Limits to Alternative Forms of Capitalization: The Case of Anatolian Holding Companies

GÜL BERNA ÖZCAN
University of London, Egham, UK

and

MURAT ÇOKGEZEN *
Marmara University, Istanbul, Turkey

Summary. — Since the late 1960s, alternative forms of capitalization have emerged in the absence of an effective capital markets regime in Turkey. We can see these alternative forms in the failed attempts to create Anatolian holding companies through the direct investment of small savings. This article shows how Anatolian holding companies became victims of poor institutional and regulatory regimes, and how the lack of institutions to promote impersonal trust in the economy in turn permitted widespread abuses. We identify populist politics, lax oversight, and social norms that incorporated gambling as three interlinked reasons which hindered the genesis and development of viable capital market reform and regulatory institutions in Turkey.

Key words — capital formation, financial markets, state regulation, Anatolian holding companies, Islamic finance, Turkey

1. INTRODUCTION

In the 1970–90s, large multiownership companies, commonly referred to as Anatolian holding companies,1 were formed through small family investments. These holding companies constituted an idiosyncratic model of capital formation. They were both a response to the lack of industrial capital and a byproduct of the politically charged strategy to initiate development and industrialization in the country. We argue that where the rules of advanced capital formation and managerial enterprise (Chandler, 1992) fail to apply, alternative structures can emerge. In Turkey, this alternative model occurred through multiownership companies whereby thousands of small investors put their savings in holding companies that promised good returns while assisting small and medium-sized firms. Our findings indicate however, that Anatolian holding companies became victims of the absence of institutional and regulatory regimes and the lack of institutions to promote impersonal trust in the economy that in turn permitted widespread abuses.

Our work highlights the importance of institutional and regulatory regimes for creating viable capital markets in order to achieve economic growth. The failure of Anatolian holding
companies along with the persistent capital market failures in Turkey lead us to ask two fundamental questions: why did no institutions and regulatory regimes evolve along with the changing needs of the economy? and why were existing controls so often subject to circumvention and abuse? The answers lie in the dynamic interaction between the politics of institution building and behavioral and social norms. We identify three factors that undermined market trust and institution building leading to chronic failures and abuses: policy formation was trapped in populist–clientalist cycles with a slippery political center; lax oversight practices were encouraged by the single-leader tutelage in party politics; and the social norms that allowed investors to accept flimsy assurances and fuzzy legality as part of their gambling habit.

The limited investigation into Anatolian holding companies so far has prevented policy makers from understanding opportunities and challenges offered by alternative capital formations. Despite the deficiencies and the business failures of the past, we believe that the continuing attractiveness of multiownership companies as a form of alternative capital formation and utilization of small family investments in local projects deserves serious attention. We also think that this model is likely to be tried again in Turkey and perhaps elsewhere. Correcting the underlying flaws is crucial to prevent hundreds of corporate collapses and massive loss of small shareholders’ investments.

The case of Anatolian holding companies also has certain similarities with the new corporate landscape created through privatization schemes in Russia and Eastern Europe where privatized company assets have been transferred through often nontransparent and illegal means. Our findings support studies on market reform and institution building in former Communist regimes where weak regulatory controls, widespread mistrust, and the abuses still prevail in these markets (Blasi et al., 1997; Kogut & Spicer, 2002).

Our study highlights a fundamental issue in economic development and regulatory reform for many developing and post-communist economies, that is the need to understand better the links between socio-political forces and behavioral norms embedded in economic life. In order to allow imaginative solutions to emerge in the wake of an endemic lack of capital for industrialization, developing economies should not look for miracles. The fundamental question for both scholars and policy makers is to find the ways to secure and nurture regulatory regimes in order to serve the long-term interests of wider societal elements in economic development rather than the speculative short-term gains of narrow groups and/or managers. The findings of this paper hold implications for studies on firm finance for small and medium enterprises [SMEs] (Becchetti & Trovato, 2002; Winker, 1999), Islamic finance and economics (Kuran, 1995, 1996, 2003; Warde, 2000) and in general on the importance of the politics of institution building and impersonal trust for economic development.²

The article is divided into six sections. Section 2 considers the viability of capital markets for countries such as Turkey through a brief critique of theoretical literature. Section 3 presents an analysis of Turkey’s experiments with capital markets. This is followed by two case studies on the formation of Anatolian holding companies. In Section 5, we illustrate the reasons for poor managerial and regulatory discipline. In conclusion we recommend the key policy changes needed in the light of our findings.

2. CREATING AND INSTITUTING CAPITAL MARKETS

Capital formation is essential for industrial and economic growth. Conventional models of capital formation stem from the experiences of advanced countries and fall into two broad categories. The first one is the bank-centered corporatist model, which is credited with the success of German and Japanese post-war industrial restructuring. They worked under conditions of enforced political stability and the focused determination of a reforming elite. In this model, ownership and control are closely tied within a framework of institutional guarantees and obligations (Miyajima, 1995). The second is the Anglo-Saxon open market model of capital formation through stock markets. In the bank centered system, the close links between the banking system and the market allow companies to finance themselves through bank loans. In this system firms raise capital by issuing new shares and the ownership of a firm is diffused. Accordingly, shareholder rights are protected and the ownership and control of firms are separated. The bank-centered regime is supported by a web of institutions in mutually binding relationships with little respect for
shareholder value (Berglöf, 1990; Charkham, 1994; La Porta, Lopez-de Silanes, & Shleifer, 1999). Although many hybrid forms are emerging through the growing activities of multinational companies and with the increased effect of liberalization and de-regulation, these two models nevertheless present clear distinctions in the ways firms raise capital (Hodges & Woolcock, 1993). 3

