

Uneven Governance and Fiscal Failure: The Adjustment Experience in Turkey

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Starting in 1980, Turkey embarked on an ambitious program of stabilization and structural adjustment. The speed with which macroeconomic stability was established and the rapid response of the private sector to the new regime made Turkey a success story among adjusting countries. Turkey has succeeded in liberalizing foreign trade, the financial sector, and the capital account, and in transforming a protected, inward-oriented economy into an export-oriented and private-sector-driven economy with a number of sectors that can compete internationally.

Nevertheless, fourteen years later, in early 1994, Turkey was once again faced with a major macroeconomic crisis, and had to embark on a new stabilization program. The crisis was driven by unsustainable fiscal deficits—overall public sector borrowing requirements (PSBR) reached almost 12 percent of gross national product (GNP) in 1993. The purpose of this chapter is to examine the economic reform experience in Turkey and attempt to explain the factors that led to the failure in fiscal policy.

The main argument of the chapter is that the failure in fiscal policy originates in a failure of

governance capacity. The aspect of governance that is most salient in explaining the Turkish experience is the inability of the state to resolve problems of cooperation between political actors. It is argued that the Turkish experience with fiscal policy, or, more specifically, the way state resources are used as an instrument of political competition, lends itself to conceptualization as a problem of cooperation. The likely outcome is the uncooperative one. In the context of competition to acquire or maintain political power, political actors behave in a predatory manner and distribute the resources of the state to political constituencies, causing inflation and macroeconomic instability. In the more desirable outcome, by contrast, political competition is less predatory, has less destructive fiscal implications, and the political actors agree not to resort to “excessive” transfers and subsidies as a means of competition. Given the incentives to deviate into uncooperative behavior, however, the realization of this more desirable outcome requires either the existence of norms that restrain predatory behavior or mechanisms that allow the actors to commit themselves not to deviate. The governance failure is associ-

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ated with the absence of the norms and mechanisms that would support cooperative outcomes.

The absence of such norms and mechanisms preceded the period of economic reform. Indeed, the inability of the mainstream political actors to reach compromises and to cooperate to resolve fundamental problems facing the country was an important factor in the economic and political crisis that afflicted Turkey in the 1970s. It seems that the failure is partially associated with a party structure that is excessively sensitive to the particularistic demands of constituencies. In any case, it is argued that this deficiency in governance was not addressed by governments that pursued economic reform in the 1980s. Instead, the centralization of governmental authority and an increase in the discretion over state resources during this period probably aggravated the problem of cooperation.

The existence of such a governance gap has important implications for the conduct of macroeconomic policy. One of the conclusions of the chapter is that a sustained resolution of the problem of macroeconomic instability may require structural reforms that change the way the state manages distributional conflicts in society. It is argued that in the case of Turkey, attempts to establish macroeconomic stability by suppressing distributional demands temporarily, without undertaking such structural reforms, has preserved the vulnerability of the fiscal accounts to the process of political competition.

This failure, however, was coupled with considerable success in another dimension. By the end

of the 1980s there was a wide consensus in the country that the preferred model of economic development would be predominantly market-oriented; the country would not be isolated, but instead would become increasingly integrated with the rest of the world. Moreover, there has been a significant change in the business culture: on the one hand, entrepreneurial activity is more appreciated. On the other, protectionist demands from industry find less support from public opinion.

This chapter argues that this consensus builds an irreversibility into economic reform and discusses the contribution of Ozal, the main architect of economic reform and the head of the government during the reforms of the 1980s, in the development of this consensus.

This combination of factors puts Turkey in an interesting situation. Fifteen years of reform have created a vibrant private sector, and a state that is lagging behind in attending to important regulatory and social functions. Having reformed the aspects of the economy that relate to the economic activities of the private sector, it seems that the majority of the remaining tasks have to do with reforming the state.

The rest of the chapter is organized as follows. The next section provides a brief historical background. The third section describes the stabilization and adjustment program and documents the fiscal deterioration. The fourth section discusses the governance aspects of the stabilization and adjustment period. The fifth section concludes the chapter.

The State, the Economy, and Party Politics before 1980

During the first two decades of the Republic, political power in Turkey was monopolized by the Republican People's Party (Cumhuriyet Halk Partisi, CHP), which represented a coalition of military-bureaucratic elites at the center, and traditional notables of the otherwise disconnected periphery. Because of the dev-

astating impact of the Great Depression in 1929 and the perception that the weak entrepreneurial base, concentrated mainly in commerce and dependent on foreign markets, could not promote structural transformation and industrialization, the 1930s witnessed a systematic effort of state-led social change. In the realm of economic policy,

this entailed an array of state activities, including imposition of exchange controls, major public investments in manufacturing, nationalization of foreign and local companies delivering public services, and imposition of import duties and quotas to protect industry. Private manufacturing started to develop under the tutelage of the state, and with the active participation of the bureaucracy (Keyder 1987).

The transition to multiparty politics occurred in 1945, when the CHP allowed the formation of an opposition party, the Democratic Party (Demokrat Parti, DP). The introduction of political competition and the ascendance to political power of the newly formed DP in 1950 represented a milestone in the country's political and economic development. With the introduction of political competition, peripheral social groups, especially the peasantry, were actively courted by political parties, particularly the DP, for the first time. The political system became sensitive to the demands of diverse groups, especially those in the rural areas, creating incentives for these groups to participate in the political process. Whereas during the single-party era patronage was a form of exchange between the state and local notables and did not entail the active participation of peasants in the political process, political competition enabled peasants to acquire power and to bargain for services. Although the leadership of the DP was from the central elite, instrumental in their succession to political power was their ability to forge and mobilize a wide-ranging coalition of landed interests, small peasantry, and urban mercantile groups. The DP advocated political liberalism and promised an end to the oppressive reach of the state. An appeal to religious sentiments

found resonance, especially in rural areas alienated by the top-down secularism of the CHP (Sunar and Sayari 1986, p. 173).

The multiparty system and political competition created incentives to use the resources of the state to win political support. Political parties, especially their local organizations, became avenues for deals exchanging support during elections for a variety of benefits, ranging from employment in the public sector, roads, credit, waterways, and "political factories" to purely personal assistance in alleviating the burdens of bureaucratic red tape. Political entrepreneurship—the ability to represent the interests of constituents in party organizations, and in local and even national political and administrative forums, and the ability to make deals with constituents—became a critical trait for success in politics. With accelerating migration to the cities, particularly after the 1950s, patronage networks in urban settings became very important elements of the political process as well.¹

The DP was more liberal in its economic policy than the CHP; it came to power as the representative of deeply rooted antibureaucratic sentiment. While the 1950s witnessed a booming private sector, however, the scope of state intervention did not diminish significantly.² If anything, perhaps the political principles guiding the allocation of resources commanded by the state changed to allow the newly represented groups to receive a larger share, and the logic of political competition gained prominence.³

In 1960 the DP regime was overthrown with a coup. The new Constitution envisaged "planned development," and the State Planning Organization was formed. Political power was soon trans-

1 See Sayari 1977; Sunar 1990, forthcoming; and Sunar and Sayari 1986 for discussions of patronage systems in Turkey and their link to the development of the multiparty system. Leder (1977) discusses the impact of political competition in rural areas. Karpat (1974) traces the development of the political entrepreneur in the urban shantytowns.

2 The DP experimented with a more liberal import regime in the early years of its rule, but returned to rigid import controls by 1955.

3 Keyder (1987) describes Menderes, the leader of the DP and the prime minister, in the following way: "he seemed to despise the ordinary constraints of accounting and was endlessly inaugurating public works projects without regard to cost" (p. 134). These were financed through the Central Bank, which in turn caused a doubling of prices between 1955 and 1959.

ferred to civilians. The center-right Justice Party (Adalet Partisi, AP) became the inheritor of the DP tradition, while the CHP gradually came to resemble a social democratic party. The two competitors differed in the emphasis to be placed on growth and equity and the desired sizes of the private and public sectors of the economy, but at least until the late 1970s there was a consensus among the main political actors on the basic premises and soundness of what has been called import-substituting industrialization (ISI). The goal of industrialization was paramount, and it was supported by business and labor. In the Turkish version of the ISI, almost no economic group was left out, and each obtained something from the state. Business and labor participated as the agents of industrialization. Peasants participated because they had the power to vote.

The consensus over ISI entailed a large extent of state intervention: state-owned banks allocated subsidized credit to the private sector, especially to industry and agriculture. While state economic enterprises (SEEs) were originally conceived as the main engines of industrialization in the 1930s and 1940s, when the private sector was very weak, over time they came to play a crucial role in the development of the private sector. They were dominant in the production of critical intermediate inputs, such as chemicals and petrochemicals, which were sold to the private sector at subsidized prices. They were also instrumental in subsidizing agriculture through the production and subsidized allocation of fertilizers. Finally, they were an important source of employment for surplus labor.

Import licenses were another significant source of rents for the private sector. Import-substituting private industry thus benefited from protection, from the rents associated with the quantitative restrictions that characterized the import regime, subsidized inputs, various forms of fiscal incentives, and subsidized financial resources. The agricultural sector, in addition to receiving subsidized credit, also benefited from support prices—

which, on average, surpassed world prices—and subsidized fertilizers and seeds.

For business, personal contacts with members of the cabinet or with the bureaucracy have been important for access to incentives, subsidized credit, and government contracts. Apart from personal contacts by leading entrepreneurs, business associations have generally been weak in exerting direct influence on the policymaking process (Bugra 1994; Onis and Webb 1994). Nevertheless, these associations were influential as voting blocks in elections. The voting power of small business and agriculture probably explains the very narrow tax base of public revenues in Turkey, as well as persistent efforts of the center-right parties to dominate the elections of business associations.

In agriculture, the predominance of small-holdings precluded direct influence on the government or its ministers. The main channels of influence were elections, local party congresses, and contacts with local party leaders. To the extent that organizations existed, their survival and any influence they had was mainly the product of the center-right parties', especially the AP's, establishment of control over these groups by placement of party sympathizers in their governing bodies (Erguder 1981, 1991).

