shocks. Turkey’s recent fiscal and financial reforms were instrumental in ameliorating these long-standing institutional flaws. Even for the staunchest critics of neoliberalism and IFI-led restructuring, these changes represent noticeable improvements.

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59 Between 1999 and 2005 the country signed three consecutive stand-by agreements and one supplemental reserve facility (SRF) with the IMF for a total amount of more than US$40 billion in current dollars, and in 2000-2008 its total loan amount with the World Bank was in the order of some US$13 billion.
over what had existed before. In agriculture as well, although reforms proved corrosive of peasant livelihoods and were soon partially subverted, top-down restructuring did energize the governance of the sector, forcing Turkish rulers to expand their policy objectives as well as repertoire.

Perhaps most important in both sectors, reforms led to extensive ‘modernization’ in state practice and helped build capacity. In developing country standards Turkey had a strong bureaucratic tradition (e.g. Heper 1976b), but it did not adapt well to the accelerated pace of social and economic change during the last quarter of the century. As a result, the Turkish state accumulated serious problems of “legibility” (Scott, 1998). It did not have a good handle on politicians’ newfound ways of public spending; it lacked strong monitoring powers over an increasingly complex banking system; it was unsure of the precise scale and beneficiaries of its rural transfers. In short, its knowledge of (both political and civil) society as well as of the outcomes of its own actions was increasingly fragmented. Postcrisis reforms did not fully resolve these problems, yet they did sharpen the Turkish state’s vision and capabilities. Today, bureaucrats have a firmer grip on public spending and deficit financing. Attempts to stray from fiscal discipline, as the AKP does habitually, are technically more difficult, and easier to detect and expose. In banking, new accounting, reporting, and disclosure standards keep actors on a shorter leash than before. In agriculture, the DIS system, which required putting together a national farmers’ registry, gave the state a more detailed ‘map’ of the production relations in the Turkish countryside. Thus, the Turkish state now ‘sees’ more. It also has more efficient instruments at its disposal to act on its surveillance.
But the record of financial and agricultural reforms also exemplifies some important shortcomings of neoliberal institutionalism. Chief among these is the problem of feasibility. The institutional turn has been criticized for promoting an overly comprehensive reform agenda (Grindle 2004; Rodrik 2006), which often entails transplantation of institutional blueprints with little consideration for their endogenous viability (Przeworski 2004; Evans 2004). On this point, the experience of fisco-financial restructuring is rather misleading. Even though top-down reforms seem to have succeeded in these areas, one should not lose sight of the exceptionally favorable circumstances involved: strong, coherent global and regional norms; patterns of market exposure conducive to institutional convergence; a natural receptivity to change riding on a long legacy of reforms; the predominance of experienced, reform-oriented bureaucratic elites in attendant public agencies; largely benign patterns of intra-state struggle; two successive governments with little opportunity for fiscal expansion and no sympathy for financiers; and finally, societal actors too deeply divided along their immediate interests to effectively influence the path of change.

Agriculture in that sense offers a better reality check for the feasibility of top-down reforms. Here, challenges have been more typical: somewhat weaker global norms; limited reform experience; stronger resistance from within the state; higher electoral stakes; and better organized collective interests. Under such conditions, difficulties of institutional transplantation come out vividly, from technical problems of implementation to unanticipated social consequences, and from bruising public opposition to political dilemmas encountered by incumbents. In such a setting novel institutions find themselves on tenuous ground, ever vulnerable to subversions from above and below. They prove
soft and malleable, and are easily permeated by older arrangements and habits. Earlier in this chapter I have provided other instances of this phenomenon, such as the hollowing out of the new public procurement regime, which is indeed a sticky point for the long-term fortunes of fiscal reforms, and the social security reform, whereby pre-existing policy parameters persisted. Besides, despite almost a decade of intense, IFI-led reforms,\textsuperscript{60} Turkey is yet to systematically tackle some important items on the “Augmented Washington Consensus” agenda, such as corporate governance and poverty alleviation. It is uncertain which problems lay ahead if the reformist impulse carries over to these areas. In a majority of sectors and policy areas, then, pure designer institutions may never take hold.

The ideals behind comprehensive institutional restructuring are as questionable as its feasibility. Evidence presented in this chapter suggests that the notion of ‘good institutions’, when defined as arrangements that are simultaneously market-enhancing and socially viable, may well be another neoliberal delusion. Institutional ingenuity may not suffice to peacefully align the two sides of that equation. In agriculture, the very rationale for the emergence of high levels of state intervention in the first place—and Turkey in this regard has been more representative of the developed than the developing world—was to actively protect rural livelihoods that were threatened at a most fundamental level by the ascendance of markets as the predominant mechanism of economic coordination. Any attempt to retreat from that rationale hits a wall of political

\textsuperscript{60} Consider, for instance, that from 1999 to 2007, Parliaments led by reformist governments passed almost twice as many laws compared to the 1991-1999 period, mainly to keep up with the extreme legislative requirements of IMF and World Bank-led programs: 719 vs. 1384 (www.tbmm.gov.tr). Even then, there is no shortage of potential reforms, and the process is never really complete: “Turkey’s challenge will be to press forward on the reform path”, declared the IMF upon its seventh review of the latest stand-by agreement (IMF Press Release, 08/106).
incentives that have crystallized around it over decades. Replacing old, economically inefficient institutions with market-enhancing ones brings only social dislocation and political disruption. As a result, novel designs such as direct income payments, even though they are only ‘half-as-good’ in that they fall well short of the current neoliberal goal of reducing the state to its regulatory functions, generate rebellion.

Banking reform illustrates the opposite problem. If good institutions in agriculture represent a step back from social viability, in banking they represent a step back from ideal-typical market relations. In this instance, novel arrangements seem to have provided an effective guard against market failures and therefore enjoy greater public legitimacy. A shallow understanding of market-enhancement may also hail these reforms for breaking the Turkish state’s bond-driven dominance in financial markets. Even then, it is hard to miss the fact that the remorphing of the banking regime gives rise to an environment that is more market-constrictive than market-enhancing in a number of ways. The new world offers relative safety, but in return imposes lower levels of profitability, denigrating overreliance on new forms of risk-taking while promoting more conventional banking operations instead. It also actively encourages oligopolization by erecting higher barriers to entry and making it increasingly difficult for smaller players to survive. All this comes at the added price of severe restrictions on business practices, more penetrating government surveillance, and assured continuance of direct state presence in the system through public banks. In this way, reforms signify a partial return to the preliberal past—certainly not in terms of an ISI-style systemic financial repression, but in market structure and in the spirit of financial activity.
CHAPTER SEVEN

EXTENDING THE TYPOLOGY

The comparative burden of the analysis has so far been fairly light. I have relied mainly on within-unit comparisons to illustrate how shifts in the value of the explanatory variables over time generated different types of institutional reshaping and led to different configurations in the same sector. Only in the previous chapter did I present a more systematic cross-unit comparison, and for the specific purpose of accounting for the divergent outcomes of identical types of change in Turkey’s financial and agricultural regimes in recent years.

By extending the typology to four non-Turkish cases, this chapter offers some remedy for the comparative dullness of the study. The goal here is not to provide controlled comparisons in proper fashion. The factors that connect distinct types of reshaping to concrete institutional configurations are manifold, and vary from one context to another, making disciplined cross-case comparisons difficult. My objectives are more modest. The first is to show that the typological framework I have offered has value beyond the narrow empirical focus of the study, and that it could illuminate with some accuracy institutional pathways in other contexts as well. Second, with a broader comparative focus, I hope to gather more information about the types of reshaping I have identified. Do they lead to outcomes similar to those in the Turkish cases? Are there completely different intervening dynamics at work? These are the questions I ask, both as I analyze these cases and, somewhat more systematically, at the end of the chapter.
Table 7.1  

Extending the Typology

<table>
<thead>
<tr>
<th>Case</th>
<th>Type of Reshaping</th>
<th>Institutional Outcome</th>
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<tbody>
<tr>
<td>China (Banking: 1978-2003)</td>
<td>Insulated Accommodation</td>
<td>Incremental Adjustments</td>
</tr>
<tr>
<td>South Korea (Corporate Governance: 1988-1997)</td>
<td>Negotiated Accommodation</td>
<td>Relative Stability</td>
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</tbody>
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Of the four cases, two are from East Asia and the other two from Latin America, each taken as illustrative of one type of institutional reshaping: Chinese banking (1978-2003) for insulated accommodation; South Korean corporate governance (1988-1997) for negotiated accommodation; Mexican agriculture (1988-2000) for insulated innovation; and Argentine labor markets (1989-2004) for negotiated innovation. All of these cases are very well represented in the comparative literature, and my analysis of them rests on secondary sources. My main interest is in showing why rulers in a certain case adopt a certain type, but as we begin to look closer at each case, it becomes impossible to extricate the analysis from the outcomes of these institutional choices (Table 7.1). This indeed is the main implication of the framework I offer. The typology provides only a vantage point for further inquiry. It is the researcher’s task to figure out the concrete outcomes of the adopted type in a given case via detailed empirical analysis and by allowing ample room for historical contingency and contextual specificity.


In a world characterized by ever tighter economic integration and the spread of democratic governance, it is difficult to find institutional trajectories that fit the type I have identified as insulated accommodation, which follows from domestic policy
considerations of technocratic elites who remain relatively detached from attendant collective interests. Yet, China’s banking regime, from the beginning in 1978 of the reform drive in that country until fairly recently, offers a case that comes as close to this type as imaginable. As in the other examples of institutional accommodation analyzed thus far (that is, the conversive and restorative patterns in Turkey’s agricultural regime), what we have in Chinese banking is not a story of simple stasis either. Likewise, as in various instances of technocratic insulation we have encountered in the Turkish context, the fact that Chinese officials enjoyed considerable autonomy from societal interests did not mean their decisions regarding sectoral governance lacked any and all political logic. Still, for about a quarter century, changes in China’s banking regime revolved around variations of the same pre-existing institutional theme of intense government involvement in and control over the sector, and appeared fundamentally out of synch with the astounding foray of the country into global markets. Moreover, the absence of powerful private financial interests and the systemic lack of public accountability in policymaking ensured that the struggles over this regime remained a within-state affair, which would be addressed via relatively simple, risk-aversive tactics of intra-bureaucratic bargaining rather than full-fledged coalition politics.

The restructuring of Chinese banking followed a gradualist path, but the extent of change was nonetheless significant and involved considerable institutional recasting. Before reform opening, China had a monobank system, with the People’s Bank of China (PBC) serving both as a central bank and the only commercial bank of the country. Reforms of the late 1970s and the early 1980s assigned the PBC with more conventional central bank functions and transferred its commercial operations to four newly
established state-owned banks: the Agricultural Bank of China, the Bank of China, the China Construction Bank, and the Industrial and Commercial Bank of China. While this first wave of restructuring was instrumental in modernizing the sector by emphasizing a two-tier system, it was never intended to put an end to “the traditional discretionary administrative commands and interventions” (Tam 1995, 3). To the contrary, it helped diversify the channels and increase the scale of public involvement in the sector.

The 1990s were marked by efforts to both reorganize the mechanisms of that involvement and redraw its regulatory framework. To relieve the state commercial banks of the colossal burden of preferential credit, Chinese officials in 1994 created three new policy banks: Agricultural Development Bank, China Development Bank, and Export-Import Bank of China. They also enacted in 1995 a Central Bank Law and a Commercial Banking Law, which replaced the “loose amalgamation of provisional regulations” (Karacadag 2002, 155). There were signs of change in market structure as well. From the mid-1990s onward, the sector saw a proliferation of smaller players in the form of new commercial banks controlled by local governments and state enterprises, various urban and rural credit cooperatives operating as commercial entities, the first truly private bank in the system (Minsheng), and some degree of foreign entry (Fung and Liu 2007).

In spite of these bold moves, by the turn of the century, Chinese financial markets remained dominated by the ‘big four’ state commercial banks that were wide open to political interference, whereas attempts to improve the governance of the sector were inspired primarily by unique domestic problems, most notably, the gargantuan non-performing loans (NPLs) of state banks. The PBC, which also acted as a supervisory agency, continued to be politically controlled, while the promise of operational autonomy
for state commercial banks never materialized. Frustrated by the limited scale of restructuring, Chow (2002, 53), for instance, remarks that “[b]anking reform…demonstrates the rule that institutions cannot be changed by legislation alone.” And given this powerful continuance of old patterns under new guises, many observers seemed to share Chen, Dietrich, and Feng’s (2002, 5) observation that “even though China has in place the composition of a financial market…it does not possess the essence of a well-functioning market.”