The separation of ownership and control in the Anglo-Saxon corporate tradition gave rise to a vast literature examining the challenges of separation and ways to cope with the diverging interests of the parties involved. The most influential of them, principal-agent theory [P-A], points out that the conflicting interests of owners (principals) and managers (agents) of a firm generate agency costs and inefficient firms. To overcome this conflict, the P-A perspective stresses the importance of aligning managerial and shareholder interests (Jensen & Meckling, 1976; Short & Kevin, 1999). Agency costs are minimized when management and shareholder interests are aligned through the ownership structure (Alexander & Cohen, 1999) and monitoring rights are secured to dissuade managers from pursuing their own interests at the expense of the owners (Alchian & Demsetz, 1972). To cope with agency costs, either managers' interests are brought closer to the owners' by tying managers' compensation to the performance of the firm, or the market must efficiently discipline managers' opportunistic or disapproved behaviors.

Institutional economists, on the other hand, emphasize the importance a regulatory framework, capable institutions and law as essential components of economic performance and corporate governance (Lal, 1998, 2000). A legal system that guarantees monitoring rights, especially the rights of small shareholders, and the market institutions that allow shareholders to monitor and react to the managerial team are prerequisites for a well-functioning, market-oriented system (Cheffins, 2000). Similarly, the self-regulatory regimes and code of practices put forward by the business community and interest groups including government agencies, shareholder associations and stock market institutions play a crucial role in safeguarding business practices. At the policy level, the importance of the regulatory framework has been recognized by national and supranational institutions in a rapidly changing and global economy (Iskander & Chamlou, 2000; Lannoo, 1998, 1999). 4

Both the P-A argument and institutional economics fail, however, to explain why there have been corporate failures and abuses that periodically invited further regulation even in the most advanced capitalist economy, the United States, and others such as the United Kingdom. The classic theory of discipline implemented by the capital market over business performance is ineffectual when stock prices have been manipulated through diluted accounting principles in the recent corporate scandals unleashed first by the collapse of Enron and WorldCom and followed by others in the United States. This trend of malpractice defies theoretical assumptions about the market disciplining businesses and managers. 5 When not only managers but the much wider business community act to defy and misinform each other in order to speculate on company shares, the impact of regulation and measures to minimize agency costs become irrelevant.

Moreover, the maximization of self-interest in a capitalist economy is justified and the destruction of businesses is also seen as part of the innovative and creative side of the market. Thus, corporate collapses and share value manipulation appear not just as an “abuse” but as an outcome of the “bullish” behavior of market capitalism. This fine line between regulation and entrepreneurial opportunism is best defended by Cressey (1980, p. 126): “Weak accounting controls are essential to modern business, just as weak police controls are essential to modern democracy.” In the boom and bust cycles of economic and technological change, the issue of managerial abuse also turns into part of an entrepreneurial drive which fuels market growth. 6 There are arguably two benefits of these business cycles: First, wider societal groups increase their earning during the technological boom through employee shares and other schemes (Blasi et al., 2002). Second, the boom cycle nurtures technological innovation and triggers further cycles of growth in the long term.

Emerging market economies such as Turkey, however, suffer persistent abuse by managers, politicians and institutions (Blasi & Shliefer, 1996; Fenkner & Krasnitskaya, 1999; Frydman et al., 1996; Kogut & Spicer, 2002). Nevertheless, there are important distinctions between capital market failures in advanced economies and the failures of developing countries to establish capital markets. While there are larger and wider distributive effects and long-term technological spillovers of capital market
manipulations in the former, the latter tend to depend on a narrow business base with no technological depth, leading to detrimental effects for the economy and society. Thus, in developing economies, the adjustment to the boom and bust cycles of financial market manipulation and financial liberalization often has long-term destabilizing effects with widespread painful outcomes (Alper & Öniş, 2001; Cizre-Sakallıoğlu & Yeldan, 2000).

We hold the premise that the politics of institution building and social and behavioral norms determine economic life and that trust in regulatory regimes can best be understood as a product of the interaction of the state and society. Trust in economic life, Granovetter (1985) points out, is a product of social relations and the obligations inherent in them, rather than some generalized morality or institutional arrangements. Similarly, politics influences the functioning of the market and regulatory structures in a dynamic interaction with social norms. When individuals do not trust the state and its institutions, mere regulation is insufficient to guarantee impersonal trust. Hence, when the state loses its power and/or impartiality in law enforcement, the narrow group interests of political clients take over the control of economic management, further undermining impersonal institutions and regulation. While accepting the flaws and paradoxes of trusting relationships and the persistent threat of abuse, we agree with Shapiro (1987) that impersonal trust permits more complex developments in economic life by allowing individual and organizational actors to engage in complex relations on behalf of principles.

The first wave of Anatolian holding companies illustrates how impersonal trust was neglected by regulators and the second shows how societal obligations and the moral grounds of Islam failed to guarantee the survival of these companies in the absence of credible institutions and regulation.

3. TURKEY’S DISASTROUS EXPERIMENTS WITH CAPITAL MARKETS

The Turkish experience with capital markets has been driven by the short-term political and financial objectives of governments, mainly to fund populist policies. The result of redistribution and public sector spending has been to channel funds to rentiers rather than to productive businesses (Alper & Öniş, 2001; Batatav et al., 1996; Cizre-Sakallıoğlu & Yeldan, 2000). Many experiments with capital markets also led to the chronic abuse of investors by governments, banks and businesses.