The transition to multiparty competition affected the bureaucracy as well. The CHP regime had cultivated a bureaucratic elite, one that was loyal to the mission of state-led modernization and Westernization. It evolved to see the formulation of public policy as its legitimate responsibility, and it did not have a conception of public interest that would arise out of a competitive political process: "Thus, it was a responsibility of the bureaucrats to carry out public services on the basis of 'objective' criteria, and not in accordance with the 'whims' and 'illegal' interventions of the politicians" (Heper 1990, p. 609; see also Heper 1987, 1989). The bureaucratic elite also saw itself as the guardian of "Kemalism" and its statist orientation toward public policy, and viewed the new politi-

cal elite as opportunists who misled and exploited an uneducated population. The political elites portrayed the bureaucracy as alienated elitists who represented an authoritarian state and were unresponsive to the expression of popular demands. The political class attempted to subjugate the higher civil service rather than devise clear mechanisms of authority and delegation, if only to turn the civil service into a passive and obedient agency that distributed the politically directed spoils. This conflict generated several outcomes, especially in the 1970s. First, the bureaucracy became extremely politicized, and the civil service ranks came to be filled by party clients and partisans. Changes in governments were followed by major reshuffling of the civil service. The civil service also became weak financially, and real salaries declined significantly over the years, which discouraged talented people from joining the bureaucracy. The bureaucracy, in turn, tried to protect its power by engaging in "pathological bureaucratization" (the term is from Heper 1977, p. 80)—policies imposed by governments would be sabotaged in a maze of rules and regulations.

By the end of the 1970s, on the eve of the adoption of a major program of structural adjustment and a military takeover, Turkey was in a deep economic and political crisis. There was a severe crisis of governance. The party system had become polarized and fragmented, leading to weak governing coalitions at the mercy of small parties. As new and more ideologically oriented parties emerged, the mainstream parties on the right and the left became unable to cooperate sufficiently to address some of the basic problems afflicting the country—most notably, the need to curb political violence and to find solutions to a mounting balance of payments crisis. The inability of the parties in the center-right and center-left to cooperate allowed ideologically oriented parties to bargain for political power incommen-

surate with their electoral power (Erguder 1988, pp. 122, 124).

A variety of reasons have been proposed to explain the failure of governance that increasingly characterized the 1970s. Such explanations have included the emergence of new cleavages generated by the immense social transformation of Turkey as a result of rapid economic development; a tendency among political leaders to see political power as absolute; and the attempts of the mainstream parties to counter competition from new, radical groups, both on the right and the left (see Erguder 1988; Ozbudun 1988; Turan 1988). What is especially interesting for the purposes of this chapter is that the combination of the state's discretionary command over a large amount of resources and a party system that became extremely responsive to the localized and particularistic demands of its constituencies inhibited the political system's ability to address matters of public policy. The first component of this combination is straightforward, but the second may require further exploration.

This excessive sensitivity⁴ has been noted by many political scientists in Turkey, and its origins are likely to lie in the particulars of the patronage system that developed in response to the introduction of political competition. It seems that in addition to the dynamics of interparty competition, patterns of intraparty competition and bargaining also played a role. Standing as a candidate for parliamentary elections depended on the candidate's ability to obtain the support of party delegates at the subprovincial level, where support was made available in return for contingent claims on various benefits if the candidate was successful in the elections. The delegates acted as "brokers" between the party and the constituency, and they were appointed by the party leaders because they could mobilize constituencies, provided, of course, that the broker himself could

4 Gunes-Ayata (1994, p. 36) calls this the "subservience" of party officials.

deliver to the constituencies. To honor the liabilities, the candidate relied on the party leadership. While this granted substantial authority to the leaders of government parties, as well as an ability to control the actions of their deputies, the same mechanism implied that the maintenance of leadership status was contingent on the government's ability to cater to the liabilities: the deputy could defect if the party leadership failed to grant the service. Party leaders, including those in the government, became preoccupied with keeping their parties together, rather than attending to pressing public policy. The legislature ceased to be an institution of deliberation and legislation, and was in constant stalemate.⁵

[T]he domination of constituency concerns over others in the behavior of the legislators affected the functioning of the GNA [Grand National Assembly, the Parliament] in several ways: First, many of the sessions of the legislature could not start because most legislators were so busy that they could not attend sessions, usually making it impossible for a quorum to obtain.

Second, parliamentary duties turned into instruments which a deputy used for the exclusive advancement of his own career. For example, a position on the committee on State Economic Enterprises, which is supposed to exercise oversight on the activities of these institutions, became a channel through which jobs could be found for constituents. Membership in the Committee of the Budget and Economic Planning became an arena where, mostly, pet constituency projects could be pushed. In summary, the Parliament became a grand-spoils operation, little concerned with other functions. [Turan 1988, p. 91]

It seems that the system suffered from a severe public goods problem: whenever a given liability was honored, all the benefits accrued to the specific constituency, but the cost (ultimately macroeconomic disequilibria and inflation) was socialized. This created an incentive to overspend. The institutional structure of fiscal

Table 1
Macroeconomic Indicators
Percent

	Growth rates			PSBR/ GNP
	GNP	Industry	Change in wholesale ^a price index	
1978	2.9	6.6	52.6	
1979	-0.4	-5.6	63.9	
1980	-2.3	-6.0	107.2	10.5
1981	5.3	7.4	36.8	4.9
1982	3.7	4.9	25.2	4.3
1983	4.6	8.0	30.5	6.0
1984	7.8	10.1	50.3	5.3
1985	4.5	6.3	43.2	3.5
1986	7.5	8.8	29.6	3.6
1987	9.3	9.5	32.0	6.1
1988	1.5	3.2	70.5	4.8
1989	0.9	3.1	64.0	5.3
1990	9.8	9.0	52.3	7.6
1991	0.5	2.7	55.3	10.3
1992	6.4	6.8	62.1	10.6
1993	8.1	8.7	58.4	11.7
1994	-6.0	-3.9	120.7	8.2

a. 1978-87, State Institute of Statistics, 1981 weights; 1988-93, State Institute of Statistics, 1987 weights.

Source: GNP and industry growth rates: 1978-79, OECD (1987) Appendix table B; 1980-91, OECD (1994) Appendix table A (new series); 1992-94, calculated from SIS figures. Percent change in wholesale price index: 1978-81, OECD (1987) Appendix table E; 1982-94, OECD (1995) Appendix table E. PSBR/GNP: 1980-83, OECD (1990) table 21; 1984-94: see table 6.

expenditure management conformed to the political necessities. Information flow was extremely poor, and there was no system to monitor the efficiency of fiscal expenditures. The Central Bank was essentially subordinated to the government: fiscal deficits were financed mainly through monetary expansion, and the system also entailed substantial quasi-fiscal subsidies distributed by the Central Bank and state-owned banks.

5 The Parliament's inability to elect a president in 1980 was one of the most visible indicators of its failure to function.

Another important characteristic of the system was that it made political cooperation between different parties difficult. The increasing inadequacy of cohesion within the parties and the need of political leaders to juggle to cater to party members made it difficult to bargain successfully with other party leaders.⁶ Difficulty in cooperation exacerbated the public goods problem mentioned above, and with it, fiscal and quasi-fiscal balances.

The economic performance of the system was, on average, quite satisfactory until 1977. There were several instances of balance of payments problems, but they were resolved without straining the boundaries of the ISI framework. Between 1950 and 1975 real GNP increased about 4.5 times (an average growth rate of 6.2 percent). The economy went through significant structural change; the share of industry in gross domestic product (GDP) increased from 11 percent in 1950, to 18 percent in 1965, and to 22 percent in 1975. Growth was inward-oriented; between 1975 and 1980 the export/GNP ratio was less than 5 percent.

When the first oil shock hit in 1973, Turkish policymakers responded to the worsening cur-

rent account deficits by running down reserves and borrowing abroad. Expansionary policies continued. The currency remained overvalued, and by 1979 international reserves were depleted. Lack of foreign exchange crippled industrial production (see table 1).

Successions of coalition governments did not exhibit any capacity to deal with the political or the economic crisis. Two stand-by agreements with the IMF, in 1978 and 1979, failed because the government was unable to curb expenditures. In November 1979, the AP came to power and Demirel became the prime minister. On January 24, 1980, the government launched a program of economic stabilization and liberalization. The architect of the program was Mr. Ozal, a former civil servant at the State Planning Organization (SPO). Political and social instability continued. The military took over in September 1980. The Parliament was dissolved, and all political parties were closed down. This represented a grand bargaining failure between the mainstream parties on the right and the left, the AP and the CHP. These were the parties that had the most interest in preserving democracy and cooperating to find viable solutions to the economic and political crisis. They failed.

The Adjustment Period

The military takeover changed the rules of the political game. The Parliament was dissolved, and all political parties were closed down. Union activity was suspended. Nevertheless, there was continuity in economic policy. The military government retained Ozal and granted him the main responsibility for conducting economic policy. Following a banking crisis in 1992, Ozal and his team resigned. The break was brief, and in 1983 Ozal returned as prime minister.

As emphasized by Onis (1992, p. 11), the military regime enjoyed legitimacy and support because it was seen as a temporary solution to the governance crisis that had gripped the country, especially because the military was successful in restoring law and order. Nevertheless, the return of Turkey to fully competitive politics with no entry barriers was gradual, and a brief summary here will be useful. First, general elections took place in 1983.⁷ The military allowed only a small number of parties to participate in the

6 See Strom 1994 on the importance of intraparty bargaining in the degree of success of interparty bargaining in political coalitions.

7 See the Appendix for a chronology of political developments after the military takeover.

elections. Former political leaders were banned from participating in politics. Two of the parties that ran in the 1983 elections, one on the right and one of the left, were led by former soldiers and supported by the military. The third, the Motherland Party (Anavatan Partisi, ANAP), was led by Ozal himself. ANAP easily won the elections and Ozal became the prime minister.

Other parties eventually were allowed to form. On the right, the Great Turkey Party (Buyuk Turkiye Partisi, BTP) was formed in 1983, and was identified as the continuation of the AP. It was closed down by the military in the same year. The AP tradition was then picked up by a new party, the True Path Party (Dogru Yol Partisi, DYP). On the left, the Social Democracy Party was formed. This later was merged with the Populist Party to form the Social Democratic Populist Party (Sosyal Demokrat Halkci Parti, SHP).