Consequently, China’s banking reforms in the 1980s and the 1990s resemble the evolution of Turkey’s agricultural subsidy regime during the same period in that, despite considerable institutional dynamism, the main parameters of sectoral governance more or less persisted. At the root of that resemblance, I shall argue, is the analogous sectoral position of Chinese banking and Turkish agriculture vis-à-vis wider patterns of economic transformation and internationalization in these countries. In chapters 4 and 5, I have shown how the relative marginalization of agriculture in the course of Turkey’s international economic integration (which was based initially on industrial exports, and then on financial flows, with progressively limited policy exposure to the IFIs) isolated this sector from external pressures for reorganization under two decades of neoliberalism. This in turn convinced Turkish policymakers to settle on accommodative strategies of institutional reshaping to address emergent domestic policy challenges. In roughly the same manner, formal channels of banking and finance in China had little to do with the country’s spectacular economic performance driven by industrial exports. This in turn should provide an important part of the explanation for the lack of genuine, transformative innovation in the governance of the sector until recently.
Evidence for the peculiar sectoral position of Chinese banking is quite strong. For instance, Chris Brammal’s (2000) definitive volume on Chinese growth in the 1980s and the 1990s is telling in its near-complete omission of banking and finance, focusing instead on the contributions of agricultural and especially industrial transformation. In a more recent analysis of China’s financial system, Allen, Qian and Qian (2008, 564) suggest that “the role of the banking sector and financial markets has been that they have done enough not to slow down the growth of the economy” (p. 564; emphasis original). They argue that, rather than formal bank credits, it was the alternative, nonbank financing channels such as foreign direct investment (FDI), informal intermediation, and internal financing that fuelled Chinese growth. Duenwald and Aziz (2002) offer conclusive ammunition for that line of argument. Accordingly, provinces with higher rates of growth which also had greater concentration of export-oriented, private sector industries had much lower bank loans-to-GDP ratios than those that experienced below-average growth. In fact, “less than 1 percent of working capital loans went to the private sector” (ibid., 56). This indicates that in China during the 1980s and 1990s, banking was rather defensively positioned to tackle or at least not to exacerbate the glaring problem of domestic (read, provincial) uneven development in the medium run. The excessive gradualism in financial liberalization was rooted in Chinese officials’ deep concerns about its compatibility with long-standing domestic developmental goals (Gang 2002).1

What relegated Chinese banking deep into the domestic side of the political-economic equation was the powerful nexus between public commercial and policy banks

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1 There was in that sense a purposive similarity between the behavior of bank funds in China and rural transfers in Turkey throughout the 1990s—a case not of insulated but negotiated accommodation. Their dynamic continuity and anomalous-looking resistance to reform stemmed from their ability to partly absorb the social pains of rapid economic transformation.
and SOEs. It was Chinese rulers’ misgivings about a rapid reformation of the country’s huge public sector, which embodied strong social welfare functions, that stood in the way of more sweeping banking reforms (Karacadag 2002, 150ff; Tong 2002, 5). As Dobson and Kashyap (2006, 104) note,

[T]he dependence of China’s government-affiliated firms on the state-owned banks for their working capital means that the banks are forced to satisfy contradictory objectives: financing employment and stability while transforming themselves into commercially viable corporate entities.

This in turn gives rise to persistent “tensions between banking efficiency and social stability” (ibid., 145). In the absence of an independent class of private bankers, trying to relieve these tensions by potentially sacrificing social welfare becomes an untenable position for reformist bureaucrats.

But once again, insulated accommodation in Chinese banking is only an approximation of that ideal-type. In actuality, both insulation and accommodation have had material limits. On the insulation side, it is true that challenges to reform did not spring from the intricacies of coalition politics in the more common sense of exposure to powerful societal interests. Yet, within-state struggles were instrumental in the process. Victor Shih (2007), in particular, makes a convincing case against running too far with arguments of technocratic insulation to explain the sluggish course of reforms. He maintains that the partial character of banking reforms under Premier Zhu Rongji, an otherwise maverick reformer of the late 1990s, was a reflection mainly of a strategy of political survival on the part of technocrats in a context of deep intra-bureaucratic cleavages.

There was, then, a core difference between the nature of technocratic influence in Turkey and China in terms of their intra-state dimension. In Turkey, technocratic
episodes coincided strictly with periods of economic crisis and extraordinary politics, which helped shield technocrats much more effectively against challenges from the traditionalist segments of the bureaucracy. The IMF-World Bank factor further strengthened the hand of technocrats during these episodes. As a result, periods of top-down reform in Turkey were marked either by declining levels of within-state struggles or, more commonly, by the decisive victory of reformist technocrats over traditional bureaucrats in policy and institutional decisions. (Recall, for instance, how ARIP was successfully pushed forward by a mere handful of Treasury elites despite fierce opposition from a vast agrobureaucracy aligned with powerful farmers’ organizations.) By contrast, Chinese technocrats operated under ‘politics as usual’ and relative economic stability. As such, they were continually subject to scrutiny by the party organization and the conventional bureaucracy, and had to strategize around these constraints at every step of the way.

On the side of accommodation, for more than two decades, China’s manufacturing export-based integration with international markets had minimal direct repercussions for the sector. But as internationalization continued apace, banking could not remain isolated from the explosion of new global financial norms and practices indefinitely. Because China was largely unaffected by the Asian crisis of 1997, it was at first in a position to pragmatically pick and choose from these emergent norms, rather than try to digest new international standards in their entirety like many other East Asian countries (Walter 2008). To resolve the chronic non-performing loan problem, for instance, Chinese officials in the late 1990s employed some externally-inspired policy and institutional tools, such as aggressive bank recapitalizations, efforts toward prudent
regulation via new loan classifications, and the establishment of asset management companies (Fung and Liu 2007, 127ff; Karacadag 2002, 156ff).

In recent years, however, and this is comparable to the experience of Turkish agriculture, there emerged more substantive efforts to converge on evolving international norms of sectoral governance. The driving factor here appears to be the country’s WTO membership, which, although it does not require across the board capital account liberalization, opens Chinese financial markets to foreign competition. This in turn has made a degree of institutional harmonization inevitable: three new pieces of legislation in 2003 reformed the central bank and commercial bank regimes in accordance with global standards, and established a new regulatory agency, the China Banking Regulatory Commission (CBRC) (Ip 2007). This normative exposure is not yet fully matched by market exposure, though, which should be expected to give Chinese reformers some leeway to mix and match their traditionally accommodative strategy with new innovative pressures from outside for the time being.²

7.2 Negotiated Accommodation and Corporate Governance in South Korea (1988-1997)

In the wake of the Asian Crisis of 1997, much emphasis has been placed on the unique corporate structure of South Korea, one of the hardest hit countries in the region. International agencies and many scholars have maintained that the weaknesses associated

² China’s current experience with foreign entry in banking mirrors the Turkish experience in the 1980s and the 1990s; by late 2005 there were over 70 foreign banks in the country, but they accounted for only 2 percent of total assets in the system. Besides, branchization is limited, and there are still constraints over the renminbi operations of foreign banks (Fung and Liu, 2007: 124). As such, both ownership and risks remain overwhelmingly domestic in Chinese banking.
with the governance of the *chaebol*, Korea’s peculiar form of industrial conglomerate, played an important part in the surprising vulnerability to external shocks of this stronghold of the ‘Asian miracle’. Korean policymakers were well aware of this problem; in turn, their comprehensive efforts to restructure the country’s corporate regime in the immediate aftermath of the crisis sparked considerable academic interest. While these efforts provide excellent examples of institutional innovation, my focus in this section remains the relative stability of that regime in the decade preceding the crisis, which comes closer to a type of reshaping I have called negotiated accommodation. The argument below suggests that the dynamics of political bargaining in a democratizing polity on the one hand, and the apparent ability of the *chaebol* to adapt to and flourish under new, financially-driven patterns of international integration, on the other, precluded attempts at structural reform of corporate governance during this period. Facing strong domestic political considerations but unchallenged by deceptively smooth modes of internationalization, Korean policymakers failed to counter intensified systemic risks via novel mechanisms. Rather, they oscillated between redeploying pre-existing mechanisms of bureaucratic control and erroneously putting faith in the disciplining powers of deregulated markets. The result was an institutional framework unable to cope with the changing realities on the ground.

The term *chaebol* refers to family-controlled business groups operating in multiple sectors via a dense network of affiliated firms. The organizational hallmark of the *chaebol* is interlocking ownership, whereby a core firm has controlling shareholder rights over a number of main subsidiaries that in turn control lesser firms in the

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conglomerate. This pyramidal ownership structure expands the managerial rights of the principal shareholders of the core firm disproportionate to their invested capital. It creates strong incentives for intersubsidiary operational as well as financial coordination, which, while encouraging diversification of group activities, also generates severe problems of transparency.\(^4\)

Historically, the rise of the *chaebol* coincided with Korea’s heavy and chemical industrialization drive in the 1960s and especially the 1970s. A military-authoritarian state, home to a highly efficient bureaucracy, extended large entrepreneurs a host of generous incentives, ranging from price and wage controls, sectoral entry barriers, tariff walls, and export subsidies. Most important, through its extensive control over commercial banks, the Korean state deployed a complex system of credit allocation to guide the investment decisions and monitor as well as discipline the market and export performance of the *chaebol*. In this way, Korea’s remarkably successful industrial policy during its take-off relied on a tight coordination between the state, finance capital, and big industry (Amsden 1989; Woo 1991; Rhee 1994).

Economic and, later, political liberalization of the 1980s and the 1990s substantially altered the nature of these relations. Yet the basic governance and corporate structure of Korean big industry appeared largely immune to these changes. This is indeed a surprising outcome because, as early as the late 1970s, Korean bureaucrats were aware of “the *chaebol* problem”. They were concerned that the oligopolistic concentration of economic power in the hands of the conglomerates could easily be translated into direct political influence and thereby create inefficiencies in credit

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\(^4\) See Lee (2002), S. J. Chang (2003), and Hwang and Seo (2004) for organizational perspectives on the *chaebol*. 
allocation, which in turn could pose a systemic financial risk for the economy given implicit government guarantees toward the *chaebol* (Lim 2003a). The collapse of 1997 was in that sense the realization of that basic fear, but through a historic path and proximate causes bureaucrats of the 1970s could not have imagined.

From the mid-1980s onward, two seemingly contradictory processes characterized state-chaebol relations. On the one hand was the relaxation of interventionist industrial policy itself, as reflected in a new Industrial Development Law, the declining powers and eventual abolition of the Economic Planning Board (EPB), and reduced policy loans to the largest *chaebol* (Rhee 1994, ch. 7 and 8; H.J. Chang 1998, 1558ff; Jeong 2004, 55ff). On the other hand were often unsuccessful attempts to tighten the government’s regulatory grip over the *chaebol*, ranging from fair trade laws to pre-empt monopolization to credit ceilings against large borrowers, and from measures to discourage overdiversification to restrictions on intersubsidiary loan guarantees. But the outcome of these efforts was what Woo-Cumings (1999, 124) calls a “regulatory albatross”, which introduced an “endless number of discretionary rules”, yet ultimately failed to tame the *chaebol*: “no regulation or special decree ever changed the essential structure of Korean corporate governance, right up to the crisis of late 1997” (ibid., 126). Instead, the *chaebol* managed to circumvent the Korean state’s old-fashioned regulatory advances. And contrary to what neoliberal policymakers had envisioned, conglomerates did not encounter much disciplinary market pressure during the accelerated opening of the 1990s either. In the end, many *chaebol*-affiliated firms were saddled by the sort of problems the earlier generation of Korean bureaucrats had feared the most: low
profitability, low productivity, overinvestment, and very high debt-to-equity ratios that together destabilized the entire economy (Joh and Kim 2003; E. Kim 2003; Joh 2004).