The longstanding practice, dating back to the late Ottoman period, was for businesses to use the informal money lending market [tefecilik]. Speculation and unfair practices leading to confiscation of businesses and properties by loan sharks continued despite banking reforms in the early 1920s (Günlük, 1983). The banks generally offered credits only to successful businesses or to new ones with good political connections. This bank-centered form of corporate governance (see Table 1) has long functioned through cosy relations between major business groups, industrialists and politicians, as happens in other similar economies (Bugra, 1994; Maxfield & Schneider, 1997). This exacerbated the gap between undercapitalized small and medium-sized businesses and large family holdings. Many small and medium-sized enterprises (SMEs) were forced to raise their equity through these informal and segmented capital markets embedded in local and family networks (Özcan, 1995a, 1995b).

(a) Bond market failures prior to 1980

During the years of expanding import-substitution policies, the government-financed industrialization through the single mechanism of bank-centered industrial growth. Starting from the 1960s onward, Turkish governments re-

<table>
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<tr>
<th>Debt\equity</th>
<th>Bank loans</th>
<th>total liabilities</th>
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<tbody>
<tr>
<td>Germany</td>
<td>0.59</td>
<td>n.a.</td>
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<tr>
<td>France</td>
<td>0.73</td>
<td>0.25</td>
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<tr>
<td>Japan</td>
<td>0.77</td>
<td>0.39</td>
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<tr>
<td>Sweden</td>
<td>0.65</td>
<td>0.24</td>
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<tr>
<td>United Kingdom</td>
<td>0.55</td>
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<tr>
<td>USA</td>
<td>0.41</td>
<td>0.09</td>
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<tr>
<td>Turkey</td>
<td>0.62</td>
<td>0.51</td>
</tr>
</tbody>
</table>

Source: For the figures about Turkey see Yener (1990) and Ersel and Sak (1986). For other countries see Berglöf (1990).

The ratios are for the year of 1983 for the countries other than Turkey. For Turkey, the average of 1984–89 was taken as the base. Bank loans include short and long-term loans and the debt equity ratio refers to short and long-term liabilities/total assets.
sponded to the growing need for financial capital, first with a set of measures to attract foreign reserves and later with the introduction of government and private bond markets. Thus, transferable foreign currency accounts, were first introduced in 1967 to overcome the shortage of foreign reserves and to fill the increasing gap in the balance of payments. Under this system, the government offered higher interest rates than European banks with variable options for investors. But, the fast growth of short-term interest had an inflationary effect that quickly became unsustainable. In 1973, the government announced the end of transferable foreign currency accounts, but this scheme was re-introduced during 1975–79. During the first period of implementation, these accounts reached US $462 million, 70% of which was held by Turkish workers abroad. This was a significant capital injection into Turkish banking (Uysal, 1996). The Anatolian holding companies were first promoted during the years of rising domestic savings when the savings accounts of Turkish workers became unsustainable due to short-term financial pressures.

Along with industrial growth in the 1960s, the amalgamation of small companies led to the emergence of holding companies. At the same time a new market for bonds and promissory notes emerged. This capital was used both by governments to finance investments and by businesses to generate growth. In the absence of any markets for issued papers and shares, there appeared a thriving informal bond market. In 1961, the government re-structured the rules governing savings bonds. The idea was to provide capital for state spending in agriculture, industry and transportation through compulsory savings schemes. These bonds were largely distributed to wage-earning families and government employees as part of tax schemes. Seeing an opportunity for easy profits, small bond traders gradually acquired many of these government bonds from families in need of ready cash until a further regulation in 1969 introduced limits on the trade. In 1972, these savings bonds were abolished, leading to the elimination of the bond traders.

Yet, informal bond trading and money lending continued to survive. A 1957 law regulated private bonds and shares issued by the holding companies and limited liability companies. This law also limited rates of return issued through these bonds. Thus, tampering with the flexibility of bond returns significantly narrowed the scope for generating financial capital through bonds. In the absence of any capital market regulation or stock exchange, businesses sought to trade their bonds in return for cash. With the increased economic instability and high inflation during the first and second oil crises of the 1970s, the bank-centered corporate regime collapsed. Many companies in need of cash consequently boosted the informal money market and its loan sharks (Günlük, 1983). Until the final collapse of the economy at the hands of an International Monetary Fund (IMF) program in 1978, the balance of payments continued to deteriorate while the external trade deficit grew sharply and industrial stocks soared.

Thus, up to the 1980s the informal bond trade served the short-term needs of the governments, businesses and bond traders alike. The governments were mainly concerned with budget deficits and current account balances at the expense of the goals of long-term industrialization and development due to strong populist policies (Cizre-Sakallıoğlu & Yeldan, 2000). The holding companies wanted to obtain capital for business growth with no financial and corporate accountability and the bond traders and investors were mainly interested in the short-term benefits of the bond trade. Thus, the semi-illegality of the bond market served the interests of all without any collective pressure to introduce a more sophisticated and institutionalized capital market with regulations and punitive measures for abusers. Shortly after the economic collapse of the late 1970s, this short-term opportunism contributed to a massive disaster in capital markets and the resulting social trauma.

(b) Military coup and economic liberalization in 1980

In 1980, soon after the post-coup market liberalization reforms, another frenzy occurred in the form of lavish bond trading. As Turkey’s pace of industrialization increased in line with global trends and liberal economic policies, the lack of capital markets became even more acute. The governments issued promissory notes and other revenue-generating bonds in order to finance growing government spending. There appeared a new function for informal money-lending bankers to fill the vacuum. The informal money-lending business which survived alongside bank-centered corporate finance for many decades was elevated to a respectable business status with political endorsements in the early 1980s. Hundreds of private banks mushroomed.