The intensity of political competition dramatically increased after the banned leaders were given the right to engage in politics in a 1987 referendum. Demirel and Ecevit, the former leader of the CHP, and about 100 other politicians reentered the political arena. The majority in the referendum was a slim 100,000 votes. Soon after the referendum, in the general elections of November 1987, ANAP received 36 percent of

the votes and, thanks to the electoral law, 63 percent of the seats in the Parliament. After that, electoral support for ANAP decreased. During the local elections of March 1989, ANAP's share dropped to 22 percent, and it emerged as the third party. ANAP lost the general elections in 1991, and Demirel, as the leader of the True Path Party, became the prime minister in a coalition government formed with the left-of-center SHP.

Throughout this period there were no fundamental divergences from the main trend in economic policy, which was to progressively reduce controls over private sector economic activity, reduce protection from imports, enhance export orientation, and increase Turkey's integration into the world economy. Indeed, as will be stressed in the next section, a consensus emerged that Turkey's future lay in an economic regime that was fundamentally different from the ISI. In apparent contradiction of this general trend, the weight of the public sector in the economy did not diminish. In the context of intensifying political competition, deficits in the public sector remained a particularly intractable problem, endangering macroeconomic stability. The next three sections will review the political dynamics behind fiscal deterioration.

Economic Reform: An Overview

The January 24 economic reform program had ambitious objectives.⁸ The program envisaged nothing less than a fundamental change in the mode of economic development, from a protected, inward-oriented approach with extensive state regulation and intervention in many areas of the economy to a stance that was export-oriented, with the private sector as the main engine of growth.

The initial stabilization package included a steep devaluation, price deregulation for industrial products produced by the private sector, and large increases in the prices of SEE products. Interest rates were deregulated in June 1980. Initial attempts at trade liberalization were undertaken in 1981. By 1982, the public sector borrowing requirements as well as the rate of inflation were reduced, and the economy resumed growth

⁸ A very partial list of detailed accounts of the reform process would include Celasun and Rodrik 1989; Krueger and Aktan 1992; Krueger and Turan 1993; Onis and Webb 1994; and Rodrik 1990, 1991.

(table 1). The outstanding aspect of growth was its export orientation—between 1980 and 1982 the exports/GNP ratio doubled, to 10 percent.

With Ozal's return as prime minister in 1983, economic reform proceeded at full speed, and the next few years witnessed reforms in diverse areas. In the financial sector, banking deregulation was accompanied by better supervision; a foreign exchange market, a stock exchange, and an interbank market were created. Foreign exchange transactions were deregulated, and the capital account was liberalized in 1989 (for details, see Atiyas and Ersel 1994). In the area of foreign trade, in addition to the sustained real depreciation of the currency, there were two important trends.⁹ The first was the liberalization of imports. Negative import lists were replaced by positive lists in 1983–84. By 1988 only thirty-three items were subject to any import licensing; quantitative restrictions were thus effectively eliminated. Tariffs and other surcharges on imports changed frequently, but there was a general reduction in these as well; unweighted average tariffs decreased to 11 percent (17 percent for consumer goods) by 1989 (Onis and Webb 1994, table 5–5).

The second important policy tool used in the trade area was the export incentive. In the pre-reform regime, exports were discouraged both by overvalued exchange rates and by protection from imports. In order to encourage exports, the government supplemented real depreciation of the Turkish lira with an array of incentives (Krueger and Aktan 1992; Rodrik 1993). These included provisions for foreign exchange retention, tax rebates (later reduced, and eventually phased out in 1989), export credits (with interest rates much lower than the very high commercial rates), foreign exchange allocation schemes, corporate tax reductions, and subsidies from a Support and Price Stabilization Fund. Exporters whose annual ex-

port volumes were above a minimum level were rewarded with additional tax rebates. These special incentives were instituted to promote large trading companies (Onis 1992), and they were eliminated in 1989. The amount of resource transfer effected by these incentives was substantial. According to Togan, nominal subsidies (net of indirect taxes) averaged about 32 percent of total exports in 1983, and 24 percent in 1984; they declined to 16 percent in 1989 and to 13 percent in 1990. Yeldan (1994) calculated that between 1982 and 1992, export subsidies were substantially higher than total corporate taxes collected by the government for all years except 1986, when they were almost equal. Arslan (1993) calculates that between 1988 and 1991 the fiscal cost of export incentive programs ranged between 2.0 and 2.4 percent of GNP.

Fast growth in exports became one of the most important yardsticks of the success of the adjustment program. Between 1980 and 1990, the value of exports increased from US\$2.9 billion to US\$13.0 billion. The share of manufactured goods in total exports increased from 29 to 72 percent.

The weakest component of the adjustment effort was macroeconomic stability. A major element of stabilization in the early 1980s was a significant retrenchment in the public sector. The public sector borrowing requirements (PSBR) were reduced from almost 9 percent of GNP to 4 percent between 1980 and 1981 (table 1). This drastic reduction was achieved by cutting both the deficit of the central government budget and SEE losses. In the case of the consolidated budget, major reductions were made in personnel expenditures and transfers to SEEs. In the case of the SEEs, the main sources of the decrease were the deregulation of the prices and a relative decrease in wages and salaries (see Celasun 1990 for a review of fiscal policy in this period). A second important component of the decline

9 For details of trade reform see Baysan and Blitzer 1990, 1991; and Krueger and Aktan 1992.

in SEE borrowing requirements was a reduction in subsidies allocated to agriculture. (The role of SEEs in Turkish agricultural policy will be discussed in more detail below.)

The initial reduction was generally maintained until the mid-1980s, with an average PSBR/GNP ratio of 4 percent in 1980–86. The first significant jump occurred in 1987 as a result of the fiscal expansion associated with the election year, and the economy recorded an extraordinarily high growth rate of 9.3 percent. This was followed by

a minicrisis, and a stabilization program was initiated in February 1988. The PSBR ratio then increased on a sustained basis until it hit a record 11.7 percent in 1993, followed in 1994 by a major crisis, a stabilization effort, and a record 6 percent drop in GNP (table 1). Below it will be argued that the deterioration in the public accounts was closely linked to increased redistributive pressures on government finances. Before that, a closer look at the origins of these pressures in the labor markets and agriculture will be useful.

The Limits of Income Redistribution

The stabilization and adjustment effort of the early 1980s entailed major redistributions of income. There were two conspicuous losers—labor and agricultural producers. In both cases, the political environment in the early 1980s was instrumental in affecting the redistribution of income. The more militant of the two largest trade unions, DISK, was dissolved by the military government. While the other, Turk-Is, continued under military rule, it operated under extremely restrictive rules laid down by the military government. The government ended strikes and banned union activity. Collective bargaining was replaced by the deliberations of the High Arbitration Board, which was controlled by the government. Moreover, the new Constitution banned unions from engaging in political activity or supporting or receiving support from political parties. The resulting decline in real wages was one of the basic pillars of the stabilization effort. For the economy as a whole, the downward flexibility of wages facilitated the real depreciation that was required for outward orientation. For the pub-

lic sector, it facilitated the fiscal retrenchment that occurred in the early 1980s.

In the case of agriculture, the suspension of political competition eliminated the main channel of influence that traditionally had served as the vehicle to obtain subsidies from the state. The main channel of influence for agricultural producers, local party organizations, disappeared when the political parties were banned. Moreover, in the early 1980s new parties were formed that did not have the extensive organizations characteristic of the parties active prior to the military takeover. Finally, ANAP did not attempt to build up a rural constituency. The outcome was that there were significant reductions in both the number of commodities subject to support purchases and the real level of support prices offered to farmers. This eliminated one of the most important instruments of income redistribution in the sector.¹⁰

The opening up of the political regime in the mid-to-late 1980s fundamentally changed the environment for macroeconomic policy. Collective

¹⁰ *The extent of the redistribution of income away from workers and farmers in the early 1980s has been documented by many scholars (including Boratav 1990; Celasun 1989; Celasun and Tansel 1993). In the case of labor income, this is captured by both a decreasing share of wages in national income and a significant decline in indexes of real wages and salaries. The share of the agricultural sector as a whole in GNP has declined. The relative decline in agricultural incomes is also captured by reductions in various indexes that reflect terms of trade (for example, between agricultural inputs and outputs, and between agricultural commodities and agroindustry products).*

bargaining was reinstated in 1987 as part of the trend of redemocratization. In the spring of 1989, right after local elections in which ANAP, the governing party, lost, collective bargaining between Turk-Is and various SEEs, involving 600,000 workers, reached a deadlock. Workers were requesting a wage increase of 170 percent to compensate for the real wage losses of the previous decade. After protracted negotiations, strikes, and other protest activities, the government agreed to an average increase of 142 percent (*Milliyet*, May 18, 1989).¹¹

Strikes were not the only reason labor was successful at the bargaining table. A very important additional factor was that public opinion and the press (and even employers) were extremely favorably disposed toward labor's plight (Cizre-Sakallioglu 1991, pp. 67, 68). Labor appealed to the public's sense of fairness, and successfully and credibly argued that they had suffered tremendously from the economic policies of the 1980s. Newspapers were filled with stories of hardships that workers faced to make ends meet. Labor's demands were generally accepted as overdue and legitimate.¹²

The whole scenario was repeated two years later, this time with the miners of the Hardcoal Agency in Zonguldak in the lead role. The Hardcoal Agency has been one of the largest loss makers in the SEE sector. When about 100,000 workers decided to travel on foot from Zonguldak, a northern city on the Black Sea, to Ankara in order to talk to the authorities and press their demands, a public opinion poll conducted by the *Turkish Daily News* found that about 85 percent of the

Table 2
Changes in Real Wages and Salaries
1981 = 100

	(1)	(2)	(3)
1981	100	100	100
1982	96	89	113
1983	88	86	103
1984	83	74	88
1985	78	62	82
1986	76	54	83
1987	86	55	87
1988	81	46	82
1989	107	64	117
1990	124	83	144
1991	186	122	150
1992	181	130	150
1993	194	141	160
1994	n.a.	133	128

n.a. Not available.