A mix of domestic and international factors accounts for this inability to rein in the chaebol despite the continuous talk of reform. On the domestic side, market and political transformations of the 1980s freed Korean big business from the shackles of intense state interference and, by doing so, inadvertently bolstered its political as well as economic power: “the old subservience to the state was outgrown and replaced by a new interdependence in which the chaebol exercised considerable leverage” (McKay 2003, 78). As a result, conglomerates managed to actively resist and in some instances subvert the state’s regulatory endeavors from within. One dimension of this was a classic story of increased cronyism that accompanied state withdrawal in almost every liberalizing late developer. As Hahm (2003, 80) observes, “policy choices…were often captured by interest groups, most notably by the chaebol themselves.” Chang and Park (2004, 44-5) also remark that, particularly during the 1990s, abuses of political power by the chaebol were ubiquitous. Consequently, problems of rule-following intensified. “[T]he rules of the game in Korea” appeared “endlessly negotiable” (Woo-Cumings 1999, 125).5

Perhaps much more important than cronyism, and in a less clandestine fashion, democratization gave rise to interest group politics and coalition dynamics impervious to institutional reform. To begin with, the chaebol did openly lobby to block systemic reform of corporate governance, and powerful business figures even ran for office, as in the 1992 presidential bid of Chung Ju Young, the founder of Hyundai. A more significant factor, as B.K. Kim (2003) argues in depth, was the growing inseparability of corporate

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5 A good example was Samsung’s entry into the auto industry in 1994 despite Kim Young Sam’s sectoral specialization policy that prohibited the chaebol from entering non-core sectors (B.K. Kim 2003, 70).
reform from labor market and financial restructuring. A strong labor movement in the process of democratization rendered wage repression an infeasible industrial strategy. During the decade focused upon here, between 1987 and 1996, real wages increased by 8.3 percent annually, a drive spearheaded by union gains in chaebol-affiliated heavy industry (ibid., 62). Such a major concession on the part of the chaebol, along with the significant welfare functions of company unionism in these firms, made it very difficult for Korean policymakers to justify sweeping changes in corporate governance. Compounding this difficulty was bureaucrats’ own reservations about further divesting state power by rocking too much of the institutional status quo. Thus, shortly after democratic opening, the political context exposed potential reformers to “a coalition of economic players who were interested in consolidating and maintaining the government-business risk partnership” (Lim 2003b, 49).

Given this powerful constraint, both Roh Tae Woo (1988-1993) and Kim Young Sam (1993-98) governments attempted to forge a ‘grand compromise’ to push for structural reform, but their feeble efforts repeatedly failed. In 1991-92, the Ministry of Finance prepared a comprehensive plan to limit intersubsidiary loan guarantees, but it never saw the day of light. A new sectoral specialization policy, announced with enthusiasm in 1993, would be easily circumvented by the conglomerates. There emerged a reformist initiative in some policy circles in 1996, but this too would be “defeated by concerted political opposition from the chaebol, organized labor, the state bureaucracy, and political parties” (B. K. Kim 2003, 74). As in Turkey during the 1990s, in pre-crisis Korea as well, intensified political competition gave rise to an impromptu coalition of collective actors dedicated to reform stalling.
A final aspect of the chaebol’s rising power was their increased financial independence from the Korean state (Hahm 2003; Jeong 2004, 58ff). Threatened by the shift in the direction of policy loans and in the face of new credit controls such as the basket system introduced in 1987, the chaebol sought alternative sources of financing in an increasingly open financial environment. From the mid-1990s onwards, most chaebol bought up and established several non-bank financial institutions (NBFIs), such as merchant banks, trust companies, and brokerage houses. In this way, they broke their dependence on state-controlled commercial bank loans and gained considerable autonomy in investment decisions, which pushed them further outside of government purview. This, however, amplified systemic financial risks exponentially, in particular after capital account opening. In a lax regulatory environment, the continued domestic and international perception of implicit government guarantees on chaebol activities led to a binge in foreign borrowing by Korean firms. By 1997, the debt/equity ratio of the 30 largest chaebol had reached over 500 percent. This vulnerable financial position of the chaebol is widely considered a proximate factor in the crisis. More important for our purposes, though, was that the newfound financial autonomy of Korean conglomerates inextricably tied corporate institutional restructuring to the wider prudential reform of the financial system. In short, not only was corporate reform a politically unpopular option, but it now posed a bigger technical-bureaucratic challenge.

Meanwhile, patterns of internationalization indirectly reinforced Korea’s corporate regime. International incentives for reform were conspicuous in their absence: just as in Turkish agriculture around the same time, nondomestic constraints were a missing variable for Korean corporate governance as well. On the policy side, it was not
that Korea was immune from external pressure. In fact, external pressures, especially from the US Treasury and on the path to Korea’s OECD membership, played a crucial role in convincing Korean policymakers to accelerate the pace of domestic liberalization and capital account opening (Woo-Cumings 1997; H.J. Chang 1998, 1559). But this policy openness had little, if any, implications for corporate governance. Korea’s economic and political opening coincided with the height of orthodox neoliberalism, which preached deregulation rather than disciplining market players; a concern for the internal organization and operational procedures of firms was not part of this wisdom. The global policy consensus that now exists about the significance of minority shareholder rights or transparency and disclosure standards is largely a post-Asian crisis phenomenon. For example, only in 1999 did the OECD publish its Principles of Corporate Governance and jointly established with the World Bank the Global Corporate Governance Forum (Mallin 2007, 31ff).

If policy exposure at the time did not encourage significant changes in Korea’s corporate structure, neither did patterns of market integration. After all, Korea appeared to be adjusting well to globalization. Between 1987 and 1997, the Korean economy grew by over 8 percent annually, and per capita GDP in terms of purchasing power almost tripled. And despite the slump of 1989-90, annual growth rate of exports topped 14 percent between 1990 and 1997 (WDI). In short, economic performance did not call for a radical fix. The novelty in Korea’s pattern of internationalization was its increased financial openness, but let alone entail a shift in existing forms of business organization, the process only strengthened the hand of the chaebol. In fact, because the continuation of easy access to foreign funds via affiliated NBFIs was the backbone of the chaebol’s

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6 See Gourevitch and Shinn (2005) on the varied ways in which countries respond to this new agenda.
newfound operational and investment autonomy, conglomerates emerged as ardent
supporters of financial integration, and fervently opposed attempts at tighter regulation
(Hahm 2003, 93). Unlike in Turkey where industrial export-led integration of the 1980s
required extensive sectoral reorganization in finance and thereby contributed to patterns
of innovation particularly in the banking regime, Korea’s exposure to financial
globalization in the 1990s created no such comparable incentive for its industrial
organization and in turn made institutional accommodation a viable strategy in that
sector. Fallout effects from market integration in other sectors mattered.

During the decade preceding the 1997 crisis, neither domestic political shifts nor
evolving patterns of internationalization generated transformative impulses for the
governance of Korean big industry. Instead, as was the case for Turkish agriculture in the
1990s, these factors worked in ways that enhanced the resilience of the pre-existing
regime. The dynamics of domestic politics under democratic competition augmented the
negotiative power of the chaebol vis-à-vis the Korean state, whereas reigning institutional
arrangements appeared quite feasible given the terms of intensified policy and market
exposure to the outside world. In such an environment, Korean policymakers’ efforts to
govern the chaebol revolved around variations of old ideas; accommodation, rather than
innovation, became the norm. Roh Tae Woo’s regulatory agenda around the turn of the
decade was in many ways a replica of the attempts of his predecessor, Chun Doo Hwan,
and “did not represent a paradigmatic shift in policy ideas on the chaebol” (B. K. Kim,
2003, 65). Meanwhile Kim Young Sam’s reformist promises never materialized under
acute policy stalemate at home and stronger neoliberal constraints from abroad. Genuine
institutional innovation had to wait until a massive economic crisis catapulted to power a
reformist government less receptive to *chaebol* demands, and exposed Korea to a much different set of normative pressures from international agencies.

### 7.3 Insulated Innovation and Mexican Agriculture (1988-2000)

To the precise opposite of Korean corporate governance lies Mexican agriculture, where the sectoral regime was transformed drastically, and with limited input from attendant interests. The primary innovative impulse behind this transformation was neoliberal elites’ strong conviction that the pre-existing modes of sectoral governance helped perpetuate a market structure and productive relations unviable for the country’s successful regional and global integration; emergent international norms offered a better alternative. To implement this reformist agenda, the administrations of both Carlos Salinas (1988-1994) and Ernesto Zedillo (1994-2000) relied on a technocratic policy process that allowed only narrow and highly selective channels of non-executive influence, preventing the vast majority of collective interests involved in Mexican agriculture from affecting the general course of change. The reshaping of rural market governance in Mexico in the 1990s therefore represents a fairly accurate approximation of the type I have called insulated innovation, although there is room for qualification, as discussed below.

The case of Mexican agriculture is particularly interesting for this study, given how similar it was to Turkish agriculture in market structure and historic patterns of state intervention, and yet how diametrically opposed were the institutional experiences of these sectors in the 1990s. In both Turkey and Mexico, we find a rich production design
based on the cultivation of numerous food and cash crops. Both sectors are marked by a large segment of smallholder peasants, which historically benefited from intense state intervention in product, input and credit markets, and in return extended political support for central rulers via corporatist arrangements. Internationally as well, Turkey and Mexico are located at the immediate periphery of highly protected and incomparably more productive developed-country agricultural markets, of Europe and the United States. Further, the 1980s was a distressful time for both sectors. Agricultural machines in both countries persisted, although fiscal constraints and changing policy priorities in the aftermath of their debt crises (1979-80 in Turkey and 1982 in Mexico) curtailed the redistributive capacity of the state. In spite of these basic similarities, the institutional trajectories of these sectors differed sharply in the 1990s. While in Turkey populist transfers were restored through a dynamic reinstatement of pre-existing institutions, in Mexico long-standing arrangements were quickly dismantled and new designs took root.

Before we account for this variation, let us first describe the dimensions of change in the Mexican case. At the center of the Mexican agricultural regime was a classic system of price supports whereby public agencies procured and marketed a sizeable portion of the annual produce in numerous crops at government-determined prices. The largest of these agencies was CONASUPO, the rough equivalent of the Turkish TMO, responsible for grains and other staples. From 1990 onward, CONASUPO withdrew from all crops except maize and beans, for which it continued to offer guaranteed prices until 1994. This was followed by a period of atrophy, and the organization was fully abolished in 1998. The price supports offered by CONASUPO were replaced by two very different arrangements, both operating under ASERCA, a new government marketing agency
established in 1991. One was a deficiency payment scheme toward various ex-
CONASUPO crops, which covered the difference between a policy price and the import
price, but only in states with surplus production in the targeted crop historically. The
other was PROCAMPO, a direct income support program announced in 1994, which
made modest direct payments to producers of selected crops, mostly foodstuffs. Both
arrangements were instituted as transitory measures to alleviate the adverse social effects
of the withdrawal of price supports (Appendini 1998; 2003; Eakin 2006, ch.3; OECD

Paralleling price liberalization was the sharp reduction in input subsidies, most
notably in rural credit. From the 1960s onward, Mexican producers had enjoyed universal
access to concessional loans through the extensive network of the state agricultural bank,
BANRURAL, the equivalent of Ziraat in Turkey. Reforms under Salinas saw a sweeping
reorganization of the bank, which closed down nearly half of its branches in the
countryside and now targeted only commercially viable smallholders, and at market rates.
The restructuring of BANRURAL had varied consequences. Whereas large and medium-
sized capitalist farmers had increased access to lending both through commercial banks
and via FIRA, a central bank-based program, subsistence farmers and most smallholders
now depended on ‘Crédito a la Palabra’ loans. These were distributed under
PRONASOL, the federal social assistance scheme, and often amounted to a tiny fraction
of what farmers used to receive from BANRURAL. In this way, “[t]he vast majority of
basic grains producers [were] abandoned by the Mexican rural financial system” (Myhre
1998, 61-2). The dismantling of ANAGSA, the agricultural insurance agency, and the
privatization of FERMITEX, the public enterprise in fertilizers, added further uncertainty to the fortunes of small producers.

Finally, a most dramatic component of rural market reforms concerned land tenure. Article 27 of the Mexican constitution had guaranteed access to land for all peasants in the form of communal landholdings called *ejido*. The new Agrarian Law of 1992 overturned this principle, allowing private ownership of *ejido* holdings through a titling program, PROCEDE. This granted participating *ejidatarios* the right to sell, rent or mortgage their land (Cornelius and Myhre 1998).