In January 1980 a banking regulation decree removed state control over interest rates. In order to attract informal and black money into the formal economy the decree also declared that banks could sell nonidentified short-term account bonds. But the major banks would only give credit to the most successful businesses and the banks of family holding companies extended credit mainly to their affiliated companies. While the bond and other paper trade grew rapidly with increased market expectations of economic recovery, many businesses ended up borrowing from the market bankers using their bonds, promissory notes or checks as equity.

High interest rates triggered a spree of investments in banks and other money lending businesses. Wage earners invested their savings, pensioners their retirement bonuses, and many families even ended up selling their houses and other properties with the expectation of high returns. Encouraged by this craze, well-established banks set up their own bond trading institutions with high interest rate accounts. Many holding companies also established their own bond trading agencies. The only legal requirement to be a market banker was to apply to the relevant town’s governorate with a petition, and after several bureaucratic steps, anyone could get permission. Small market bankers, however, took higher risks with much higher interest rates, up to 140%, and traded their own promissory notes and personal checks in addition to company bonds. While the bond and other paper trade grew rapidly with increased market expectations of economic recovery, many businesses ended up borrowing from the market bankers using their bonds, promissory notes or checks as equity.

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While holding companies went to well-established banks or used their own bond-trading institutions, many small and medium-sized businesses in financial difficulty preferred borrowing from market bankers since their low credibility and lack of political links barred them from getting loans from the established banks. With the economy and businesses in need of capital, the government remained silent; and did not attempt to regulate the market. During 1980–81, the total amount collected by market bankers was estimated to be around US $3.2 billion, one-quarter of total bank deposits. The formal banking sector lost massive revenues to informal bankers.

By September 1981 the losses to the formal banking sector became unsustainable, and the government put limits on the free market bond trade and banned advertisements by market bankers with a series of new decrees in September and October 1981. This shrank the flow of cash and many bankers ran into difficulties in paying back the interest. In panic, investors rushed to bankers demanding their deposits back. By December 1981 over 250 listed bankers went bankrupt and the total number of bankrupt institutions may have numbered more than 1,000 (Dincel, 1998; Yildirim, 1998). When the banker scandal ended in collapse, the high moral and financial costs included loss of savings, collapsed businesses, runaway bankers and family tragedies. 11 The government finally intervened and forced the bankruptcies of many major bankers and bond trading agencies.

This was followed by the resignation of three responsible ministers. The Economy Minister, Mr. Kaya Erdem, shrugged off his responsibilities with these words: “Our people have gambled” (Gunluk, 2000). The Capital Market Law was introduced and was soon followed by the establishment of the Istanbul Stock Exchange in December 1985. These institutions did not however significantly alter the ills of the financial regime.

The bank-centered financial regime faced a new wave of abuse at the hands of holding companies and their political allies through the 1990s. The deep economic crises in the late 1990s forced the government to respond with new regulatory reforms under the IMF program. But despite the institutional and regulatory amendments to create capital markets, the Istanbul Stock Exchange succeeded neither to attract significant savings from investors, nor to become a source of raising equity for Anatolian industrialists. As shown by Yurtoğlu (2000), only a small number of companies are traded in the stock exchange and the total market capitalization is around 12% of GDP. In this highly concentrated and centralized ownership structure, family-controlled holdings own directly or indirectly more than 75% of all company shares and exercise majority control. Thus, an active market for corporate control or monitoring shares does not exist given the limited openness and concentrated ownership of traded companies. Consequently, takeovers and hostile bids are not possible through stock market dealings but rather companies change hands through politically linked financial and banking deals, many of them scandalous. In this system, small shareholders are being persistently abused or at best ignored. Public companies of family
holdings traded on the stock market are being used as yet another way to transfer funds into the holding system.

Ordinary investors have prudently shied away from stock market dealings and often preferred foreign currency or real-estate investments. This further limited the securities trade and took funds away from businesses. Studies on household savings and investments quantify this trend and show that on average families retain their wealth in the form of real-estate (85%) bank accounts (11%), and while securities account for only 2.3% (Eser, 1999). A recent study by the State Planning Organization also highlights the remarkable growth of the shadow economy in Turkey throughout the 1990s. 12

These catastrophic experiments indicate that a pattern of abuse of investors occurred in an environment where abusers have not been punished and where honesty and dishonesty have been blurred in the eyes of the public. Enforcement actions have also become a hostage of these relationships where legality and illegality have had paradoxical interdependency further eroding the state's credibility. Thus, all parties hoped to maximize their returns by benefiting from the gaps in the legal and institutional framework and the generally weak rule of law.

4. THE RISE AND FALL OF ANATOLIAN HOLDING COMPANIES

Against the background of persistent capital market failures which undermined small investors and entrepreneurial businesses alike, the formation of Anatolian holding companies appeared to be a credible response by offering direct investment opportunities in productive activities. The belief in this form of alternative capital formation was promoted through various agents of change such as academics, technocrats, and politicians. But above all, the political ideologies of social democracy in the 1970s, and later political Islam in the 1980s, led the way as promoters of economic development with more social equality.