Note: (1) index of real gross wages in the private sector; (2) index of real gross wages in the public sector; (3) index of real cost of civil servants' salaries.

Source: SPO: 1994 Annual Program.

respondents supported the strike as well as the march of the miners.

The increase in public sector wages increased the gap between public sector wages and salaries, and led the government to adjust civil servant salaries in the public sector as well. In July 1989, two months after the conclusion of collective bargaining involving SEE workers, civil servants' net salaries were increased by an average of 80 percent for the second half of 1989. The result was that a persistent trend of declining public sector wages and salaries was reversed in 1989, as shown in table 2.¹³

11 OECD's estimate of the wage increase in the public sector is lower (112 percent). See OECD 1991.

12 Young labor leaders' ingenious techniques to appeal to public opinion probably also played a role in generating this sympathy. Rather than resorting to a discourse based in the language of class conflict, which was generally the case in the labor protests of the 1970s, labor appealed to a sense of fairness and paternalism, with an added twist of dark humor. In one province, vast numbers of workers applied collectively to courts for divorce because, as they put it, they were disgraced for not being able to take care of their families. Workers went to work barefoot because, they said, they did not have the means to buy shoes. Growing a beard, boycotting meals, and paying collective medical visits to doctors were other typical acts of protest. The press characterization of these activities as "nonviolent" or as "passive resistance" reflected a sense of empathy in the public, if not one of support.

13 The reader should be cautioned that indexes of real wages and salaries do not reveal that civil servant salaries are, on average, much lower than wages of public sector workers.

Table 3
Staff Positions in the Civil Service

Thousands

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
Number of positions	1,170	1,170	1,176	1,196	1,286	1,317	1,356	1,491	1,507	1,518	1,541	1,600	1,650	1,811	1,812
Percent increase	-	-0.1	0.6	1.6	7.5	2.4	3.0	10.0	1.1	0.7	1.6	3.8	3.1	9.8	0.1

Source: Undersecretariat of Treasury and Foreign Trade *Main Economic Indicators*, March 1994.

The burden of salary increases on the budget was aggravated by significant increases in the number of personnel. Data on actual employment in the civil service are not available, but there are data on the number of staff positions in the public sector, irrespective of whether these positions are

occupied or not. Although not perfect, the data are very revealing, because they underscore the extent of patronage in the public sector. During the early years of economic reform, the number of staff positions increased only marginally, and was kept below 1.20 million until 1983 (table 3).

Table 4
Price Support for Selected Products, 1979-93

		1979	1980	1981	1982	1983	1984
Wheat	Production price, TL/ton	5,020	10,220	18,740	22,950	28,980	46,670
	Reference price, TL/ton	4,452	11,794	19,123	28,038	34,888	59,769
	Price support, TL mn	7,876	-20,565	-5,156	-71,320	-77,604	-180,433
	Percent support ^a	12.8	-13.3	-2.0	-18.1	-16.9	-21.9
Coarse grain ^b	Production price, TL/ton	5,646	8,935	14,365	17,043	22,059	44,009
	Reference price, TL/ton	4,192	9,678	16,209	18,451	27,904	46,636
	Price support, TL mn	8,394	-4,187	-11,243	-8,390	-35,779	-18,607
	Percent support ^a	34.7	-7.7	-11.4	-7.6	-20.9	-5.6
Sugarbeet ^b	Production price, TL/ton	1,420	3,100	4,580	5,860	6,750	8,960
	Reference price, TL/ton	1,063	4,992	5,735	4,920	6,613	7,840
	Price support, TL mn	2,915	-21,373	-12,204	11,374	1,679	11,833
	Percent support ^a	33.6	-37.9	-20.1	19.1	2.1	14.3
Cotton	Production price, TL/ton	66,000	134,000	177,000	218,000	370,000	510,000
	Reference price, TL/ton	53,229	128,563	144,392	179,210	244,368	442,675
	Price support, TL mn	6,079	2,719	15,913	18,968	65,580	39,048
	Percent support ^a	24.0	4.2	22.6	21.6	51.4	15.2

a. (Production Price-Reference Price)/Reference Price.

b. Reference price is calculated by the author from production price, quantity of production, and price support.

Source: OECD 1994b.

Then, during the year of local elections, it increased by an unusually high 7.5 percent, to 1.29 million. The next big jump occurred in 1987, the year of general elections, and the number of positions increased by 10 percent. After marginal increases in 1988–90, the next significant increases were recorded before and after the general elections of 1991.¹⁴ By 1994, the number of staff positions reached 1.8 million, almost 55 percent higher than in 1980.

The wage settlements in the public sector also affected those in the private sector, where the declining trend was also reversed after 1988 (see table 2). There was, however, one important difference in the way the private and public sector industries responded to the change in the relative

price of labor. In the early 1990s, following the real wage shock, many industries in the private sector undertook significant restructuring, shedding labor, updating equipment, and increasing productivity.¹⁵ No such restructuring took place in the public sector, because the political costs of layoffs were perceived as prohibitive.

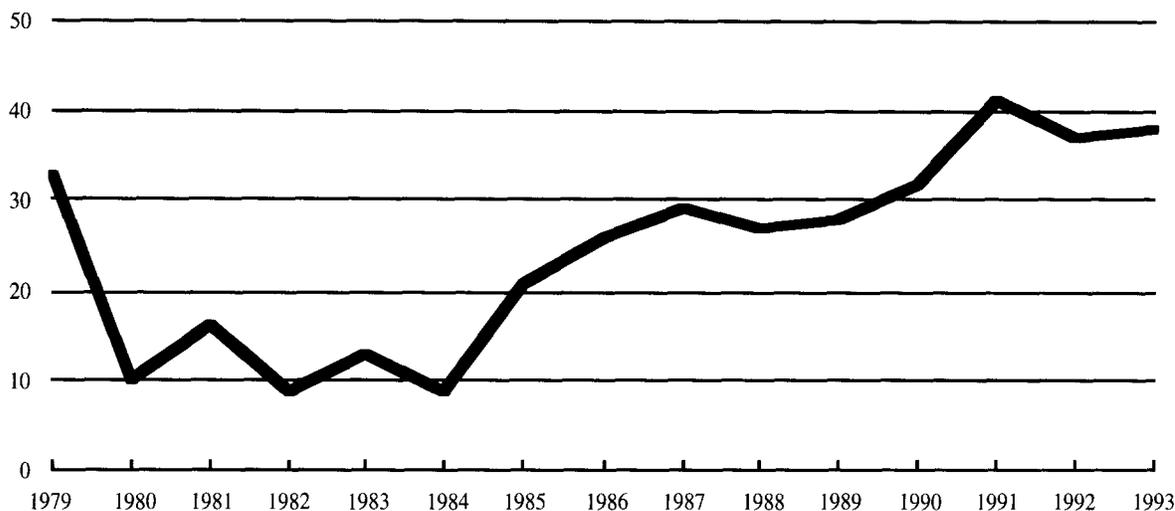
In agriculture, the return of competition to the political process made agricultural subsidies, particularly support prices, prominent instruments in mobilizing votes in the countryside once again. Although initially ANAP was not interested in developing an agricultural constituency, the emergence of DYP, which inherited AP's networks in the countryside, pushed ANAP to participate in the traditional game of using agricultural policy

1985	1986	1987	1988	1989	1990	1991	1992	1993
62,450	79,030	96,760	168,090	327,650	50,370	762,590	1,155,910	1,850,000
68,723	74,564	70,442	102,656	245,748	427,873	44,190	96,355	1,658,605
-86,380	-68,729	402,904	10,986,653	1,086,653	1,250,225	5,399,783	2,997,200	3,248,739
-9.1	6.0	37.4	63.7	33.3	17.6	72.2	19.4	11.5
55,633	64,871	81,439	154,714	282,471	401,206	635,768	1,037,501	1,556,072
53,778	49,232	54,264	151,198	260,536	279,444	397,489	689,006	916,225
13,967	130,528	224,662	30,280	129,635	1,051,784	2,188,352	2,924,655	5,450,372
3.4	31.8	50.1	2.3	8.4	43.6	59.9	50.6	69.8
13,960	17,110	2,830	45,270	83,990	142,190	217,780	359,460	539,190
9,821	14,345	20,552	42,876	90,447	124,891	141,792	217,322	340,394
37,862	28,469	27,007	25,015	-66,160	226,499	1,110,443	2,093,834	298,936
42.1	19.3	1.1	5.6	7.1	13.9	53.6	65.4	58.4
706,000	826,000	1,633,000	1,825,000	3,768,000	4,875,000	6,948,000	1,100,000	16,500,000
667,069	627,047	963,963	1,650,676	2,676,096	41,054,544	6,519,650	8,931,015	13,317,084
20,166	103,058	359,139	113,311	673,705	503,285	240,304	1,253,805	1,970,225
5.8	31.7	69.4	10.6	40.8	18.7	6.6	-87.7	23.9

14 It is likely that the increases in more recent years, especially in 1993, are related to increased deployment of security personnel to the southeast as part of the military campaign against Kurdish nationalists. See Ekinçi 1994, p. 39.

15 Especially in textiles, large wage increases were granted with an implicit understanding between industry and the unions that the latter would not effectively resist layoffs.

Figure 1
Producer Subsidies to Agriculture, 1979–93
 Percent



Source: OECD 1994b.

to generate political support. One set of indicators of government subsidies is given in table 4. The figures in this table are calculated from a recent study of agricultural policies in Turkey by the Organization for Economic Cooperation and Development (OECD 1994b). The variable of interest is "percentage support," which is defined as production price minus a reference price, expressed as a percentage of the reference price for the specified commodities. The production price is the purchase price of the relevant government agency engaged in support purchases. The reference price is often the border price of imports of the same commodity. Hence, percentage support estimates prices paid over and above world prices (a negative percentage support implies that the government support price is lower than the world price). Especially in the case of wheat, sugarbeet, and coarse grain, the data shows a general increase in support at the end of the 1980s and during the 1990s. In the case of wheat and coarse grain, the support is actually negative until the mid-1980s, and increases thereafter.