Two main themes stand out in analyses of this radical transformation in Mexico’s agricultural regime, which also set it apart from the Turkish case—that change was primarily driven by nondomestic considerations, and that rural interests were by and large excluded from this process. The difference in international factors affecting Turkish and Mexican agriculture could be traced at the level of both policy perceptions and market (and especially regional) integration. The heyday of neoliberalism in Turkey was the early 1980s. In this pre-Uruguay Round context, Turkey’s corporatist interventionism did not look particularly out of tune with global norms in agriculture. As we have seen in chapter four, both Turkish reformers and the IFIs framed the agricultural question as one of institutional effect rather than design. By contrast, Mexico’s reformist window of opportunity under Salinas after 1988 coincided with the beginnings of a fundamental shift in global perceptions about rural market governance, which would progressively weaken the state interventionist paradigm in international policy circles in subsequent years. This

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7 This was the one significant difference between Mexican and Turkish agriculture, as in the latter private property had long been the norm and the state’s commitment to land reform had been historically weak. Still, the class map in the countryside was similar in both countries, with a large segment of commercial and semi-commercial smallholders that enjoyed relative protection from the state, a sizeable stratum of middle farmers, and few large-scale capitalist producers.
imparted Mexican reformers with a much more comprehensive vision of change in agriculture than their Turkish counterparts. They were not concerned merely about the fiscal cost of subsidies, but perhaps more about “the need to make Mexican agriculture more competitive internationally” (Gledhill 1996, 170). The precondition of such competitiveness was to have “institutions compatible with free markets”, as the Undersecretary of Agriculture Luis Téllez put it in 1991 (quoted in Cornelius and Myhre 1998, 5). This was the rationale behind rural market reforms. In this task, Mexican policymakers received generous technical support from the World Bank, which also helped pacify intrastate resistance. In the early 1990s several Ministry of Agriculture teams, comprising mainly of bureaucrats skeptical of Salinas’ reform program, traveled to Washington for policy discussions with bank officials. Out of these deliberations followed a process of “social learning” for Mexican bureaucrats that helped build “a consensus sufficient for the reform…to go forward” (Teichman 2001, 141).

The terms of market integration were just as consequential. Here, political geography mattered. It is true that by the 1990s the IFI influence was negligible in Turkey and that older arrangements in agriculture had already adapted to liberal constraints. Yet, being in the vicinity of Europe did not put much pressure upon Turkey’s support regime either. Suffering from internal resistance to trade liberalization itself, the EU, as Turkey’s main trading partner, did not oppose to Turkish proposals to bind tariffs in most crops at excessively high rates during the Uruguay Round negotiations. In fact, agriculture was the only sector excluded from the Turkey-EU Customs Union Agreement in 1995. This contrasted sharply with the Mexican experience, where agriculture has been an integral part of the regional integration mechanism, the North American Free Trade
Agreement (NAFTA). It is commonly held that NAFTA did serve as a catalyst for *ejido* reform (e.g. Jilberto and Hogenboom 1996, 151), but nowhere was its influence more transparent than in the design of new transitory arrangements that followed state withdrawal from price supports. The deficiency payments under ASERCA targeted those crops that faced immediate competition from U.S. and Canadian imports. The other major arrangement, PROCAMPO, was designed in line with the liberalization timetable for the import of corn and beans: payments were to cease after 15 years, at the same time as corn tariffs would be abolished. As a result, while international trade had limited repercussions for Turkey’s grain-producing smallholders, in Mexico “NAFTA [set] the standard for winners and losers in the countryside” (Appendini 1998, 27). 8

Domestic political dynamics facilitated this innovative impulse set in train by nondomestic policy and market constraints. Unlike in Turkey, where intensified party competition for rural votes re-empowered agricultural interests and ultimately forced a dynamic restoration of populist corporatism via the accommodative strategy already in place, in Mexico rural forces found it difficult to counter or manipulate the broad changes imposed by technocratic elites. This in a way was a surprising outcome, given Mexico’s vibrant history of peasant mobilization, with strong organic connections to the ruling PRI (Institutional Revolutionary Party). Moreover, the 1980s had seen the emergence of new

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8 A comparison of Mexican corn and Turkish wheat, the main food staples in these countries, is instructive. Both crops are the lifeblood of independent smallholders: In Turkey wheat is the dominant crop of Anatolian plains; in Mexico almost three quarters of corn producers are in the *ejido* sector (Appendini 2003, 262). Neither country has a comparative advantage in these crops; production is oriented toward domestic consumption, and farmers face, if allowed, severe international competition, mainly from wheat-exporting France and Germany, and corn-exporting U.S. Despite this challenge, prices received by Turkish wheat farmers consistently exceeded world prices throughout the 1990s—by about 20 percent. In Mexico, however, corn farmers felt the pressure of international prices most severely. In the early 1990s, the withdrawal of CONASUPO from other crops made corn, which still benefited from floor prices, a safer and thus popular choice for many farmers. But government policy quickly defied this logic as support prices were pushed, politically, below world prices. In the few years following the implementation of NAFTA, prices for domestically produced white corn dropped by 35 percent in real terms (Eakin 2006, 43).
peasant organizations that hoped to increase the political visibility of smallholders at a time of systemic change.⁹

Yet the power of rural interests proved more apparent than real. In transforming the agricultural regime, Mexico’s neoliberal technocrats managed to circumvent societal actors, as was the case in most other policy areas (Teichman 1997). The *ejido* reform was designed behind closed doors by a small technocratic team; neither peasant organizations, nor large landowners, nor even PRI officials were actively consulted in the process (Grindle 1995, 46ff). In fundamental issues such as tariff reductions, the restructuring of rural credit mechanisms, and the replacement of old price subsidies with new welfare instruments, peasant interests failed to exert direct influence (Foley 1994, 70). Even segments of the agro-industry found it difficult to affect policy; the Mexican state was highly selective in granting subsector representatives access to the NAFTA negotiation process, including some (e.g. wine and beer) while excluding others (e.g. chocolate and canned foods) (Martinez and Schneider 2001).

For smallholder peasants, the obstacles to meaningful interest aggregation were two-fold. First, there was little genuine political contestation in the Mexican countryside. In Turkey, the reformist ANAP was decisively outflanked by the more traditionalist DYP, which made excellent use of corporatist farmers’ organizations to push forward its populist agenda. Mexican politics, by contrast, was marked by “the absence of strong *rural* partisan competition”, as reflected in the “limited differences between the agrarian programs of the three main political parties” (Kurtz 2004, 183, emphasis original). The

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⁹ One such organization was the left-wing, grassroots CNPA (the Ayala Plan National Network); another was the more productivist UNORCA (the National Union of Regional Campesino Organizations). In 1989, a Permanent Agrarian Council (CAP) was formed, which included UNORCA, several other autonomous peasant organizations, and most importantly, CNC (National Confederation of Campesinos), PRI’s peasant arm (Foley 1994, 60ff).
right-wing PAN (National Action Party) was a worse choice for peasants than PRI, whereas the center-left and worker-biased PRD (Party of the Democratic Revolution) was able to garner rural support only in a few states (Fox 1994, 254). Ultimately, channels of institutional influence were tied up in the hands of PRI-linked organizations and local elites. These elements did not share Salinas’ enthusiasm for agricultural reform, but they could not subvert the national party line dictated by technocrats either. Peasant leaders who opposed the ejido reform, for example, were “threatened with loss of access to the few government support programs still available” (ibid., 262). By mid-decade, rural discontent was no longer so easily containable; but by then the old regime had already been almost fully dismantled, and reformers were in a position to selectively deploy such federal programs as PRONASOL and PROCAMPO to quell opposition. Having redefined rural policy as a matter of social welfare rather than active market governance, these schemes had the eventual effect of “cutting out peasant organisations as intermediaries between the State and the campesinos” (Gledhill 1996, 179).

Second, the character of the reform process itself was inimical to the emergence of sector-wide counter-reformist initiatives. As Foley (1995, 71) aptly observes:

By treating separately, crop by crop, service by service, such issues as price supports and fertilizer supply, credit availability and market access, governments take major steps toward depoliticizing issues, insulating larger macroeconomic and macropolitical decisions, and dispersing organized discontent.

It must not be dismissed that this particularistic nature of neoliberal reforms also permitted some isolated instances of peasant organizational influence over the direction of institutional innovation. Snyder’s (1999; 2001) well-known analysis of the coffee sector, for example, documents the emergence of participatory policy frameworks in Oaxaca and, to some extent, Chiapas. We can safely surmise that, in these sub-national
cases, patterns of reshaping were geared toward negotiated rather than insulated innovation. At the same time, we need to keep in mind that such “success stories of peasants coping in an open economy” were invariably limited to “potential export crops” (Appendini 2003, 265). In broader, sector-wide issues such as the credit regime or the transition from price supports to direct payments, and for the most significant crops such as corn and beans that together accounted for about half the total harvested area, Mexican peasants could not escape the “disorganizing and atomizing effects of neoliberalism” (Kurtz 2004, 164). Insulation in that sense stemmed not only from a lack of partisan alternatives or the technocratic clogging of organizational channels, but also from the inability of sectoral interests to act in unison in the face of a complex and highly fragmenting reform agenda. Reforms went too far too quickly, compelling its victims to fight tactical rather than strategic battles.

Seen this way, there is indeed a shared dynamic between the Mexican and Turkish experience with rural market reforms. Faced with a comparably overwhelming project in 1999, Turkish farmers too failed to prevent top-down institutional restructuring in its early years. And even after 2002, when the political context grew more permissive of popular demands, they would find it impossible to subvert novel arrangements in their entirety, and had to settle for a hybridized regime. The basic lesson from both cases is simple: the synergy between technocratic engineering and international norms generates too powerful and lasting a reformist momentum to be fully counteracted even by the

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10 Indeed, coffee may not be the best crop to understand the dynamics of institutional recasting in rural Mexico. Coffee producers did not benefit from price subsidies: OECD data suggests that coffee consistently received ‘negative transfers’ throughout the 1980s and 1990s (OECD PSE/CSE Database). As a result, peasant organizations welcomed price liberalization in coffee, and in many states actively supported the privatization of the public marketing agency, INMECAFE (Krippner 1997).
strongest collective actors. As far as sectoral interests are concerned, insulated innovation is a very unpalatable prospect.

7.4 Negotiated Innovation and Labor Reform in Argentina (1989-2004)

Sectoral regimes make excellent targets for institutional analysis. This is the level where we tend to find a wide array of formal arrangements with powerful legacies, where alternative designs often reflect clear shifts in global norms and are promoted programmatically by international agencies, and where reformers and organized interests clash over institutional design with dramatic repercussions for collective fortunes. But alongside sectoral regimes, the typological framework I have proposed might also apply to other mid-range institutions that govern core policy areas. The record of labor market reforms in Argentina offers one such case, and is analyzed below as an illustration of negotiated innovation, albeit an ultimately aborted example of this type.

Negotiated innovation is potentially the most complex of the four types of reshaping I have identified, for it forces institutional reformers to reconcile nondomestic incentives for change with the coalitional exigencies of domestic governability. The outcome of this juggling act in the Argentine case was a highly incoherent reform path. While reformers and the IFIs saw the flexibilization of the labor market imperative for the country’s international competitiveness, attempts at genuine institutional innovation in that direction were constrained by opposition from organized labor, a core actor in Argentina’s reform coalition due to its organic links to the Peronist party, PJ (Partido Justicialista). Only after the PJ lost the 1999 elections could radical reform proceed, but
even then it would be short-lived and was summarily reversed once Peronists returned to power following the economic collapse of 2001-02. Consequently, although innovation along the neoliberal norm of labor market flexibility dominated the policy debate for over a decade, negotiations with attendant interests in a politically competitive environment failed to bring about lasting change.

By the late 1980s, Argentine labor markets were still governed by arrangements dating back to the heyday of Peronism in the 1940s and the 1950s. These arrangements were emblematic of the country’s long legacy of populist corporatism, the main constituency of which was organized labor. For nearly half a century, unions comprised the primary support base of Peronist politics, embodied first by the Labor Party and then the JP. In exchange, union leaders were generously represented in the congress and often held cabinet posts, and used their power to secure a labor-friendly industrial relations climate: Collective bargaining was compulsory at the industry level and was centralized through union monopolies in each subsector; expired collective agreements remained in force indefinitely if no new settlement was reached, assuring the continuity of earlier gains (a clause dubbed ‘ultractividad’); probation periods were short, severance payments were hefty, and there was little room for fixed-term contracts; finally, unions were directly engaged in providing health and welfare services through their extensive control over social security funds (obras sociales), from which they derived significant economic power (McGuire 1997, ch.3, ch.8; Galiani and Gerchunoff 2003).

This highly protective regime was in obvious contradiction with neoliberal ideals of deregulation and labor market flexibility, and was slated for reform during the first Menem administration (1989-1994). In particular, the Cavallo Plan of March 1991, which
represented the pinnacle of neoliberal restructuring in Argentina, called for structural changes regarding temporary contracts, wage indexation, sectoral union monopolies, and the obras sociales (Acuña 1994, 46-7). Menem’s economic team portrayed these proposed measures as a potent remedy for the grueling rates of urban unemployment Argentina suffered under structural adjustment. But independent of this problem, there were concrete nondomestic incentives at work. For one, the idea of sweeping labor market reforms received broad support from the IFIs. A World Bank study in 1990 had already recommended “the decentralization of wage bargaining and the elimination of both wage indexation and government intervention at large” (Riveros and Sanchez 1990, 42). Argentina’s Letters of Intent to the IMF concerning a stand-by agreement in 1991 and an extended arrangement in 1992 also promised comprehensive labor market reforms (IMF 2004, 31). Both the IFI staff and the economic team believed that the relaxation of labor regulations was critical for the country to attract foreign investment and successfully compete in global markets in the long run.