(a) Pioneers: Anatolian holding companies and socialist ideals in the 1970s

In the 1970s, Turkey had a closed economy with little industrial diffusion beyond a handful of metropolitan centers such as Istanbul, Izmir and Bursa. State-run enterprises and large family holding companies controlled the majority of industrial establishments in the country. The price of many goods was subject to state or local authority approval. There was almost no foreign direct investment and the foreign exchange reserves were fragile and small. National per capita income was around US $700. The severe shortage of industrial capital and the lack of industrial diversity and diffusion in the country were recognized as the main barriers to business development and growth. Political actors, local communities, and individuals were acutely aware of this problem. The idea of using small family savings and expatriate workers' remittances for business establishments and industrial diffusion first emerged in the early 1970s under the slogan of the “people’s sector” of the Republican Peoples’ Party (CHP) (Göklä, 1981; Soral & Tekeli, 1976).

The people’s sector initiative was primarily an economic mechanism to generate finance capital. At the same time, it was a means to diffuse social market capitalism and material prosperity through the widespread ownership and participation of “the people.” This initiative ambitiously aimed to achieve four major goals: to support a successful form of democratic left politics, to initiate economic development through diffused and decentralized modes of production, to enhance popular participation in the economy, and to create a new form of public–private cohabitation and partnership. These ideas were political but largely engineered by technocrats and a handful of academics in the powerful State Planning Organization. The ideological justification was related to the Cold War realities of a NATO member country as well as the moderate socialist teachings of the Republican Peoples’ Party which was inspired by the success stories of Yugoslav economic reforms (Ak Günlere, 1975; Soral & Tekeli, 1976).

The political and agency actors of the pioneering Anatolian holding companies wanted to benefit from the robust and growing rates of Turkish workers’ savings in Germany to overcome severe shortages of financial capital and hard currency (Van Renselaar & Van Velzen, 1975). 13 Turkish migration to Western Europe started in the late 1950s and grew very quickly. From the early decades of this migration until the first and second oil shocks of the 1970s, after which European countries closed their doors to emigrant workers, savings sent to
Turkey provided the main source of foreign exchange. Thus, migrants’ remittances quickly became a dominant source of foreign exchange and consequently the major source to balance the trade deficit of the country. This was quite similar to the experience of emigrants from other southern European countries at the time such as Greece, Spain and Italy (King, 1984). Savings of Turkish workers rapidly increased from a mere US $107.3 million in 1968 to US $1,426.2 million in 1974 accounting for 40% and 63.5% of foreign payments respectively (see Table 2). The Turkish government first tried to channel these savings to village cooperatives in the mid-1960s and later, encouraged by the spontaneous workers’ investment companies established in Germany, attention turned to ‘’workers’ companies.’’

The number of ‘’workers’ companies’’ reached 322 by the-mid 1970s. As Van Renselaar and Van Velzen (1975) point out, the existing family-run companies failed to raise capital through workers’ savings due to the lack of any stock market or experience with financial transactions. The social networks of workers, their local origins, and family ties played a role in the locational choices of investments. The workers took pride in the development of and the contribution they made to their towns (Ertuna et al., 1975). Yet, many companies were launched and funds collected without any investment feasibility analysis. Poorly educated and low skilled workers were unable to appreciate the importance of financial and technical project planning and the institutional setting for share ownership. A study conducted in 1973 covering 88 worker’s companies indicated that only 10 of them had investment projects and they were able to gather 19,439 shareholders with an average investment of TL5, 250 (US $380) per share. These companies had altogether TL102, 2 million capital (US $7.51 million) in investments and benefited from TL33, 375,000 (US $2,490,000) in investment credits (Van Renselaar & Van Velzen, 1975, pp. 124–125). By 1975, a selection of 77 worker’s companies had 60,000 investors with total capital of TL500 million, around 36 million US dollars in 1975 prices (Van Renselaar & Van Velzen, 1975, p. 131).

The majority of Anatolian holding companies (72%) were set up in priority development regions identified by the State Planning Organization and almost all of them (90%) were established away from major commercial and industrial towns. The inner Anatolian region witnessed the most rapid creation of Anatolian holding companies and attracted most investment while the poorest towns in the east and southeast had no investments. The investment incentives operated by the government played a strong role in locational choices. In terms of the sectoral composition, there was an obvious emphasis on industrialization as most of the investments were in the traditional manufacturing sector: investments concentrated on foodstuffs and beverages (23.4%), weaving and clothing (18.7%), construction material (14.1%), and animal feed (12.5%). An analysis of the shareholder composition indicated that the majority of these companies (87.5%) had more than 100 shareholders and a significant proportion (12.5%) had more than 2500 shareholders (Ertuna et al., 1975).

Weak institutional guarantees inhibited the survival and growth of Anatolian holding companies. Only a handful of new institutional players were created (see Table 4). Already existing institutions, such as the State Planning Organization, jealously presided over the process. There was however a serious effort to create financial institutions to secure investments such as the Co-operative Bank, the State Industry and Worker’s Bank [Devlet Sanayi ve İşçi Yatırım Bankası], Social Security Funds, and the People’s Investment and Partnership Limited [Halk Yatırım Holding Anonim Ortaklığı]. Despite the efforts at institution building, the initial euphoria was quickly replaced with institutional conservatism as the State Planning Organization wanted to preside over the entire process through its incentive schemes.

<table>
<thead>
<tr>
<th>Table 2. Money transferred to Turkey by Turkish workers abroad between 1965 and 1974 (in 1,000 US dollars)</th>
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<tr>
<td>------</td>
</tr>
<tr>
<td>Total Transfer</td>
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<td>Average per Worker</td>
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Again, the government failed to build an efficient institutional and regulatory structure to govern the new form of finance capital and the corporate entities created. The result was a dramatic failure rate among newly established businesses. Most of the failed companies were bought by the state. Surviving ones lost their multiownership character. This experience not only damaged the local economies and the shareholders but also created public mistrust of similar initiatives. This meant small family savings either remained dormant or were channelled into speculative investments rather than to productive activities for industrial growth. The outcome of this failure was also visible in the increasing property investments by Turkish emigrants in urban areas and holiday resorts (Keleş, 1985).