A more general index of support is provided in figure 1. The index is the producer

subsidy equivalent (PSE) for all the commodities in the sample (which includes all commodities that receive support in Turkey, with the exception of tobacco), and includes not only price support, but also estimates of subsidies provided through credit, fertilizers, seeds, and services (price support is always the dominant subsidy). The index suggests that resources de-

Table 5
Terms of Trade for Agriculture

	GDP deflator	Wholesale price index
1984	100	106
1985	98	102
1986	91	97
1987	87	94
1988	74	79
1989	85	87
1990	103	99
1991	99	145

Note: Column one is the ratio of implicit GDP deflators for agriculture and industry. Column two is the ratio of agriculture and manufacturing industry components of the wholesale price index.

Source: State Institute of Statistics.

voted to agricultural producers were high—one-third of the production value—in 1979. Then, with the suspension of political competition and the fiscal retrenchment of the early 1980s, support declined considerably. It started to increase again in 1985, and reached around 40 percent in 1991–93.

The impact of this shift in policy can be traced through the movements in terms of trade between agriculture and industry. Following Boratav (1990), table 5 displays two estimates of terms of trade between agriculture and industry. Both indexes reflect a continuation of the deterioration of terms of trade against agriculture until 1988 and 1989, and improvements in 1990–91.

It is beyond the scope of this chapter to discuss agricultural policy in detail. It should be pointed out, however, that budgetary resources are spent not only as support to farmers, but also to maintain additional stakeholders in the government agencies taking part in the support mechanism. The case of Agricultural Sales Cooperative Unions (ASCUs) provides a good example. ASCUs are authorized to set prices for members' commodities and implement support purchases on behalf of the state. In many cases they also have established capacity to undertake the initial processing of the produce, be-

fore it is sold to traders or exported. Even though this makes economic sense, some ASCUs have integrated forward to establish manufacturing plants that are uncompetitive and chronic loss-makers. The activities of the ASCUs are financed through credit from the state-owned Agricultural Bank. Accounting is very poor, and the bank cannot monitor how its advances are used—it cannot differentiate advances used for the implementation of agricultural policy from those used to finance the losses of the manufacturing plants. At the end of the financing season, only a fraction of the loan is repaid, and the remainder generates a claim for the bank on the Treasury in the form of "duty loss." The Treasury ultimately finances not only subsidies allocated to farmers through support prices, but also the losses of the manufacturing plants. This form of rent dissipation increases the cost of agricultural policy substantially.

What about the fiscal impact of agricultural subsidies? An important part of support policies is implemented by specialized SEEs, and thus a significant part of the fiscal impact ultimately shows up in the borrowing requirements of the SEEs or in the transfers from the budget to the SEEs. A review of fiscal accounts is presented next.

Impact of Distributional Pressures on Public Finances

A brief perusal of the main components of public accounts in Turkey will help identify some of the dynamics behind the galloping deficits and locate the effects of increases in wages and agricultural subsidies. Table 6 records the distribution of total PSBR among the public accounts. The largest items are the central government and the SEEs. The borrowing requirements of the rest of the public sector, most notably the extra-budgetary funds (EBFs), local administrations, and Social Security, also increased, from a surplus of 1

percent of GNP in 1984 to a deficit of about 2 percent.

The next step is to examine the important accounts in more detail. Starting with the consolidated budget (see table 7), one can make several observations. The first is the big jump in personnel expenditures in 1989 and the sustained increase thereafter, which more than doubled these expenditures as a percentage of GNP between 1988 and 1993. Interest payments became the second major component of budgetary deficits, increasing, in a more or less sustained way, from

Table 6
Public Sector Borrowing Requirements (PSBR), 1984–94
 Percent of GNP

	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
Total public sector	5.3	3.5	3.6	6.1	4.8	5.4	7.6	10.3	10.6	11.7	8.2
Nonfinancial public sector	5.6	3.5	3.6	6.2	4.8	5.4	7.8	10.5	11.0	12.0	8.1
Consolidated budget	4.3	2.2	2.7	3.5	3.1	3.3	3.0	5.3	4.3	6.7	3.8
Nonfinancial SEEs	2.2	2.4	2.6	3.4	2.1	2.0	4.0	3.3	3.8	3.5	2.7
Extra-budgetary funds	-0.5	-0.6	-1.6	-0.6	-0.5	0.3	0.8	1.3	2.0	0.5	0.7
Local administrations	-0.0	-0.1	0.3	0.5	0.4	0.2	0.2	0.4	0.8	0.8	0.4
Financial SEEs	-0.4	0.0	-0.0	-0.2	0.0	-0.0	-0.2	-0.2	-0.5	-0.3	0.2
Revolving funds & Social Security	-0.3	-0.4	-0.3	-0.6	-0.3	-0.4	-0.3	0.2	0.2	0.6	0.5

Source: State Planning Organization.

Table 7
Consolidated Budget Revenues and Expenditure Components, 1985–94
 Percent of GNP

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
Revenues	12.8	13.7	13.9	13.6	13.6	14.2	15.3	15.8	17.6	19.3
Expenditures	15.0	16.4	17.4	16.6	16.9	17.3	20.5	20.1	24.3	23.0
Personnel	3.6	3.	4.0	3.9	5.4	6.7	7.8	8.5	8.5	7.0
Other current	2.3	2.3	2.1	1.9	1.8	1.8	1.8	1.8	1.8	1.9
Investment	3.1	3.9	3.5	2.8	2.5	2.5	2.7	2.7	2.7	2.0
Interest payments	1.9	2.6	3.0	3.9	3.6	3.5	3.8	3.7	5.8	7.6
Foreign borrowing	0.7	1.3	1.3	1.4	1.4	1.1	1.1	0.9	1.2	1.7
Domestic borrowing	0.5	1.3	1.7	2.5	2.2	2.4	2.7	2.8	4.6	6.0
Transfers to SEEs	3.7	0.3	0.6	0.8	0.5	0.3	1.9	0.7	1.3	0.5
Other transfers	3.7	3.9	4.2	3.4	3.0	2.5	2.6	2.7	4.3	4.0
Budget balance	-2.2	-2.7	-3.5	-3.0	-3.3	-3.0	-5.3	-4.3	-6.7	-3.7

Source: Treasury Monthly Indicators.

Table 8
Financing of the Consolidated Budget Deficits, 1985–94
 Percent of GNP

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
Budget balance	-2.2	-2.7	-3.5	-3.0	-3.3	-3.0	-5.3	-4.3	-6.7	-3.7
Deferred & advance payments	-0.3	-0.3	0.0	-0.0	-0.3	-0.1	0.0	-1.1	0.4	0.0
Cash balance	-2.5	-3.1	-3.4	-3.1	-3.5	-3.1	-5.3	-5.4	-6.3	-3.7
Financing	2.5	3.1	3.4	3.1	3.5	3.1	5.3	5.4	6.3	3.7
Foreign borrowing	-0.6	-0.0	-0.4	0.1	-0.2	0.0	0.3	0.4	1.1	-1.8
Domestic borrowing	1.4	0.9	1.2	1.9	2.6	2.0	0.4	1.4	1.5	-1.8
Short-term borrowing	1.4	1.8	1.7	0.8	0.6	0.6	3.7	3.7	3.8	7.6
Central Bank	0.7	0.5	0.5	0.5	0.2	0.0	1.7	1.6	2.7	1.3
Other	0.4	0.4	0.9	0.2	0.5	0.5	0.9	-0.1	-0.0	-0.3

Source: Treasury Monthly Indicators.

less than 2 percent of GNP in 1985 to close to 6 percent in 1993. Direct budgetary transfers to the SEEs were not very high, which is quite misleading, as will be seen below.

The financing of the consolidated budget deficits is summarized in table 8. Although at the end of 1970s recourse to Central Bank advances (at a low interest rate of 1 percent) was the main source of financing, during the 1980s the deficit was increasingly financed by selling government securities, most of which were held in the banking sector (see table 8). The increasing share of short-term borrowing in the 1990s is indicative of the increasing credibility problems of fiscal policy, as well as attempts by the government to reduce the interest cost of borrowing.

The next step is to examine the factors behind SEE borrowing requirements. Most of the borrowing requirements of SEEs are concentrated in seven enterprises. In 1990, these accounted for about 90 percent of total SEE borrowing requirements. By 1993, with the rapid rise of total SEE borrowing requirements, this share had decreased steadily to 65 percent. They collectively obtain about 80 percent of budgetary transfers, and account for about 50 percent of personnel expenditures of all SEEs.

The reasons for financial deficits vary across SEEs. Three of the seven are the government's instruments in agricultural policy and carry out support purchases of sugarbeet, wheat, and tobacco.¹⁶ Their financial deficits are thus closely related to their purchase of commodities at subsidized prices to sell at market prices. This category of the SEE borrowing requirement simply reflects agricultural subsidies. These three companies accounted for about 42–44 percent of total SEE borrowing requirements in the 1990s.

Among the remaining four in this group, two are industrial companies (a hard coal producer and an iron and steel producer). Their borrowing re-

Table 9
SEEs—Personnel and Interest Expenditures
Percent

	Personnel expenditures/ revenues	Interest payments/ revenues
1986	10	4
1987	11	6
1988	11	5
1989	15	4
1990	19	5
1991	34	10
1992	33	10
1993	34	11

Source: Calculated from Treasury Monthly Indicators, Dec. 93, Table V.4.

quirements originate from operational losses brought about by inappropriate technology, overemployment, and lack of investment to raise efficiency. One is a railroad company, and the last one is the electricity company, which is burdened by a heavy investment program. In these nonagricultural SEEs, the main reasons for losses are rapid increases in wages and interest payments. Table 9 demonstrates that for the SEE sector as a whole, the ratio of wage and salary expenditures to revenues increased from 15 percent in 1989 to 34 percent in 1993, and that of interest payments to revenues almost tripled, from 4 to 11 percent, in the same period.