What made this shared neoliberal belief in the virtues of flexible labor markets more meaningful in the Argentine case was a structural drawback of the exchange rate regime adopted as the centerpiece of the Cavallo Plan, which, as a radical anti-inflationary measure, ditched traditional discretionary monetary policy on behalf of a currency board, and pegged the peso to the US dollar.\textsuperscript{11} As effective as this was in putting a long-awaited end to Argentina’s hyperinflationary cycles, it would soon lead to the overvaluation of the peso, undermining the competitiveness of the economy as a

\textsuperscript{11} Hence, it is also known, somewhat more commonly, as the Convertibility Plan. See Starr (1997) and Wise (2000) on political-economic analyses of Argentina’s currency board. See also Cavallo and Cottani (1997) for an insider account of the respective positions of the Cavallo team and the IMF staff on the convertibility regime.
whole and hurting the current account. Lowering factor costs via downward wage flexibility was about the only ‘permanent solution’ to this problem (Starr 2003, 67). The antiquated labor market institutions stood in the way.

Despite the stated resolve of the reformers at home, and market as well as policy incentives from abroad, the scale of change in the labor regime under Menem was modest, due mainly to resistance from unions. Certainly, the advent of neoliberalism forced the Argentine labor movement, the strongest in the region, into the defensive. In 1989, controversy over the PJ’s ideological change of heart created a split in the umbrella association of organized labor, the CGT (General Labor Confederation). This division in the PJ’s traditional base proved as much a curse as a blessing for the party leadership. On the one hand, it forestalled the emergence of a unified labor opposition to early reform measures (Canitrot and Sigal 1994, 129ff). On the other hand, it compelled Menem to regain the acquiescence of dissident labor factions, by targeted rewards and punishments, particularly in the privatization process (Acuña, Galliani, and Tommasi 2007, 51-2).

But as reforms proceeded toward items that exacted significant costs on all segments of labor, the fresh rift between opposing CGT factions began to close, and the burden of societal negotiation got heavier. The National Employment Act, passed in late 1991 after two years of deliberations, was the product of such a compromise. The legislation opened the door to various new types of temporary contracts that granted employers greater flexibility in the hiring and firing of workers. It also introduced some inducements for the employment of younger workers, and set up a basic unemployment insurance scheme. But the new act was a far cry from what reformers had in mind. In particular, the implementation of fixed-term contracts would be contingent upon union
approval, which made the new arrangement near-useless for big industry. Most important for organized labor, proposals regarding union monopolies, the ultractividad clause, the decentralization of collective bargaining, and the reform of the obras sociales were scrapped during negotiations. Some flexibility, mostly toward individual contracts, was a small price to pay for the preservation of these pillars of union power under rampant neoliberalism (Murillo 2001, 145-7; Madrid 2003, 75; Cook 2007, 74-5).\textsuperscript{12}

The dissatisfaction with the new law among both the reformist elite and business associations provoked Menem to try to achieve via executive decrees what he could not via congressional approval, as he often did in other areas of reform (Peruzzotti 2001, 151ff). This attempt at \textit{decretismo} toward the PJ’s most loyal base would quickly backfire. Decrees that targeted the obras sociales were either withdrawn or amended under threat of general strike by a unified CGT (Cook 2007, 75). In subsequent years, labor reform would settle on an irrevocably negotiative path. Tripartite talks in 1994 concluded with a framework agreement, and inspired several pieces of legislation the following year. The scope of these new laws was quite limited: one gave small and medium-sized firms greater autonomy in temporary contracts; others dealt with issues such as occupational hazards and accidents, contract suspensions under bankruptcy, and apprenticeship contracts (ibid., 82). While these arrangements were broadly flexibility inducing, none posed a discernable threat to vested union interests. Still, the increasingly conciliatory and pro-Menem attitude of CGT leadership generated sufficient dissidence among its member base to trigger the formation of two new breakaway confederations,

\textsuperscript{12} Another example of negotiated change was pension reform, which passed in early 1993, and included a number of concessions addressing union demands (Murillo 2001, 143-144; Madrid 2003, 73ff).
the CTA (Congress of Argentina Workers) in 1992 and the MTA (Movement of Argentine Workers) in 1994, both advocating a more militant posture.

By the start of the second Menem administration (1995-1999), nondomestic incentives for reform resurfaced forcefully. The fallout from the Mexican peso crisis of 1994 amid continued currency overvaluation put further pressure on the economy, necessitating a new IMF package in 1996. Puzzled by the uncharacteristically slow pace of reform in this one area, the Fund “pressed the economic team…to submit legislation to reform collective bargaining agreements” (IMF 2004, 32). The World Bank too kept pushing for a massive reform of labor market institutions; in a July 1996 country report, it advocated the decentralization of collective bargaining, the elimination of unemployment insurance, the full deregulation of fixed term contracts, and an end to both ultractividad and union provision of social services (World Bank 1996, 56-58).

Facing intense IFI pressure, the government announced plans for a radical overhaul of the labor regime. Rather than wait for policy debate and negotiated legislation, Menem in late 1996 issued a number of decrees that fully satisfied IMF demands, including the elimination of centralized bargaining and ultractividad, and the deregulation of the obras sociales. Unions mobilized quickly, organizing a general strike in December; further, Menem’s decrees were taken to court and quashed. Thus followed another round of negotiations with the CGT over a new package, which nonetheless drew stringent opposition from the CTA and MTA. Intensified party competition, reflected in the victory of the center-left FREPASO-UCR alliance in the 1997 lower house elections, further weakened the PJ’s hand. After one and a half years of negotiation, and desperate
to bring organized labor back into the Peronist fold, Menem brushed aside the IMF constraint and agreed to a legislation that met most union demands (Cook 2007, 78ff).

The new law, enacted in September 1998, rolled back almost all measures that had been introduced since the 1991 reforms (Murillo and Schrank 2005, 988ff). Dubbed the *contrareforma* (counterreform) by employers, it revoked most contractual stipulations of the 1991 law, cut down probation periods, reinforced centralized bargaining and union monopolies at the industry level, and re-emphasized ultractividad (Cook 2007, 80-81). Overnight, collective labor relations in Argentina were thrown back into the thick of corporatist interventionism. This lack of substantive change in labor market institutions “constituted a crucial gap in the reform agenda” (Corrales 2002, 204); after a decade of neoliberalism, labor markets were still marked by “significant rigidities” (Kiguel 2002, 92), representing an “illiberal enclave” (Wise 2000, 99).13

In the 2000s, the cycle of reform and counterreform would be played out once more. When Menem was voted out of office in 1999, the economy was on the brink of abyss. The Brazilian crisis, followed by the devaluation of the *real*, severely undermined the competitiveness of the Argentine economy in the midst of massive capital outflow from the region. The Alianza government led by Fernando de la Rúa signed a new stand-by agreement with the IMF, in which labor market reform was designated as the top structural benchmark (IMF 2004, 84). Under similar pressures from the World Bank (World Bank 2000c, 18-19; 25), the Alianza government passed a new labor legislation in 2000 that terminated ultractividad, increased probation periods, and granted priority to decentralized bargaining. But the law would be marred by a corruption scandal regarding its enactment in the Senate. The crisis of 2001-02 was followed by the resurgence of the

13 See also Pastor and Wise (1999, 495); Teichman (2001, 166-167); and Baer et al. (2002, 69ff).
PJ under Nestor Kirchner. Riding on public distaste with IFI-guided neoliberalism and in the context of an agreement between unions and the main employer association (UIA, the Industrial Union of Argentina), the government introduced a new law in 2004 that restored ultractividad, reduced probation periods, increased severance payments, and emphasized ‘articulated’ bargaining (Cook 2007, 92-98). With the institutional sources of union power preserved, the past few years have been characterized by the swift reconstruction of labor-based corporatism (Etchemendy and Collier 2007).

The convoluted record of Argentine labor reforms shows that judging institutional trajectories simply by institutional outcomes may not be a wise analytic choice. After nearly two decades of struggling, labor market institutions are roughly where they were when it all started. The scale of change even pales in comparison to most instances of institutional accommodation we have examined. What distinguishes the Argentina case from episodes of accommodation in Chinese banking (1978-2003), South Korean corporate governance (1988-1997), and Turkish agriculture (1980-1999) is that in these latter cases substantive innovation was never seriously tried. Changes, however extensive (e.g. in Chinese banking), essentially reflected a reworking of the existing institutional repertoire. By contrast, in its main character the Argentine case is much closer to the experience of Turkish agriculture after 2002: in both examples, there were strong, radical projects for innovation in place, which were nonetheless defeated as a result of opposition from collective interests, certainly more decisively in Argentina.

As in the Turkish case, the main catalysts for change in Argentina too were nondomestic. Labor reform was formulated primarily as a matter of international
competitiveness and sectoral adjustment in a context of outward-oriented development. Industrialists, as the domestic group that would most benefit from reform, could not autonomously push for it, but tagged along when nondomestic constraints intensified. The two proposals for sweeping change (in 1996, defeated, and in 2000, passed) were both introduced at times of regional crisis (Mexican and Brazilian currency meltdowns in 1994 and 1999, respectively), which eroded investor confidence in Argentina’s rigid exchange rate regime and opened the gates to heightened IFI influence. In both, IMF conditionality and World Bank recommendations played an incomparably more critical part than domestic lobbying.

The emergence of radical reform proposals and the difficulty that one of the strongest labor movements in the developing world encountered in thwarting them attest to the power of these nondomestic incentives for change. But ultimately, the puzzle of defeated reform in the Argentine labor regime boils down to the fact these international incentives, although formidable enough to lay the groundwork for radical reform along new norms, were still insufficient to overcome the systemic synergy between pre-existing institutions and coalition dynamics. The sources of relative weakness (and the word ‘relative’ is key here) in nondomestic incentives for change were three. First, whereas the idea of labor market flexibility is ingrained in the neoliberal wisdom, international practice assigns it a more modest normative status than such issues as privatization or financial liberalization. Country experiences with labor market reform have varied sharply (e.g. Crowley and Ost 2001; Kubicek 2004; Cook 2007). Besides, there are important countervailing forces, such as the International Labor Organization (ILO),

14 Note that reforms in individual labor law and incentives toward small and medium-sized businesses in the 1990s could not resolve the unemployment problem, despite concealed flexibilization in the form of the growth of the informal sector (Galiani and Gerchunoff 2003, 156ff).
whose skepticism toward unfettered flexibilization in the formal sector has only been bolstered by the public outcry against cases of abuse and extreme exploitation in the informal, by definition flexible, labor markets in some parts of the global South. Second, where international norms are contestable, it takes immense market and political incentives for them to inspire substantive innovation. This was the case for Mexican agriculture in the early 1990s, where global norms were certainly moving in a pro-reform direction but had not yet reached ecumenical status. As in labor flexibility, this allowed countries some wiggling room. In such a context, powerful market and policy pressures from the US under NAFTA were instrumental in tipping Mexican authorities over to the pro-reform camp in agriculture. By contrast, Argentina’s main export partner, Brazil, was also an underperformer in the area of labor flexibility (Cook 2007, ch.3), whereas US policy toward Argentine reforms was at best indifferent (Arceneaux and Pion-Berlin 2005, 42ff). Besides, throughout the 1990s, Argentina attracted more foreign direct investment as percentage of its GDP than both Mexico and Brazil, and its export to GDP ratio was higher than Brazil’s (WDI), so competitiveness did not seem as pressing a problem as reformers and the IFIs made of it. A third factor that constrained the effectiveness of international incentives was the limits of IFI pressure. The World Bank urged flexibilization, yet because reform was mainly legal in nature, there were no corresponding bank projects. This left the IMF as the primary force, but given the country’s impressive track record of neoliberal restructuring, it was willing to let this one instance of noncompliance slip by. As the fund’s internal evaluation report suggests, “when political obstacles surfaced, it was reluctant to jeopardize its relationship with Argentina over labor market matters” (IMF 2004, 32-33).15

15 This too mirrors the recent Turkish experience, where given strong reform compliance in such crucial
Under different circumstances, moderately powerful global norms, supported by a general concern with international competitiveness and some pressure from the IFIs, could suffice to bring about substantive innovations in a mid-range institutional regime. This was roughly the case for Turkish finance in the early 1980s; in the absence of opposing domestic forces, international incentives, although not as strong or well-articulated as those in the 2000s, were enough to spearhead institutional convergence through radical innovation. But in the Argentine case, the targeted arrangements were too central a concern for the sustainability of the reform coalition, and thus proved too resistant to change. Against a deep-seated legacy of intense distributional conflict that translated into very high levels of party competition since redemocratization, the PJ’s reliance on labor support to see through neoliberal reforms proved a most stringent constraint. How this support was obtained from a social group potentially least friendly toward market reforms inspired a variety of explanations. A common side story of all these explanations, though, is that the internationally-driven agenda of labor market reform caused great tension in party-union relations. In turn, Menem tried to circumvent the labor constraint altogether by putting the PJ’s fluid, highly adaptive organizational structure in the service of clientelistic machine politics (Levitsky 2001; 2003). While this, along with Menem’s populist rhetoric (Weyland 2003; Teichman 2004) and fiscal areas as fiscal and banking restructuring, the IMF seemed willing to tolerate deviations from the reformist path in less crucial areas, such as agriculture, social security, and anti-corruption.