Early studies on Anatolian holding companies stress the interruption of permanent capital inflow and managerial problems as the main sources of the failures of workers’ companies (Balci, 1996; Ertuna et al., 1975; Şengün, 1977; Yılmaz, 1993). Many businesses faced severe liquidity problems during their intermediate investment stage. Some also suffered from export and import limitations. Financial problems originated from several sources. First, investors (typically workers) were not familiar with investing in shares. Therefore they were shy to invest in such unknown assets. Second, frequent business failures and high expectations discouraged them to invest in new ventures. Third, since investments concentrated in areas where returns can be obtained in the long run, such as manufacturing industry, investments yielded nothing for years. For this reason, company shares were less attractive than alternative investments such as real estate or gold. In addition, whereas it was difficult to cash-in the company shares because of the nonexistence of a stock market, the alternatives were easily traded.

Business problems stemmed both from managerial inability and abuses. Studies investigating the reasons for failure as well as our interviews indicate many poor decisions taken either at the establishment and/or early operation stages. Once again the technocratic nature of the initiative was apparent. Ertuna et al. (1975) found that 23% of the people who took investment decisions and 36% of board of director members had been civil servants. Managerial fraud was another major source of problems. The distance between the managers and shareholders who lived in Europe facilitated abuses. Due to reduced visibility, shareholders gradually lost their interest and failed to participate in a long-term engagement with the companies they invested in. The absence of bodies informing investors about the performance of the firms and mechanisms to control the managerial team (hire or fire them) further exacerbated the extent of abuses and the concentration of shares in the hands of a few individuals, especially managers. All of these factors but in particular the deficient regulatory regime contributed to the collapse of these business ventures by the late 1970s, even before the 1980 military coup.

Thus, another form of investment for workers and a less inflationary form of hard currency supply for the government was provided by workers’ companies. But the motives of both investors and the policy makers diverged when the early trust could not be maintained under the short-term pressures of seeing a concrete return. Investors, although ambitious and enthusiastic about generating jobs and businesses in their homeland, did not fully trust the state, the managers or the social democratic principles of workers’ companies, and invested only a small proportion of their savings.

(b) The second wave: Anatolian holding companies and Islam’s conversion to capitalism

After the dramatic collapse of the socialist ideals of the “people’s sector,” the second revival of Anatolian holding companies came as a “new model” and as part of “the just order” of political Islam in Turkey. Despite remarkable similarities in form, it took place under conditions very different from the 1970s. Turkey had its third military intervention in 1980. Although six years of street fighting and bloodshed ended with the coup, the new political regime, on the one hand, widened business opportunities and liberalism, but on the other hand, it narrowed the scope of democracy in the country. Turkey entered the 1990s with an open liberal economy with export-led growth. The per capita income rose to US $5,000 as measured in purchasing power parity.

Market deregulation opened many new business opportunities and Turkey witnessed a rapid rise in new business ventures and entrepreneurial activities. The growth of small and medium-sized enterprises in many nonmetropolitan towns and capital accumulation in the hands of people who had strong rural traditional ties created a new generation of
These capitalists developed a strong antipathy toward the family cartels that controlled the country’s economy as well as the inefficient state enterprises. This antagonism crystallized around a notion of hard-working, genuine Anatolian people with Islamic traditions, as opposed to the cosmopolitan and disingenuous Istanbul capitalists (Çokgezen, 2000; Tugal, 2002). These small-scale entrepreneurs in conservative Anatolian towns later played a crucial role in reforming Islamic politics and in building the second wave of Anatolian holding companies (Ozcan, 2000).

The new entrepreneurs desperately needed more financial capital. Small investors and families, too, hoped to make long-term, income-generating investments in the growing economy. Most of these small investors traditionally channeled money into the property market and land speculation. But this began to change as the rhetoric of political Islam found popular support in Turkey and among Turkish workers abroad. Following the 1980 coup, Islam became a favorable ideology against communism and therefore was modestly promoted by the army and Turkey’s major allies. The number of Islamic groups, organizations, and publications increased rapidly in the 1980s. The increased presence of Islam in political and social life was accompanied by an intensified debate on development and modernization within Islam.

Industrialization and business ventures became the symbols of Islamic modernization, an intellectual development which was led by Islamic scholars and a group of educated devotees from the 1960s. This conversion of Islam to capitalism should be seen as part of deeper changes in the political and ideological scene as Turkey adjusted to the turbulence and inequalities created by late modernization and liberal capitalist development. Already by the late 1980s, but especially during the 1990s, a new form of multiownership company emerged under the banner of Islamic economic revival and just order. This synthesis of industrialization, development and Islam took decades to find a receptive audience beyond its core engineers and thinkers within party politics.

The enthusiasm with Islamic development and Islamic finance among Turks also followed a worldwide trend of the increasing popularity of Islamic banking in Saudi Arabia around 1970. The function of Islamic banking as a pious form of lending gradually spread out from mainly oil-rich countries to Islamic regimes such as Pakistan and later to secular regimes such as Turkey (Warde, 2000). But, Islamic economics is a rather new scholarly concern initially developed by Indian Muslim thinkers during the years of India’s partition and the most visible element of this concern has been Islamic banking.