It is well known that SEEs suffer from overemployment. Nevertheless, it is generally believed that employment in SEEs has not increased appreciably in the last decade. Depending on how one treats enterprises that are slated for privatization, the number of employees ranged between 550,000 and 650,000 in the mid-1980s (SPO 1993). The data also suggest some decline in the 1990s, possibly resulting from a combination of a ban on hiring and attrition. Based on a more consistent sample, Boratav and colleagues

16 These are the Sugar Company, Soil Products, and the State Monopoly.

(1993) reached a similar conclusion. Hence, the increase in the wage bill mentioned above is mainly the product of higher wages rather than increased employment.

Another source of revenue losses was created by the government's policy of keeping the prices of producer SEE products low before elections. Although Decree Law 233 of 1984 stipulated that SEEs are to operate as commercial entities subject to the commercial code, and they are authorized to set their prices freely, in practice price

increases are subject to ministerial review. The 1987 election is a case in point. The average wholesale price index of public sector production and agriculture was lagging behind its private counterpart by almost 20 percentage points over the first eleven months of 1987. After the November elections, prices jumped by 21 percent, but could not recover the lost ground; private sector prices increased by 7.2 percent after the elections (World Bank 1993). Expecting price increases after elections has become customary

Table 10
Public Revenues, 1984–94
Percent of GNP

Category	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
Total public	18.0	19.0	22.0	22.2	21.9	20.9	20.0	18.0	18.1	18.7	19.5
Direct taxes	5.7	4.6	5.6	5.8	5.5	6.4	6.5	7.0	7.3	7.1	7.9
Indirect taxes	5.2	7.1	8.2	8.8	8.7	8.3	8.9	9.3	10.0	10.5	10.5
Non-tax normal income	2.5	2.2	2.9	1.8	1.6	1.4	1.3	1.3	1.3	1.4	1.3
Factor income	4.6	5.1	5.4	5.6	6.3	5.0	3.1	0.6	-0.0	0.6	0.8
Social funds	0.0	-0.1	-0.2	0.3	-0.3	-0.1	0.0	-0.3	-0.4	-0.9	-1.1
Consolidated budget	10.3	10.5	11.4	12.0	10.9	11.0	11.3	12.3	12.7	13.1	14.9
Direct taxes	5.9	4.9	5.9	5.9	5.4	5.8	5.9	6.4	6.4	6.3	7.1
Indirect taxes	4.4	5.6	5.5	6.1	5.5	5.2	5.5	5.9	6.4	6.8	7.8
EBFs	0.3	0.8	2.1	2.0	2.4	2.5	2.8	2.5	3.0	2.9	1.8
Direct taxes	0.0	0.0	0.2	0.2	0.0	0.1	0.2	0.0	0.3	0.2	0.2
Indirect taxes	0.3	0.8	2.0	1.9	2.3	2.3	2.6	2.5	2.7	2.6	1.6

Source: State Planning Organization.

Table 11
Tax Burden of Wage Earners
Percent

	Wage earners			Non-wage-earners		
	Share in national income (1)	Share in income tax (2)	Tax burden (2)(1)	Share in national income (3)	Share in income tax (4)	Tax burden (4)(3)
1973	28.3	63.9	2.3	71.7	36.1	0.5
1987	17.1	38.2	2.2	82.9	61.8	0.7
1988	14.0	49.9	3.6	86.0	50.1	0.6
1989	15.0	54.9	3.7	85.0	45.1	0.5

Source: Oyan and Aydin 1991, p. 49.

in Turkey. This pattern was repeated before the elections in 1991.

A brief mention of the structure of government revenues is also necessary, if only to identify some of its political economy features. The tax base in Turkey is extremely narrow; agriculture is generally not taxed, and tax evasion among business establishments (except perhaps for the largest businesses) is widespread. Except for the introduction of a value added tax in 1985, the tax system has not undergone any significant reform. The share of indirect taxes has increased steadily (see table 10).

The tax system is heavily biased against wage earners. The share of wealth taxes is below one-quarter of 1 percent of GNP. The share of corporate taxes was as low as 2 percent of GNP in 1982, and it declined even further, to 1.6 percent, in 1991 (IMF, *Government Financial Statistics*). Tax brackets are not indexed to inflation, which leaves wage earners prey to bracket creep. The increase in the direct tax/GNP ratio in 1989–92 (table 10) essentially reflects the higher incomes of wage earners. Oyan and Aydin (1991) estimate that in 1989 the share of taxes collected from wage earners was more than three times their share in national income, whereas this ratio was about one-half for non-wage-earners (see table 11; also see discussion in Celasun 1989, 1990).

The corporate income tax, by contrast, was loaded with exemptions and deductions that substantially reduced the tax burden on corporations. Saygilioglu (1990) has estimated that these exemptions and deductions reduced the effective corporate income tax rate to 21 percent in 1988 from a nominal rate of 46 percent.

The Crisis and the Stabilization Program of 1994: Does History Repeat Itself?

The deterioration of fiscal accounts accelerated after the elections of 1991. The government was in a bind (see Ozatay 1995 for an account of the events that triggered the crisis of

1994). Financing the deficits by borrowing from the market was extremely costly; by 1993, interest payments had already become a major burden on the budget. Moreover, the government saw reducing interest rates as an important short-term policy objective (Ozatay 1995, p. 10). It tried to overcome the dilemma both by increasing the Treasury's recourse to advances from the Central Bank and by attempting to administer the interest rate. A rapid increase in Central Bank advances occurred in the last quarter of 1993 and the first quarter of 1994. At the same time, its attempts to administer the interest rates in the Treasury auctions caused a rapid contraction in the bond market. A flight from the Turkish lira occurred. Foreign reserves of the Central Bank decreased from US\$7.2 billion in November 1993 to US\$3 billion in April 1995. Between January and April 1995 the currency depreciated by 150 percent.

On April 5, 1994, the government announced a new stabilization program (see OECD 1994a for a review of the program). The main elements of the package were a severe cut in expenditures, a once-and-for-all application of a net asset tax (and some other one-time taxes, such as a 10 percent surcharge on personal and corporate incomes), and rapid price increases for SEE products. There was a deep contraction of output in 1994, but the envisaged fiscal contraction did take place. There were strict cuts in current expenditures, both in personnel and other areas.

As can be seen in the final row of table 2, the brunt of the fiscal adjustment was again born by civil servants and public sector workers. In that sense, the fiscal contraction of 1995 is reminiscent of the one that took place in 1980–82. Its sustainability will be contingent on additional measures that address the structural problems that make public finances captive to distributive pressures. A number of such measures were included as government's intent. Not much was done in 1995, however, except for the passage of a privatization law. That in itself was very important, but the passage of the law is still only

a first step in an arduous process that is both politically and administratively complex. Moreover, the impact of privatization on the major loss-making SEEs is unlikely to be large; it is probable that it will not be possible to privatize

some of the enterprises, such as the coal mines. In the case of agricultural SEEs, financial problems originate from the structure of agricultural support policy; the implications of privatization for these SEEs are not yet clear.

Governance in the Economic Reform Period

An important dimension of the government's approach to governance was centralization of key decisionmaking processes and increasing the discretionary authority of the executive, especially the office of the prime minister.¹⁷ In a sense, centralization was seen as the solution to the governance problems that afflicted the country before the military takeover. On the one hand, it was seen as a means to circumvent "pathological bureaucratization"; on the other, it was viewed as a solution to stalemate in the Parliament.

Centralization was aimed at reducing the power of the traditional bureaucracy. The civil service was seen either as too slow, not dynamic, and unresponsive to people's demands, or as ideologically too committed to state intervention, not market-oriented, and too caught up in its procedural maze. Ozal attempted to restructure or bypass the traditional bureaucracy. For example, the Ministry of Finance was left with the responsibility of revenue collection. Other fiscal tasks were transferred to an Undersecretariat for Treasury and Foreign Trade, which was linked to the prime minister's office, and someone close to Ozal was put in charge (Heper 1990, p. 612). Autonomous groups were created in some units to carry out projects that were seen as important. In other cases (for example, in the state-owned banks, the Central Bank, and some SEEs), people outside the civil service were appointed to positions of authority.

These appointees were usually young, foreign-educated, and, most important, people that Ozal could trust. More generally, Ozal worked with a small set of advisers, and the influence of the rest of the cabinet on the policymaking process was reduced. A governmental decree passed in 1984 supported this arrangement by strengthening the prime minister in relation to individual ministers.

A closely related aspect of centralization was the attempt to bypass the Parliament. This effort was facilitated by the restructuring of the political system that was brought about by the Constitution of 1982, written under the military regime. In order to prevent the stalemates that characterized the political process in the late 1970s, framers of the Constitution wanted to empower the executive over the legislature.¹⁸ The Constitution enables the government to request authorization to issue decrees that have the force of law. Once published in the *Official Gazette*, the decrees must be referred to the GNA for approval. What this meant was that the executive could avoid the legislative process and the accompanying debate, and limit the legislators' choice to whether or not to approve a policy already being implemented. In 1984 a law was passed that enabled the Council of Ministers to pass such decrees with the force of law (Heper 1989, p. 465).

Another instrument that the government used to circumvent legislative oversight was the establishment of extra-budgetary funds (EBFs). Al-

¹⁷ Various aspects of the process of centralization are discussed in Heper 1989, 1990; Onis 1992; and Onis and Webb 1994.