16 See Mallon (1975), Manzetti (1994) and Corradi (2003) on how distributive conflicts played out in Argentine politics at different times.
17 In a relatively early work, Levitsky and Way (1998) explain CGT support for Menem’s early reforms by citing such variables as strong social linkages between union and party leaders, party strength, low levels of union competition, and partial overlap between party and union leadership. Likewise, Murillo (2001) emphasizes the role of partisan loyalties and leadership competition. Madrid (2003), by contrast, adopts an issue-oriented approach that stresses the severity of the impact of proposed reforms on unions; as such, organized labor in Argentina approved financial, tax, trade and privatization reforms, while it bargained over pension reform and blocked most labor reform proposals.
generosity toward the provinces (Gibson and Calvo 2000; Eaton 2001), helped broaden the party’s mass appeal for a while, the electoral defeats in 1997 and 1999 in the face of heightened party competition on the left cast doubt on the viability of a Peronist future without persistent union support. Internal divisions and leadership rivalry within the PJ since Menem’s departure have only augmented the significance of organized labor for the party. Unlike in Mexican agriculture, domestic political dynamics in Argentina have reinforced the resilience of the pre-existing labor market institutions and shielded them from destruction in the face of somewhat weaker nondomestic incentives for change. The outcome was not accommodation, but outright defeat of innovation.

7.5 Types Compared

None of the four cases examined in this chapter is a pure representation of the type it exemplifies. Chinese technocrats were constrained both by the social ramifications of reforms and intra-bureaucratic dynamics, and, after the mid-1990s, seemed willing to selectively incorporate global norms. In South Korea there emerged some reformist initiatives, even though these revolved around old ideas. To offset potential political resistance, Mexican reformers retained state subsidies in critical crops for a few more years until new support schemes fully took over. In Argentina, the centrality of pre-existing arrangements for the maintenance of the reform coalition was a crucial catalyst for the eventual defeat of the innovative project. A seamless fit between an abstract type and social reality is nowhere to be found.
Even then, these cases provide plausible approximations of the types of institutional reshaping I have identified in this study. With a broader empirical sample, we can now endeavor, somewhat more justifiably, to infer contingent generalizations about these types and their real world consequences for both institutional configurations and attendant social interests.

To begin with the last case, Argentina’s aborted labor market reforms, taken in the context of the diverse fates of three Turkish cases analyzed before (finance in the 1990s and then again after 2002, and agriculture after 2002), suggests that the outcome of negotiated innovation is most unpredictable. All four examples of this type were marked by formidable external incentives for reorganization and high levels of domestic political competition, generating attempts at substantive innovation in consultation with societal interests. Yet the combined differences in (a) the strength and coherence of global norms as well as the character and intensity of market, regional, and IFI pressures through which they are transmitted, and (b) the dynamics of coalition politics, as reflected in the electoral and associational prowess of collective interests as well as shifts in their formal and informal links to executive circles culminated in remarkably different configurations. In Turkish finance during the 1990s, the result was selective innovation that soon degenerated into reform forbearance. Conversely, after 2002, novel banking and fiscal regimes were consolidated and refined. Under the same type, Turkish agriculture saw the resurfacing of older arrangements alongside new ones to form a hybrid institutional framework. In Argentina, radical reform was thwarted repetitively as a result of failure of negotiation with unions.
These divergent outcomes underscore the earlier argument that, from the same type of reshaping, different institutional profiles may follow in different contexts. Evidence from other cases also supports this proposition.\(^\text{18}\) Still, in comparison to cases that represent other types, variations in outcomes seem much more acute in the instances of negotiated innovation analyzed here. This, I believe, is not the contingent side effect of case selection, but the symptom of a condition specific to this type. When handed the opportunity to influence policy at the same time as the institutions that govern their livelihood are enlisted for change, collective interests try to manipulate the process most forcefully, by testing the limits of their political-organizational strength and exploiting any weaknesses in international incentives.\(^\text{19}\) This leads to a complex game in which the two synergies mentioned in chapter two are pitted directly against one another: the prominence of international norms, even under strong negotiative constraints, tend to give some voice to technocratic concerns; at the same time, the prominence of coalition politics, even under strong innovative constraints, tend to assign some significance to pre-existing institutions. That is why outcomes are least predictable and hence the burden of analysis is much heavier in this type, calling for more nuanced explanations.

What makes this finding even more significant is that, given the twin global trends toward market internationalization and democratic accountability during the past few decades, we can reasonably expect negotiated innovation to be the most common

\(^\text{18}\) For instance, insulated accommodation in Chinese banking involved deeper changes than in Turkish agriculture in the 1980s; negotiated accommodation in Korean corporate governance proved more protective of pre-existing institutional forms than the restorative pattern in Turkish agriculture in the 1990s.

\(^\text{19}\) Note that even in Turkish finance after 2002, where innovations went farthest, bankers and some bureaucratic elements mobilized against the consolidation of reforms, and lost. In the Argentine case, unions successfully blocked innovation. In the remaining two cases (Turkish finance in the 1990s and agriculture after 2002) some compromise was reached. In their analysis of Russian tax reforms Luong and Wienthal (2004) provide another example of such compromise.
type of institutional reshaping in contemporary late developers. Yet the built-in tension specific to this type puts reforms, especially the kind inspired by imported blueprints, on tenuous ground: only in one of the examined cases (Turkish finance after 2002) did reforms actually proceed as planned. In the other three, building designer institutions or consolidating those that were newly established proved impossible. Instead, the politically inclusionary character of change nurtured counterreformist tendencies, resulting in significant deviations from the projected path.

The opposite type, that is, insulated accommodation, is much less conflictual. Here, technocrats lead the way, but they neither encounter the technical challenges of building new institutions (which, in cases of innovation, often involve a time constraint as well, to meet the conditions of an IFI program or regain investor confidence after crisis), nor do they face opposition from attendant interests. Rather, they are driven by domestic policy considerations, but without having to pay much attention to everyday domestic politics. This was the general dynamic of change in both Turkish agriculture in the 1980s and Chinese banking until recently. The Chinese case, which I think is a better example of this type, certainly generated more formal change than the former, but then it corresponds to a quarter century of institutional development. Nonetheless, configurational outcomes were similar. In the absence of strong nondomestic incentives for sectoral reorganization, reformers in both countries recycled the existing institutional repertoire to adapt existing arrangements to new domestic realities or even new purposes. In Turkish agriculture, the support regime was redeployed as a means for demand management and fiscal restraint; in Chinese banking, continued state control over the

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20 I think this is also the type that roughly fits Garrett and Lange’s (1995) model of international influences on domestic institutional change.
sector became an important concern for social welfare. Yet this similarity in configurational outcomes is shadowed by the differences in the consequences for collective interests. In the Turkish case, insulated accommodation ate away at agricultural fortunes. By contrast, in the absence of an independent class of private bankers, accommodation in China could be said to have favored social groups that stood to benefit from the continuation of a politically managed public banking system, namely, bureaucrats in general and workers in the public sector. Overall, though, insulated accommodation is the least challenging of the four types, both for the rulers to implement and for the analyst to examine and explain. Probably, it is also the least common type.

In neither negotiated innovation nor insulated accommodation can we predict institutional outcomes with certainty: change can be cosmetic or profound; social actors may win or lose. By comparison, insulated innovation and negotiated accommodation offer a clearer contrast in respective outcomes. Insulated innovation often yields the greatest scale of transformation, and is generously represented in our sample by three Turkish cases (finance in the 1980s, and finance and agriculture in 1999-2002) along with the case of Mexican agriculture examined in this chapter. In these sectors, top-down reforms fundamentally refashioned the incentive structures that guided economic activity. As such, these examples also show why collective actors, when given the chance, fight so hard to manipulate innovative impulses: the cost of exclusion from this process is unbearably high. Only in Turkish finance in the 1980s were the consequences of reform favorable to sectoral interests. In others, collective fortunes suffered under technocratic exclusivism, which invariably proved more receptive to nondomestic market and policy pressures. Mexican and Turkish peasants paid the price of political exclusion by losing
their long-established redistributive privileges. Even in the Turkish case, where reforms were to be partially overturned, the initial damage to rural livelihoods was significant. Most dramatically, in Turkish finance after 1999, insulated innovation led to the eradication of a class segment: rentier capitalists that had recklessly preyed on fiscal expansionism for over a decade were almost entirely destroyed.

Negotiated accommodation illustrates the opposite scenario. With little or no pressure for sectoral reorganization from outside, policymakers are inclined to work within existing institutional paradigms with minor adjustments. In a political context responsive to societal demands, this policy predisposition leads to configurations that benefit attendant interests. Both Turkish peasants and Korean industrialists, roughly around the same time period, took advantage of these fortuitous circumstances and, as founding partners of ruling coalitions, secured the broad survival of the arrangements they deemed indispensable for their interests. In Korea, reformist incentives revolved around old ideas; even then, they were not to be pursued with conviction. In Turkey as well, innovative ideas did not surface until the late 1990s. Some expectable sacrifices had to be made (such as limited privatization), but in return populist redistribution was fully restored. In both cases, institutional preservation was much more pronounced than in the insulated variety of accommodation. And in both, the mutual adaptation of institutions and actors to changing intra- and extra-sectoral realities was critical. The chaebol quickly compensated for the loss of state financial subsidies by extending their operations to a fast internationalizing financial sector. Meanwhile, Turkey’s farmer organizations and agrobureaucrats learned how to sustain their cooperation within emergent policy constraints. They also manipulated the novel opportunities for fiscal expansion to keep
the support regime on a redistributive track. Curiously, in both sectors institutional survival was aided by financial globalization.
CHAPTER EIGHT

CONCLUSION

From a set of simple hypotheses, this study constructed a typology of sectoral institutional pathways in contemporary late developers. Weak international market and policy incentives for sectoral reorganization encourage an accommodative strategy of reshaping that redeploy pre-existing arrangements through modest adjustments. Conversely, strong international incentives for reorganization provoke substantive innovations in sectoral regimes in tune with reigning international norms. Lower levels of domestic political competition tend to insulate executives from societal and other intra-state forces, facilitating technocratic projects. However, higher levels of political competition compel incumbents to negotiate the terms of change with attendant collective interests through coalition politics. The first two conditions determine the overall direction of reshaping; the last two its political character. By pairing either of the first two with either of the last two, it is possible to deduce four ideal-typical pathways: insulated accommodation, insulated innovation, negotiated accommodation, and negotiated innovation. In each ideal-type, two variables are considered dominant: either pre-existing institutions (accommodation) or international norms (innovation); and either technocratic engineering (insulation) or coalition politics (negotiation).

Because all four of these variables are potentially present in any given context, real-world institutional trajectories never fully fit these ideal types, but can only be approximations. And because the manifestations, interactions, and outcomes of these
variables will differ from one case to another, the typology cannot predict concrete institutional profiles. The framework I propose, then, only provides guidance for further empirical analysis: it can show us the way, but can neither take us to our destination nor tell us what to find at the end of the path.

In chapters 4 through 6, I employed this framework to analyze in detail the evolution of Turkey’s financial and agricultural regimes from 1980 to 2007. Variations in patterns of internationalization and levels of political competition are used to rearrange these units of analysis into eight distinct cases that exemplify, and thus offer insight into the workings and outcomes of, the different types. Chapter 7 introduced four non-Turkish cases to formulate contingent generalizations about each type with the benefit of a comparative outlook.