Euphoria around Islamic economics found new strength in the Welfare Party and its affiliated community and business organizations that pioneered Anatolian holding companies among Turkish workers in Germany. Many but not all Anatolian holding companies followed the Islamic finance principle of profit and loss sharing or partnership finance through selling issued bonds of companies and investors to individuals, families and businesses. In its pure form, this was a micro capital formation through thousands of bonds and investors. The early attempts led by investors and managers and their agents proved to be enormously successful. These Anatolian holding companies quickly became romanticized and heroic symbols of “new industrialization and just order” associated with Islamic populism.

This branding of moral salvation with material benefits points out the core sentiment which made the so-called Islamic economic order attractive to ordinary investors. While Islamic rhetoric condemned the individualistic societies of the West for being immoral, individual interests, nevertheless, provided the core motivation for investing in Anatolian holding companies. This paradox is addressed by Açıkel (1996) as the desire of repressed and marginalized masses to seek power while Tugal (2002) identifies Islamic populism with unfulfilled aspirations and desires to change the hegemony. Çakır (1995) among others (for example Göle, 1999) sees the rise of Islam as a movement against and in response to modernity. The Islamist party of the early 1990s, the Welfare Party, used the shortcomings of secularism as part of its propaganda to show its unique position in defending Islam and traditions as well as just society. Paradoxically, both sterile secularism and political Islam have long survived by side by side despite periodic clashes in Turkey. Indeed, as Shankland (1999) illustrates, Islam and Islamic politics were rather well accommodated within the secular state establishment. Açıkel (1996) goes further to suggest that the Turkish-Islamic synthesis has been the semi-official ideology of the Republic from the 1950s onward.
The success of Islamic politics has also been due to its strong penetration of communities and families through voluntary associations, brotherhoods and pious associations. This penetration also helped political Islam to gain popular support among Turks in Germany. The prototypes of the second wave of Anatolian holdings first occurred in the 1980s but they only became popular in the 1990s. The new companies, established largely in conservative Anatolian towns, especially Konya, were not only successful in attracting small investors, they also developed a diversified business portfolio. The rise of these Anatolian holding companies under the banner of Islam has been dramatic. For example, over 80,000 shareholders invested in just 11 of these holding companies (see Table 3). Companies such as Yimpas and Kombassan also have many international investments. The small investments were gathered through the use of a wide range of Islamic associations, mosques and coffee houses, family and kinship networks. Most of the practices to collect and transfer savings have been illegal, as no intermediary financial institutions or banks were typically involved. 22 MUSIAD, the association of Islamist businessmen, and Islamic finance institutions assisted the formation of the companies by providing their networks, political protection and business information. Along with Turkish-owned financial institutions such as Anadolu Finance, Ihlas Finance and Asya Finance, there were also major Arab Islamic institutions involved such as Faisal Finance, Al Baraka Turk, and the Kuveyt Evkaf Finance. These financial institutions were controlled by different Islamic groups which supported mainly their business associates. 23 MUSIAD later became the only business organization where such companies played a leading role in business formations and Islamic politics, especially during the short coalition period in the early 1990s when the Welfare Party was a junior partner in the ruling coalition.

Although there are no credible data, the scale of money transfers through Anatolian holdings has been enormous. According to some figures, the investments channelled from Germany and Europe by holding companies reached billions of DM by the end of 1990s (Şen, 2000) and the number of holding companies reached 200, although many remain unaccounted for. Germany became the major source of capital and corporate activity. A survey by the Turkey Research Center in Berlin traces the link between mainly Konya-based Anatolian holdings and their Islamic organizational roots and shows them mushrooming in Germany. The study reports 54 holding companies, many of them based in Konya. We were able to trace some information on only 20 of these companies (see Table 3). As part of their semi-legal presence, there is very little public information on these companies and their corporate nature. 24 There is also no research on their formation, growth or shareholder structure. All that we know for sure is that a large number of shareholders reside in Germany.

Part of the problem comes from the fact that these holding companies have been continuously threatened by the scrutiny of the official Capital Markets Board because of their blurred accountability and nontransparency. The Capital Markets Board often issued warnings and decrees asking for more information on the nature of bonds and for disclosure of company activities. Our survey on these decrees between 1999 and 2001 shows that the majority of these companies issued shares illegally without complying with Article 4 of the Capital Markets Regulation, which requires all shares or bonds issued to be reported to and registered with the Board. There are also issues related to the lack of transparency in registering the shares and in company accountings. These irregularities were noted and legal action was taken against at least nine companies: Kombassan, Yimpas, Kaldéra, Kübra, Endüstri, Şule Besicilik, Jet-Pa, Trakya and Kimpas.

One of the main differences of the second wave is the character of the assets sold to investors. These are called “shares” but legally they provide no rights that an ordinary share in a regulated market provides. Investors were promised a fixed return beforehand. The entrepreneur/managers offered to provide a profit and loss share to avoid interest, since yielding interest is forbidden in Islam. The shares are issued in the name of the holding company. In this way, permanent payments are justified. If the shares were in the name of a constituent firm within the holding company it would have been impossible to maintain payments to investors when that division made losses. Though it seems tricky, the new assets promoted permanent capital inflow since investors received high returns on their investment in the short run. Despite its advantages, the new asset had the big drawback of not being defined and protected legally. Even though it was very similar to the bonds issued by regulated public
Table 3. Holding companies based on multiownership structures in Turkey