¹⁸ The 1982 Constitution introduced some fundamental changes into the political process. For reviews see the papers in Ozbudun and others 1988; Ozbudun 1994; and Turan 1994. The discussion of decrees in the text draws on Kalaycioglu 1988.

though EBFs existed in Turkey prior to the 1980s, their use in the public sphere to mobilize and allocate resources has greatly expanded during the economic reform period (see Arslan and Akkaya 1993; Oyan and Aydin 1991). The stated reason for the establishment of the funds was the need for flexibility in raising new and temporary revenues and the advantage of the ability to effect expenditures without having to go through the arduous procedures of budgetary approval and control. The EBFs accorded the ANAP governments—especially the prime minister—discretionary authority to allocate fiscal resources without the prior approval of the Parliament. As of 1992, out of a total of 104 funds, only three were audited by the High Court of Accounts (Sayistay), which audits public accounts as an agent of the Parliament. The rest of the funds were audited by a High Board of Supervision, which is affiliated with the Prime Ministry.¹⁹

The tendency to centralize decisionmaking authority and to bypass the traditional bureaucratic and political processes was coupled with a preference to appeal directly to the public. Although in the early 1980s the majority of the established media elite was opposed to economic reform, Ozal made effective use of the media, especially state-controlled television, to explain to the public his objectives in pursuing the reform program. He would present himself as a reformer; his discourse

emphasized individual entrepreneurship and initiative, “free market economy,” international competitiveness, economic development, and the primacy of the individual in relation to the state. He argued that the state should not and could not act as a paternal state. In recessionary periods, he would respond to the private sector’s complaints and requests for assistance by inviting them to “sell their villas” to finance their companies. These themes were presented as essential components of a development strategy for Turkey’s leap into a new epoch (*cag atlamak*). In a regular television program he would talk about how state intervention in the past had violated the “laws of the market” and why the government’s reform program was “the only alternative.” Although even at that time it was possible to identify fundamental inconsistencies between his words and the deeds of the ANAP governments,²⁰ he was successful, at least until the second half of the 1980s, in presenting himself as a leader with a new vision for the future of the country. The term “vision” became an important theme in public discourse.²¹

Ozal presented new parameters for the discourse on economic policy. At the same time, there was a concerted effort by the government and business to accelerate Turkey’s integration into Europe, and a formal application was filed in 1987 for full membership in the European Community (EC).²² It is difficult to assess the relative impacts

19 By 1992 the total expenditures of the funds reached about one-third of the expenditures of the consolidated budget. The funds are primarily financed by earmarked levies and income generated by their investments. Their objectives vary from providing investment and export incentives, financing public investment (especially in infrastructure), providing subsidized credit, and providing resources for social programs. Two of the funds, the Support and Price Stabilization Fund and the Development Support Fund, took part in the government’s agricultural support policy. Over time, it seems that even the government lost track of the activities of the funds. In 1988, as part of austerity measures, the EBFs were required to transfer up to 30 percent of revenues to the Treasury. In 1993 most EBFs were incorporated into the budget.

20 Many inconsistencies were emphasized in the press. For example, the centralization of the state and the legal framework that restricted trade union activity were inconsistent with his liberal and market-oriented discourse. Columnists would present examples of favorable treatment of businessmen associated with Ozal, contradicting his statements that the state should become less interventionist.

21 It may be pointed out that Ozal’s discourse was not limited to economic issues, although those were dominant in the earlier years. He progressively presented a disposition that was more liberal than was characteristic of the central right and left on issues such as religion, the military, and especially the Kurdish problem. Controversy about the extent of his liberalism continues today among the Turkish intelligentsia.

22 Integration into Europe is valued both because it is seen as a guaranty for the consolidation of democracy in Turkey, and because it would provide access for Turkish exports to the European market.

of Ozal's discourse and policies and the prospect of membership in the EC in the change in the business culture that came about in the 1980s, but that a change occurred is without doubt. At the minimum, it can be said that Ozal provided terms and even a language that popularized the idea of market orientation, and the reforms, and their relatively successful outcomes in the 1980s, provided the material basis for it. In any case, two important changes in the business culture seem to have occurred. First, entrepreneurial activity came to be more appreciated. The moral insecurity associated with profit-seeking, and a general suspicion, especially among the bureaucratic elite (see Bugra 1994), of business in general appear to have been greatly reduced in the 1980s. Market values such as efficiency gained salience. The second change has to do with the boundaries of what business legitimately could expect from the government. Demanding high protection from the state on the grounds of the promotion of national industry or the enhancement of national independence are no longer considered a legitimate business demand by the public, as it was in the 1960s and the 1970s. Exports, and ability to compete internationally, have become indicators of how "good" a businessman one is.²³ This does not mean that some elements of business do not demand protection (or, for example, oppose integration with Europe), or even that they would fail to obtain it. The point is that such demands no longer can count on the automatic support of public opinion. This change in the business culture is likely to be a very important factor that will build irreversibility into at least some of the market-oriented reforms introduced throughout the 1980s, especially in the area of international trade. The salience of the protectionist import-substitution model has terminated.

There was a visible concordance between Ozal's emphasis on entrepreneurship and the ten-

dency to increase discretionary authority to the detriment of—and even to circumvent or disregard—established rules and norms, especially as they related to political and administrative procedures. What differentiated ANAP was its emphasis on getting things done; if that required going around rules, so be it. Initially this was refreshing for a populace that suffered from "bureaucratic pathology" and political stalemate. In both a central government and local governments dominated by ANAP (most notably, in Istanbul), going around rules, or even engaging in alleged irregularities, was condoned by the general public if that was necessary to deliver services. This was seen as form of effective governance; its effectiveness made it legitimate. Moreover, it is clear that centralization enabled the government to push ahead with economic reform on a number of fronts in a relatively short period of time.

Some measures taken to facilitate the citizens' dealings with the bureaucracy also projected an antibureaucratic attitude. Procedures such as obtaining driver's licenses, identity cards, passports, and building permits were simplified. Similarly, it became easier to pay taxes, obtain foreign exchange for travel abroad, get a marriage license, or even apply to a state school (Heper 1989, p. 465). These measures affected the daily life of ordinary citizens and were extremely popular. In a similar vein, but perhaps of more economic significance, in order to expedite the granting of export incentives and reduce red tape, the disbursement of incentives was centralized in the Directorate of Incentives and Implementation (TUD) within the State Planning Organization. Previously, exporters had to deal with each agency that granted incentives separately.

In time, however, this style of governance was carried to extremes, and it became a weakness of the ANAP governments. Rules were changed arbitrarily, and governance started to look

23 *Perhaps one of most illuminating examples occurred when one of the largest holding groups in Turkey attempted to oppose a partial liberalization of automotive imports—their opposition was largely condemned.*

personalized and arbitrary.²⁴ The initial appeal of circumventing oppressive rules gave way to a concern about lawlessness or an absence of respect for the norms. What had been interpreted earlier as entrepreneurial initiative came to be seen as improper behavior, accountable to no one. In extreme cases, newspapers reported large numbers of alleged cases of irregularity in the disposition of contracts or allocation of export incentives. EBFs looked completely out of control, and they were seen as ANAP's instruments of pork barrel, and one with no accountability. More generally, concern arose about the absence of norms and moral values. As one sociologist put it, "liberalism is not an unconstrained [state of] freedom where anything goes. As liberalism develops, the need for ethical values increases" (Gole 1993, p. 16, author's translation). A general decay in codes of conduct, especially surrounding the state and political power and in areas where private citizens interact with the state, became prevalent. This was probably one of the reasons why ANAP started to lose its popularity toward the end of the 1980s.

To summarize, while extensive discretion and centralization of decisionmaking were instrumental in pushing reform and gaining popular support for it in the early 1980s, it created an atmosphere of lawlessness that eventually resulted in a decline in the popularity and political power of ANAP. The same factors had even more serious implications for interparty competition, and in consequence, on the fiscal policy that was conducted by the different governments. This problem is taken up next.

Distributional Conflict and the Problem of Cooperation in Politics

Failure in macroeconomic stabilization was shown in the preceding sections to result from rapid

increases in wages and salaries, as well as agricultural subsidies. In the case of wages and salaries, it is interesting to note that while workers in the public sector could exert pressure in an organized manner through their unions, this was not the case for civil servants. Rather, it seems that an increase in the general public awareness about income losses incurred by civil servants throughout the adjustment period was sufficient to prompt the government to take corrective actions. It seems that in the case of civil servants, it was the government's concern about looking unfair that was important, rather than the effects of direct pressures or confrontation. In the case of agricultural subsidies, increases were closely associated with the return of political competition and the reemergence of the agricultural sector as an important block of votes.

In hindsight, one is not surprised that persistent worsening of income distribution proved unsustainable over time. No amount of "political will" could have resisted what looked like legitimate demands, especially at a time when the economy was growing. The important question is whether the crippling effect that improvements in wages, salaries, and agricultural incomes had on public finances could have been avoided. The answer is probably affirmative, but only if these improvements were undertaken along with other significant structural changes.

In the case of the civil servants, who are still grossly underpaid compared with workers in the private or public sector, this would have required civil service reform, including a significant retrenchment. There is overwhelming consensus in Turkey that there is severe overemployment in the civil service, and that, as in many other countries, at least in terms of financial considerations, a reduction in its size would free resources and allow for more reasonable pay schedules.

²⁴ In a much-quoted example, Ozal is reported to have said that "no harm would be done by violating the constitution once" (Bugra 1994, p. 164).

In the case of nonagricultural SEEs, granting wage increases without major restructuring or privatization was bound to cause further deterioration in their financial positions. Major restructuring would have required de-linking the SEEs completely from the political process and preventing their use as instruments of patronage (through employment policy) or electoral politics (through pricing policy). It would have meant closing down enterprises that are not viable within a program that provides adequate compensation for workers who lose their jobs. In the case of SEEs that are used as instruments of agricultural policy, a major revamping of that policy would have been necessary, both to target the subsidies better to the poor farmers and to increase the efficiency of transfers, thereby reducing the amount of resources that would be necessary to support the targeted social group.²⁵

A final and important possible measure was to improve the system of taxation. A fundamental tax reform could have improved both equity and income distribution, decelerated the deterioration of the incomes of wage and salary earners in the early years of reform, and increased the fiscal resources of the state, enhancing its capacity to meet distributional challenges without crippling public finances. There was certainly ample room to increase tax revenues.

The difficulty was not that there were fundamental disagreements on what needed to be done, especially among the parties on the center-right. They did not have any deep ideological differences on the model of development—both conformed to market orientation. Moreover, it did not take much to see that this race to disburse the state's resources would soon create an unsustainable situation. That this race could not be stopped identifies a major instance of the failure of governance capacity.