In this chapter, I put the typology mostly aside, and reflect on the implications of my empirical findings. There are four: the need to get beyond dichotomous notions of continuity and change; the inescapability of analytical pluralism; the challenges of institutional transplantation; and the political significance of mid-range institutions.

8.1 Continuity and Change

Neoliberal institutionalists assume three basic institutional scenarios: already existing market-enhancing designs may persist to support market transition; already existing market-impeding designs may persist to cause transitional failures; market-impeding designs can be changed into market-enhancing ones via institutional reform. Students of reform politics challenge this obvious functionalism at two levels. First, they
question the purported predictability of outcomes of change. In Richard Snyder’s words, neoliberal reforms do not lead to “the triumph of free-market forces” but “result in different kinds of new institutions for market governance” (2001, 195). Some new institutions may give market forces greater freedom, others may inhibit their development. What neoliberal institutionalists consider bad design may not be inherited from a preliberal past but emerge in the process of market reforms often overseen by the very agencies that advocate this view. Second, political scientists and sociologists shift attention from a simple focus on outcomes and emphasize the complex social and historical processes through which new mid-range regimes are built. While doing so, they engage numerous variables, including institutional legacies, policy repertoires, strategic collective interests, macropolitical institutions, coalition dynamics, intra-state struggles, and, to a lesser extent, international influences (Snyder 1999; 2001; Johnson 2001; Frye 2000; Luong and Wienthal 2004; McDermott 2007a; 2007b). My findings also yield strong support for such a multivariate analysis.

Common to both neoliberal institutionalism and its critics, however, is a dichotomous vision of continuity and change. Economic functionalism projects two extreme states of institutional existence—rapid guided transformation whereby bad institutions are cured via comprehensive reforms, or sticky endurance whereby good or bad institutions persist with diametrically opposed developmental outcomes. Students of reform politics are aware how such a view obscures non-reformist change, but in their preoccupation with the emergence of brand new regimes and thus origination and change, they too tend to neglect alternative pathways. Instead, they indirectly reinforce a conventional view of institutions that is sharply divided between a notion of continuity
that is all too often associated with infinite homeostasis and a notion of change that is all too often associated with revolutionary reconstruction.

This duality impairs our understanding of institutions fundamentally. The cases analyzed in this study draw strong attention to the vast realm of possibilities between these poles. First, in our sample, we have no instances of undiluted institutional stasis. Even cases of accommodation and defeated innovation (Turkish agriculture in the 1980s and 1990s, Turkish finance in the late 1990s, Chinese banking, Korean corporate governance, Argentine labor markets) display varying levels of institutional dynamism; at a minimum, policymakers rework old designs in the hope that this would suffice to address new challenges. Second, instances of revolutionary change are in the minority. “The construction of new institutions for market governance” (Snyder 2001, 3), the primary focus of the institutionalist wing of the reform politics literature, is not the dominant scenario after all. Only in cases of insulated innovation do we encounter large scale transformation, and even in these situations there is often room for partial survival and redeployment, such as the continued reliance on the age-old office of sworn bank auditors as the primary supervisory mechanism in Turkish banking in the 1980s.

What we find in cases of both accommodation and innovation, then, are gradations of change: institutional arrangements in late developers appear as works in progress, continually reshaped by a host of domestic and nondomestic forces. Looking at institutions from this window leads to an inescapably rich picture, in which arrangements change in different ways only to produce similar outcomes, perform functions that are not specified in user guides, and constitute not sites of orderly purposefulness but social tension and political uncertainty. Furthermore, in this picture institutions do not proceed
on lanes of their own, isolated from one another, but they frequently collide, entwine, and disentangle. From the eccentric reciprocity between Turkey’s fiscal, financial, and agricultural arrangements that gave way to the double redistribution of the 1990s to the significance of Korea’s novel financial regime for reinforcing the institutional preferences of the *chaebol*, and to the link between the monetary regime and incentives for labor reform in Argentina, complex interaction effects abound. Future research should try to develop more systematic treatments of these interaction effects.

To accurately capture this variety of institutional experiences, we need a much more nuanced view of institutional continuity and change. In fact, some economists (e.g. Acemoglu and Robinson 2006; Aoki 2007) and political scientists (e.g. Streeck and Thelen 2005; Boas 2007) are already moving toward less dichotomous and more integrated formulations of continuity and change. But such an effort requires more than will; as attempts to overcome this duality testify, it requires an enhanced vocabulary, new descriptive and analytic concepts. Throughout the study I tried to incorporate a few such concepts from various literatures: conversion, layering, bricolage, regrouping, diffusion, complementarity, translation, transplantation, coevolution, hybridization, and so on.

An important problem, however, is that the majority of these concepts originates from studies on advanced political economies. Although developing countries tend to offer more colorful institutional trajectories, the paucity of research on mid-range regimes in late developers on the one hand, and the bias toward instances of radical change in existing scholarship, on the other, have prohibited the emergence of a similarly rich conceptual toolkit to explore the unfamiliar, yet analytically rewarding, terrain between sticky endurance and revolutionary change. Given this limitation, the contributions of
students of developed areas become an acceptable place to start. But in the medium run, we should question, through detailed case studies, the usefulness of these concepts for analyzing institutions in late developers and try to offer reformulations and alternatives.

8.2 Analytical Pluralism

The current diversity of institutional experiences in late developers is not accidental. It is the outcome of their exposure, during the past few decades, to a multiplicity of forces and contexts that pull configurations in opposite directions and variously impact the influence and preferences of internal and external actors. The main objective of the typology I have proposed is to model this inherent complexity of institutional reshaping by bringing together different variables in a simple matrix. These variables point to different analytic traditions upon which the researcher will have to rely while examining institutional pathways. And because the typology always highlights the combined effects of at least two variables, the analysis that follows from this framework is bound to adopt a synthetic approach. Having accumulated and processed extensive empirical evidence by employing these different traditions, we can now reflect on their respective merits and limitations.

The historical institutionalist notion of path dependence, along with concepts such as self-reinforcement and feedback effects that are used to explain institutional stability and reproduction, is most helpful when sectors and policy domains are relatively undisturbed by external pressures for reorganization. Thus, the third chapter, which deals with the origins and the evolution of Turkey’s financial and agricultural regimes under an
inward-oriented model of development, could comfortably rely on this approach. Here, it was possible to start path dependence from the critical juncture of the 1930s and 1940s, and then follow the gradual remolding and eventual hardening of these regimes by looking at their organizational development and the evolving preferences of and realignments between societal and policy actors. The reinforcing mechanisms that emerged during that half-century continued to carry enormous weight for the internationally insulated Turkish agriculture under neoliberal reforms.

But the stronger the external pressures for reorganization, the more path dependence becomes a background variable. In both Turkish finance from 1980 onward and agriculture after 1999, such pressures seemed to undermine existing factors of resilience and erode self-reinforcement to bring about substantive innovation. In Mexican agriculture as well, a dense organizational network and thickly instituted historic linkages between policymakers, agrobureaucrats, local elites and smallholders mattered little in

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1 The notion of ‘critical juncture’ is the primary analytic tool through which historical institutionalists account for institutional origination and change (e.g. Collier and Collier 1991). Yet I have found it challenging to employ this notion to illuminate institutional histories of late developers in more recent times. First, if we are to take outward-oriented liberalization as a critical juncture, then given the ever-incomplete nature of this process, as reflected in calls for second and third generation reforms and the ongoing battles over international trade and financial integration, we will be forced to treat the past 30 years as one long critical juncture, which is at best analytically inconvenient. Second, if we focus more narrowly on the instigation of market reforms as a destabilizing force, this does not seem to be a critical juncture for many sectors; for Turkish agriculture, Korean corporate governance, Chinese banking etc. macro processes of liberalization did not seem to affect sectoral governance too much. Third, if we try to focus on economic crises, here again there is considerable sectoral variation, and effects sometimes tend to wear out. The 1994 shock in Turkey did not lead to strong reformist initiatives in either finance or agriculture. The 2000-2001 meltdown had more profound effects, but once growth resumed and fiscal balances improved, the reformist impetus in agriculture faded and old arrangements resurfaced. Economic difficulties that led to the Argentine crisis of 2001 triggered a renewed focus on labor market reform, but in this example as well, postcrisis governments overturned the reforms and reinstituted old arrangements. Fourth, even if we take either market reform or economic crisis as a critical juncture for a given institutional domain, the concept itself, unlike self-reinforcement or feedback effects, is not explanatory but descriptive in nature for our purposes since it says nothing about the determinants of forthcoming institutional designs. For this task, we will still have to perform a ‘conventional’ analysis that would focus on multiple external and internal factors; pinpointing a critical juncture has little analytic utility for this study. Finally, the notion of critical juncture, by overemphasizing discontinuity, is prone to the problem discussed in the previous section, that is, an unwarranted dichotomy between persistence and change.
the face of a powerful technocratic reform agenda inspired by nondomestic considerations. The only exception among our cases to this vulnerability of self-reinforcement to international pressures is Argentine labor market reforms, where moderately strong nondomestic incentives were trumped by the utter indispensability of pre-existing arrangements for staying the reform course in all other areas.

Whereas historical institutionalism, at least in the way I engage this approach, is effective only under particular conditions, an IPE-informed perspective is useful at all times. Yet nondomestic variables have inexplicably remained on the fringes of the existing scholarship on sectoral institutions in late developers. At a minimum, it is important to detect the absence of strong international incentives for sectoral reorganization, for this alerts us to the potential significance of pre-existing institutions and path dependence for subsequent configurations. But when external market and policy incentives are strong, as in the majority of our cases, it becomes categorically impossible to trace institutional pathways without systematic reference to nondomestic phenomena. In both Turkish finance throughout the entire period analyzed in this study and Turkish agriculture after 1999, the neoliberal bureaucratic will to converge on international norms was the overarching theme of policy debate and political struggles over sectoral regimes.

The relationship between international norms and the different dimensions of external pressure is nonetheless a complicated one. Norms that are comparatively weak or politically or organizationally too taxing to enforce constrain the effects of policy exposure; this was in part why Turkey’s support regime in the 1980s and Argentina’s labor market arrangements in the 1990s remained relatively stable despite the overwhelming influence of international agencies over domestic policymaking. Without
sufficient market and/or policy pressure, however, even strong emergent norms will have little inspirational value, as exemplified by both Turkish agriculture and Chinese banking in the 1990s. Finally, there are also times when the terms of market integration and emergent international norms pull in different directions, as was the case for Turkish finance in the late 1990s and has been the case for Turkish agriculture since 1999; this in turn complicates innovative projects. The upshot of this complexity of international influences over domestic institutions is the need for multi-factor analysis, which should combine a focus on general strategies of market integration (e.g. export-led vs. finance-led) and wider patterns of policy exposure (e.g. the extent of IFI influence) with a focus on sector-specific dynamics (e.g. trade position of the sector within the general strategy of integration, the particular demands of the IFIs and regional/international organizations, the state of the global normative wisdom in that sector etc.). Drawing out the implications of the links between these different nondomestic phenomena for institutional development poses an interesting challenge for future research.

The obvious limitation of an IPE-based explanation is that external incentives cannot shape institutions on their own; they need to be filtered by domestic agents and packaged into political projects. I have argued that technocratic engineering and coalition politics are two contending ways through which incentives for accommodation or innovation are transformed into concrete institutional strategies. I have also pointed out strong synergies between technocratic engineering and international norms, and coalition politics and pre-existing institutions. As seen in several cases, these two pairs generate ‘purer’ types of reshaping, which lead either to top-down restructuring at significant risk
to attendant interests (insulated innovation) or redeployment of existing arrangements usually to the benefit of societal and intra-state actors (negotiated accommodation).

This focus on technocrats and coalitions highlights the importance of conventional political analysis for making sense of institutional trajectories. Two points deserve emphasis. The first is the significance of proper alternatives to incumbents and their institutional strategies. Authoritarian episodes exclude this possibility abrasively. The tendency of nondemocratic governments to technocratic exclusion poses problems even for those social groups whose interests are favored by the policy regime, as was the case for Turkish bankers and industrialists in the 1980s. Consequently, political pluralism, at the very least an electoral democracy, is a necessary condition for social actors to manipulate institutional projects. Democracy itself is not sufficient for such influence, though. Economic hardships, often accompanied by powerful external policy pressures, may also accentuate technocratic engineering and momentarily insulate executives from societal and intra-state forces, such as in Turkey in 1999-2002, which ironically was also a period of externally-inspired democratic progress. In fact, even under strict coalitional constraints that give voice to social groups associated with an institutional domain, such contingencies may fuel technocratic outbursts, as exemplified in Menem’s attempts to circumvent unions through executive decrees.