The fiscal problem, or the way in which state resources are used for political competition, can

be usefully conceptualized as a problem of cooperation. When all contenders for political power behave in a predatory manner, and use, or promise to use, state resources to enhance their chances of public office, the outcome is ultimately severe fiscal deterioration of the kind Turkey experienced in the late 1980s and the 1990s. There is a cooperative outcome as well, where the contenders are able to commit themselves to refrain from behaving in a predatory manner, or refrain from the excesses of fiscal expansion. This way may avoid macroeconomic instability and crises, which hurt all contenders. Without commitment mechanisms, however, the cooperative outcome is unlikely to prevail, because if one party refrains from behaving predatorily, the other has incentives to predate. The governance problem in Turkey can be thought of as the absence of mechanisms that would support the cooperative outcomes and prevent predatory behavior.

As discussed in the second section of this chapter, The Turkish political system lacked norms and mechanisms that could support compromise and cooperation among political actors. In the fiscal area, the very availability of vast discretionary resources probably encouraged noncooperative outcomes. Perhaps more important, however, the use of fiscal resources has been deeply ingrained in the political culture, and it was very much the mechanism through which political participation and democracy have developed in Turkey. Predictably, there were no legal or procedural rules, such as limits on the accumulation of public debt, that could have restrained fiscal expansion. There were some limits on the extent to which the Central Bank could depend on Central Bank financing, but these were flexible; they actually became irrelevant because the fiscal expansion was primarily financed by government debt.

If absence of such norms was the “structural” governance problem, one can perhaps go a step

25 Possible approaches to reform agricultural policy in Turkey are discussed in Ziraat Muhendisleri Odasi 1993 and OECD 1994b.

further and identify a leadership problem as well.²⁶ Put differently, if norms to constrain predatory behavior are absent in the Turkish political culture, could the political leaders of the last fifteen years have taken steps to support more cooperative behavior? Perhaps, but clearly this is not what happened.

ANAP's centralized and discretionary approach to governance not only eventually undermined its own popularity with the public, but it also reduced its capacity to install interparty cooperation. During its rule, and with the prospect of intensifying political competition, ANAP was faced with a choice. Resolving the cooperation problem would have required soliciting basic agreements about the fiscal rules of the political game and/or implementing mechanisms to tie both its hands and those of its competitors. Given Ozal's rhetoric for reducing the role of the state, one would have expected steps in these directions. Interestingly, implementing the structural reforms mentioned above would have created mechanisms of commitment by fundamentally altering—and in some cases eliminating—the instruments that allow fiscal resources to be used for political competition. Instead of creating such mechanisms of commitment and cooperation, the ANAP governments increased their discretion over such resources and undermined any potential for cooperation.²⁷

As for the coalition that followed the rule of ANAP, in the noncooperative mode that characterized the elections environment, they came to power with a long list of liabilities.²⁸ In an editorial entitled "Great Expectations in Ankara," one

journalist described the days following the elections in the following way (Ulagay 1994, p. 58, author's translation):

People who have been far away from political power for ten plus years, now are flowing to Ankara expecting a lot from their parties that are partners in political power. . . . Along with their congratulations, they are bringing their demands. . . . A job for an acquaintance, support for an unfinished project, resources for such and such local government, demand for appointments in order to save such and such place from the influence of the sympathizers of the former government. Endless demands. . . .

Demirel himself, returning to power after eleven years, "spent about three months receiving delegates from his party's organizations all over Turkey, giving speeches, listening to their demands, and making promises" (Gunes-Ayata 1994, p. 58).

One observes here the extreme sensitivity of the party organizations and leadership to constituency demands that was endemic to the polity before the military takeover. The collective action or public goods problem that characterized this sensitivity was discussed earlier in this chapter. The interesting aspect of the Turkish experience lies in the acceleration of fiscal deterioration *after* the 1991 elections. This demonstrates that the "expectations" and "promises" referred to in the quotes above are not empty plays to win elections; there are mechanisms in the political process that make these promises enforceable.

26 Here I follow Frischtak (1995) in differentiating between aspects of governance that can be assessed by governing institutions, and those "intangible" and "less predictable" elements such as leadership.

27 There were a number of additional incidents that possibly increased the dose of confrontation between the ANAP government and the opposition. Among these were ANAP's manipulation of electoral laws to increase its chances of success (which was interpreted as unilateral disregard for the rules of the game) and ANAP's opposition to the lifting of the ban on former political leaders (Ozbudun 1994, p. 48).

28 In some incidents, the electoral campaign resembled a bidding war in an auction. One contestant was quoted as addressing tobacco growers: "whatever ANAP is paying for tobacco, we will pay five thousand liras more" (the Turkish daily, *Hürriyet*, June 2, 1994).

Concluding Remarks

There was an important deficiency in the governance capacity of the state that manifested itself during the political crisis of the late 1970s. That deficiency was related to the inability of the political process to encourage the main political competitors to cooperate, especially during periods of tension, to attend to basic issues of public policy. Political scientists have identified this deficiency as the absence or inadequacy of political institutions that encourage successful bargaining and compromise.

The suspension of political competition by the military takeover and the restricted competition that characterized the earlier periods of the ANAP governments reduced the importance of this aspect of capacity in the making of public policy. ANAP adopted a style of governance that was centralized and emphasized results rather than procedures. It sought support and legitimacy by appealing directly to the public, emphasizing results, while it bypassed the traditional channels of debate, negotiation, and, whenever possible, implementation of public policy. This enabled the ANAP governments to implement a wide range of economic reforms without much challenge.

One must also emphasize here the leadership of Ozal in articulating a new set of social objectives and values that emphasized market orientation, entrepreneurship, and internationalization. His contribution was not so much in building the consensus that eventually emerged, but rather in providing the symbols, the themes, and the language that helped people to construct a generally shared sense of the future. In hindsight, contradictions in words and deeds, and even among the words themselves, turned out to be of secondary importance in the consolidation of this new "vision."

It seems that there were two things missing in Ozal's—and, for that matter, ANAP's—discourse and practice. First, it did not project a sense

of social compassion, a recognition that there were groups who did not participate in sharing the benefits of the new regime and a willingness to do something about it. The importance of this in decreasing the popularity of the ANAP manifested itself most clearly when public opinion warmly supported the quest of workers for higher wages in 1989. Second, ANAP's centralized approach to governance eventually became a weakness in more than one respect. First, it underestimated that legitimacy ultimately required some accountability, which was lacking. Second, as a matter of pure political strategy and tactics, it underestimated the eventual challenge of political competition ANAP would have to face. Third, centralized decision-making, restricting delegation to a small circle of technicians, must have ultimately overwhelmed the ANAP government and reduced its ability to control and monitor, as exemplified by allegations of irregularity and corruption. All of these added to the decline in the political support ANAP could muster from the population.

At a more general level, when political competition resumed, ANAP's style must have aggravated the governance problem identified above. Resumption of political competition challenged the capacity of the state and the political process to encourage cooperation where cooperation is the desirable—but not the likely—outcome. Regulating political competition so that it generates acceptable and sustainable policy outcomes, preventing it from being disruptive, and encouraging political actors to reach agreements requires commitment mechanisms and institutions that reduce discretion (see Shepsle 1992 and Moe 1990 on the problem of commitment in politics). This is particularly true in the area of fiscal policy, and especially in this area, the ANAP governments increased the discretionary power of the state, rather than reducing it. Not only did the ANAP governments not attempt to undertake structural

reforms that would have reduced such discretionary capacity, but they also used the traditional instruments of patronage, and actually created more instruments that could be used for that purpose. There may be two explanations. One could be that this was ANAP's mistake, or short-sightedness; the second could be that ANAP's declared intention to reduce the size of the state was not sincere.²⁹ It is difficult to judge which explanation is correct. The point is that during the ANAP governments, not much was done to repair this governance deficiency.

There is an important lesson of macroeconomic policy to be gained from the Turkish experience: in environments where norms and mechanisms to resolve cooperation problems are weak,³⁰ stabilization programs that affect fiscal retrenchment by suppressing distributional demands are likely to be successful in the short run. Once the problem is resolved and macroeconomic

stability is established, however, at least as long as the political system is competitive, distributive demands, and with them the public good nature brought about by macroeconomic stability re-emerge, leading to macroeconomic disequilibria. A more sustained solution to the problem of macroeconomic instability may require "structural" reforms that address the mechanisms for the management of distributional conflicts in the society. In the case of Turkey, this would entail major reforms of SEEs, agricultural support policy, and the civil service.

Turkey currently is in an interesting situation. The last decade and a half of reform has created a vibrant private sector, and a state that is lagging seriously behind. Having reformed the aspects of the economy that relate to the economic activities of the private sector, it seems that the majority of the remaining tasks have to do with reforming the public sector.

29 Waterbury (1992) argues that the purpose of ANAP's involvement in patronage and clientelism was to secure enough votes for reelection. I do not challenge the presumption that this was an important motivation, but the argument is incomplete. A more complete argument would have to show that patronage was the best strategy for reelection. Given that ANAP's competitors had stronger party organizations and better links with rural local constituencies, it is unclear that this was the best strategy.

30 One should add that the emergence of major fiscal crises may in many cases reflect governance failures.

Appendix

Chronology of Turkish Politics in the 1980s

- September 12, 1980** The military coup.
- November 1982** National referendum accepting the Constitution and Evren's presidency for the next seven years.
- Spring 1983** New electoral law on political parties; 15 new parties formed. Demirel, Ecevit, and another 700 politicians were banned from politics.
- November 1983** General elections. ANAP, under the leadership of Ozal, wins majority. Ozal becomes prime minister.
- March 1984** Local elections won by ANAP.
- September 6, 1987** Referendum with which Demirel, Ecevit, and 100 other politicians were returned the right to political activity with a small majority of 100,000.
- November 29, 1987** Second general elections. ANAP gets 63 percent of seats with 36.2 percent of the votes. Ozal remains as prime minister.
- March 26, 1989** Municipal elections: ANAP, 22 percent; SDP, 28 percent; DYP, 26 percent of vote; big loss for ANAP.
- April–May 1989** Labor unrest. May Day rallies for the first time since the coup.
- November 1989** Ozal becomes the president through parliamentary vote.
- January 3, 1991** One-day general strike organized by Turk-Is, which was spearheaded by 50,000 miners in Zonguldak.
- October 20, 1991** General elections. DYP won the elections and ANAP came second. Coalition formed between DYP and SHP.
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