This brings us to the second point. Assuming that authoritarianism is a thing of the past in the majority of late developers and that non-authoritarian technocratism is an exception rather than rule, the determinants of collective actors’ capacity to influence decisionmaking under competitive politics, surely a central concern for conventional political analysis, also become a fundamental concern for institutional analysis. At this
level, we observe four recurrent factors. Arguably the most important is organization, associational prowess; another is electoral salience; a third is formal and informal linkages with policy elites; and a final one is the preferences of other societal actors. A well-organized and electorally salient social group with strong allies within the bureaucracy and the ruling party and whose preferences are in tune with, not detrimental to, or trump those of other players yields immense influence, in particular during periods of intensified political competition. Such actors (e.g. Turkish peasantry after 2002, but especially Argentine organized labor) can successfully oppose reformist impulses and may even force a partial or full resurrection of old arrangements under ongoing innovative projects.

8.3 Transplantation

That developing countries can improve their fortunes by acquiring institutions that are simultaneously market-sustaining and socially viable is a common belief among students and practitioners of development today. The underlying assumption, of course, is that institutional domains in late developers are seldom occupied by arrangements that fit this description. Therefore, such virtuous institutions can be acquired only through purposive action, through comprehensive reforms that are often inspired by apparently more successful designs in advanced political economies. Chapter 6 focuses on how this neoliberal institutionalist wisdom has been put into practice in the Turkish context. My findings offer little support for this view. Only in finance did reforms proceed as planned, but under exceptionally favorable domestic and international circumstances and through
policy processes that largely excluded sectoral actors and undermined their perceived short-term interests. In agriculture, as well as in a number of other areas briefly mentioned, reforms ran into serious organizational and political problems, exacted significant social costs, and were either implemented with major deviations or partly subverted afterwards. There are thus good reasons, as I have concluded in that chapter, to remain skeptical about both the feasibility of the reform process itself and the desirability of its outcomes.

The institutional reform agenda revives a long-standing concern of the development literature: the complications that result from attempts to model development on the past or current practices of developed societies (e.g. Riggs 1964; Badie 2000). Critiques of neoliberal institutionalism thus particularly target its assumptions of transferability, in other words, its negligence of institutional endogeneity (Przeworski 2004) and its proclivity to rash transplantation (Chang 2002; Evans 2004; Leftwich 2005). This study has significant findings that relate to these issues.

Although reforms concerning sectoral regimes come wrapped in a thick developmental discourse, in actuality they frequently serve as agents of objective compulsion in the process of market integration. At this level the experience of economic sectors differs from some other areas of institutional reform, such as anticorruption or social security. In banking, the BIS standards have long been a guiding force and Turkey’s regulatory laxity in the 1990s was a deterrent for potential foreign entrants; size does matter for stability and competitiveness, and a stricter regulatory environment proved necessary for market consolidation. In agriculture, Turkish governments in the mid-2000s took advantage of the ongoing stalemate in agricultural trade talks while
reinstituting old-style subsidies, but these instruments will be much less available in the event of an agreement. In fact, in the summer of 2008 the second AKP government terminated DIS payments, and declared a full return to old-style price supports. Observers are skeptical, though, suggesting that a revival of the DIS is quite probable given the EU constraint and the availability of a feasible infrastructure. Other novel instruments are still in operation as part of the hybrid support regime.

And in both sectors, institutional reform agendas have been tailored in accordance with existing or projected EU constraints. Transplantation in that sense is not a simply misguided policy advice rooted in the fads and fashion of the day; at times it emerges as a concrete necessity.

We also need to distinguish between transplantation on the one hand, and what institutionalists call ‘translation’, on the other. Translation, which could be taken as sensible diffusion, has been a common practice. The preliberal arrangements in both finance and agriculture were indeed imported ones, but they were adapted to the Turkish scene through a long evolutionary process marked by continuous negotiations with attendant interests; this way, they functioned reasonably well under state-directed developmentalism. In light of this experience, the problem with transplantation appears to be two-fold. First, economic globalization and the increased weight of international and multilateral agencies in defining what is normatively acceptable narrow the design choices for importation. While constructing new sectoral regimes in the 1930s and 1940s, Turkish rulers were inspired by German, Italian, French and Soviet models, mixing and matching a range of design characteristics, combining them freely with existing and evolving local practices, and flexibly rearranging emergent institutions over a long period of time to balance changing economic and political priorities. Such freedom, diversity and flexibility do not exist today. Despite the World Bank’s purported commitment to complementing (rather than uprooting) existing arrangements, sectoral institutional

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2 In fact, in the summer of 2008 the second AKP government terminated DIS payments, and declared a full return to old-style price supports. Observers are skeptical, though, suggesting that a revival of the DIS is quite probable given the EU constraint and the availability of a feasible infrastructure. Other novel instruments are still in operation as part of the hybrid support regime.
reforms continue to rely on a logic of monocropping with little tolerance for arrangements that are considered categorically market-disruptive, regardless of their social or political utility. This uncompromising attitude is in turn the primary source of political tension surrounding reform projects. It makes novel designs less adaptive and more brittle, leaving them open to threats of subversion from above and below.

A second and related problem with transplantation is economic actors’ varying levels of vulnerability to externally imposed designs. The contrasting experience of Turkish peasants and bankers brings this problem into sharp relief. Certainly there were costs attached to top-down restructuring in banking, as seen dramatically in the eradication of parasitic smaller and medium-size finance capital, but also in sector-wide job losses and declining profitability. In the longer run, however, the new regime offered stability, a more collaborative integration with international market forces, and resilience to external shocks. It thus imposed what Stark and Bruszt call “beneficial constraints” that proved crucial for “long-term competitiveness” (1998, 199). Peasants’ experience was radically different. Their livelihood tied to archaic forms of state intervention and their exit options limited, Turkey’s smallholders were not in a position to adapt to a new order that pit them directly against more productive and often better protected agrarian sectors in the developed world. These divergent sectoral effects of transplantation stem not from the political manner in which reforms are implemented but from their normative content. The institutional responses to the problems that emerge in the process of outward-oriented liberalization have different implications for different collective

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3 At the time of writing (January 2009) no Turkish banks needed rescuing despite the deleterious effects of the ongoing global financial crisis. To the contrary, the Turkish financial sector grew by 9% in 2008, despite a sharp decline in overall GDP growth.
interests. It is this fundamental variation and its macro consequences to which we turn in the concluding section.

### 8.4 From Sectoral Institutions to National Patterns

Sectoral regimes are important because they define the rules by which social groups operate as economic agents in the national marketplace, with major consequences for their exposure to international market forces. Such regimes are the direct products of historic relations between these social groups, the state, and other economic agents, so their reconstruction also corresponds to a reconstruction of these relations. Sectoral institutions, in short, are solid indicators of both past and current economic and political fortunes of collective actors. For this reason, their trajectories contain important clues about wider political-economic patterns.

The way sectoral institutional paths reflect broader political-economic projects is forcefully exemplified in the comparative cases studied in the previous chapter. Chinese officials’ reluctance to abandon state dominance in banking represented their continued commitment to a large public productive sector crucial to both social welfare and bureaucratic control over the economy. The inability of Korean bureaucrats to rein in the *chaebol* was a reflection of not only changing state-business relations but also changing state-labor relations. Mexico’s radical agricultural reform challenged the historic links between the state, the ruling party, and smallholders, and destabilized national politics while also triggering efforts to reconstitute these links at the subnational level. The
zigzags of labor market reform in Argentina showed the significance of a single mid-range institution for the political sustainability of the entire neoliberal project.

In the Turkish context as well, the broader implications of institutional reshaping were profound. Through the window of evolving governance mechanisms in Turkish finance and agriculture, we were able to peer into the rearticulation of key popular and elite interests within a political-economic sphere whose organizing principles shifted fundamentally with the demise of state-led developmentalism and the social compromises that lay underneath. The resultant institutional profiles we have analyzed came deeply entwined with wider political, economic, and ideational changes; they reflected the preferences of state and societal actors not only toward sectoral governance but often the governance of the entire economy. If these linkages between sectoral and national patterns of reshaping are not explored more systematically in this study, it is because such an examination, which cannot be done casually, would have distracted the analysis from its main concerns in a major way. In closing, however, I propose two general points that deserve further study.

In agriculture, the dynamic continuity of populist corporatism offered an important economic reward for rural interests, but exacted a grave cost on Turkish politics. On the one hand, it partly shielded Turkish peasants from the potential ill-effects of neoliberalism. With the exception of two technocratic episodes two decades apart, Turkey’s petty producers were not exposed to the level of impoverishment, social dislocation, and political atomization that ravaged the countryside in other liberalizing late developers that had once offered comparable protections to smallholders (e.g. Kurtz 2004). Rather, the preservation of rural transfers in Turkey ensured that the inevitable
decline of the sector stayed on a path of ‘soft landing’ for the mass interests involved. On the other hand, populist corporatism, as in other instances of this phenomenon, continued to act as a deformed substitute for social democracy (Sandbrook et al. 2007, 28-9). Just as under import substitution, under neoliberalism as well, populist side payments and corporatist mechanisms of control stood in the way of mass mobilization and genuine democratic participation in the Turkish countryside. The center-right bias within the support machine made certain that center-left parties would fail to combine urban and rural popular grievances to push for a feasible social democratic alternative at critical moments of political and economic opening. The paternalistic protection offered by populist corporatism, regardless of the transformations it underwent, reproduced a pernicious pattern of national politics that could not be fully broken to date.

Even then, there are increasing challenges to this pattern, as reflected in the move toward democratic consolidation and the erosion of formal channels of corporatist intermediation in recent years. The question for Turkey thus becomes a familiar one—whether politicians’ quest for democratic legitimacy in the absence of formal corporatism will suffice to protect popular interests from the destructive tendencies of liberal globalism in the long run. The answer to this question will depend not only on domestic political and institutional projects, which for now seem to have aligned through a hybrid support framework, but also on institutional norms and dominant policy preferences in advanced political economies, which appear to be on the brink of major renovation.

If the trajectory of the agricultural regime gives us a glimpse of the Turkish state’s scrambles with popular interests and democracy in a neoliberal age, the evolution of the
fisco-financial regime offers clues about its relations with elite interests and capitalism in general. From the mid-1980s onward, Turkish governments faced an increasing polarization of financial and industrial interests that decidedly worked against the latter. Their failure in the 1990s to prevent the atrophy of a nascent export-led developmentalism, their easy capture by pockets of financial rentiers, and their inability to establish even a semblance of control over a nebulous public expenditure regime at a time of heightened distributive tensions revealed how “overstated”, to quote Nazih Ayubi’s (1995) title, the Turkish state actually was in its autonomy and especially bureaucratic capacity. Surely regime troubles, party fragmentation, and exploitive attacks by international rentiers posed additional constraints, but in the final analysis the regulatory resources of the Turkish state had to be rebuilt from ground up. It is at this level that we have found the stickiest collective action problems: capital factions demanding greater pro-market state action but deeply divided, even within the same sector, over the terms of such activism; traditional and reformist bureaucratic segments both clashing with politicians over which new regulatory capabilities to nurture, and so on. This steep learning curve involved in the building of a regulatory capitalism exacted structural economic costs no less serious than the political cost of populist corporatism: an inability to redirect banking capital into productive usage; a failure to guide industrial development to regain export competitiveness; and a lack of defenses against the perils of financial integration.

The replacement of the shaky alliance of populist politicians, traditional bureaucrats and financial rentiers with the ideationally and politically stronger coalition of industrialists and IFI-supported liberal bureaucrats in the postcrisis period fuelled a
reformist momentum through which an array of new regulatory capabilities was built. But these novel capabilities, inspired by the latest global norms, remain relatively untested. Turkey’s impressive growth rates, fiscal stability, and virtuous financial deepening after 2002 were achieved in a favorable international economic conjuncture. The real value of the ‘cautious new world’ of fisco-financial regulation will be judged strictly on its ability to shield Turkey, as much as possible, from the unfolding global economic catastrophe and help it back onto a path of sustained growth.

There are thus good reasons to expect the basic scenario encapsulated in the typology to be played out vividly during the next few years. International market and policy constraints will generate incentives for adjustment in current sectoral regimes. Domestic policy and societal actors will interact to transform these incentives into tangible projects based on their political capabilities and strategic preferences. From this interplay of the domestic and the nondomestic, future institutional configurations will emerge, with profound consequences for collective fortunes.
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