<table>
<thead>
<tr>
<th>Holding</th>
<th>Town of origin</th>
<th>Year of establishment</th>
<th>Investments in towns Countries</th>
<th>Total no. of companies</th>
<th>Businesses activity</th>
<th>No. of employees</th>
<th>No. of shareholders</th>
<th>The share limit (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kombassan</td>
<td>Konya</td>
<td>1989</td>
<td>Aksaray, Antalya, Karaman, Istanbul, Mersin, Mușla, Tekirdag Kazakhstan and Germany, USA, China</td>
<td>40</td>
<td>Motor vehicles, shopping malls, paper, packaging, marble, textile, transport</td>
<td>8,000</td>
<td>26,000</td>
<td>speculated to be 80,000</td>
</tr>
<tr>
<td>Yimpaş</td>
<td>Yozgat</td>
<td>1982</td>
<td>Thirty towns in Turkey Germany, Bulgaria, Turkmenistan</td>
<td>24</td>
<td>Supermarkets, food processing, entertainment, health services, education and marketing</td>
<td>10,000</td>
<td>30,000</td>
<td>1</td>
</tr>
<tr>
<td>Ittifak</td>
<td>Konya</td>
<td>1988</td>
<td>Beyşehir, Denizli, Istanbul, Konya, Seydisehir</td>
<td>16</td>
<td>Machinery production, delivery, shopping malls, data processing, textile, rental cars, packaging</td>
<td>1,150</td>
<td>14,000</td>
<td>1</td>
</tr>
<tr>
<td>Adim</td>
<td>Istanbul</td>
<td>1993</td>
<td>Istanbul</td>
<td>5</td>
<td>Construction, automobile trade, printing and publishing, insurance and marketing</td>
<td>100</td>
<td>250</td>
<td>1</td>
</tr>
<tr>
<td>Sim</td>
<td>Ankara</td>
<td>1993</td>
<td>Ankara, Kemer Germany</td>
<td>3</td>
<td>Tourism, rental cars, construction</td>
<td>200</td>
<td>90</td>
<td>n.a.</td>
</tr>
<tr>
<td>Kimpas</td>
<td>Konya</td>
<td>1988</td>
<td>Beyşehir, Denizli, Istanbul, Konya, Seydisehir</td>
<td>3</td>
<td>Trade, packaging, food processing</td>
<td>80</td>
<td>800</td>
<td>n.a.</td>
</tr>
<tr>
<td>Büyük Anadolu</td>
<td>Istanbul</td>
<td>1993</td>
<td>Bafra, Istanbul, Samsun</td>
<td>11</td>
<td>Health services, construction, cleaning materials</td>
<td>1,050</td>
<td>4,000</td>
<td>n.a.</td>
</tr>
<tr>
<td>Sayha</td>
<td>Konya</td>
<td>1993</td>
<td>Konya, Ismil</td>
<td>10</td>
<td>Data processing, granite and marble, tourism, construction, metal products</td>
<td>550</td>
<td>5,000</td>
<td>2</td>
</tr>
<tr>
<td>Aksaray Holding</td>
<td>Aksaray</td>
<td>1997</td>
<td>Aksaray, Frankfurt, Istanbul</td>
<td>10</td>
<td>Furniture, textile, health services, tourism, foreign trade, spare parts production, media, insurance</td>
<td>500</td>
<td>n.a.</td>
<td>n.a.</td>
</tr>
<tr>
<td>Holding</td>
<td>Location</td>
<td>Year</td>
<td>Description</td>
<td>Capitalization</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Umpas Holding</td>
<td>Uşak</td>
<td>1997</td>
<td>Foodstuff, plastic, construction, fuel distribution, automobile trade</td>
<td>700</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kamer Holding</td>
<td>Konya</td>
<td>1998</td>
<td>Food, industry, service, tourism</td>
<td>500</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kimpas Holding</td>
<td>Karaman, Netherland</td>
<td>1993</td>
<td>Supermarkets, food processing, packaging, construction, pad production</td>
<td>500</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kubra Holding</td>
<td>Konya</td>
<td>1998</td>
<td>Glass, stock-breeding, nail production, water (bottling and marketing)</td>
<td>250</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Osmanlı Holding</td>
<td>Kirşehir</td>
<td>1999</td>
<td>Textile, foodstuff, plastic, iron</td>
<td>165</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Büyük Selçuklu Holding</td>
<td>Kayseri</td>
<td>1998</td>
<td>Textile, foodstuff, construction, automobile trade, media</td>
<td>110</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Başak Holding</td>
<td>Konya</td>
<td>1997</td>
<td>Packaging</td>
<td>60</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hasandağı Holding</td>
<td>Aksaray, Konya</td>
<td>1998</td>
<td>Packaging</td>
<td>22</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tuğra Holding</td>
<td>Konya</td>
<td>1997</td>
<td>Food processing, textile</td>
<td>16</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Maksia Holding</td>
<td>Karaman, Konya</td>
<td>1999</td>
<td>Construction, power, insurance, textile</td>
<td>150</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>İmet Holding</td>
<td>Konya</td>
<td>1998</td>
<td>Tourism and foodstuff</td>
<td>50</td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>

companies, the new ventures did not refer to them as “bonds” since such a classification would cause them to lose their investors. Since the companies had to pay the agreed return to the investors, they invested in areas where cash flow is fast and secure. As one consequence, some of the best run modern supermarkets and hypermarkets were established by Yimpaş and Kombassan. This form of investment is an obvious diversion from their initial promise of bringing industrialization and high-technology. Our interviews with company managers also show that this ambition has long been undermined by the need for fast cash returns.

Early in 2000, an ever-increasing number of bankruptcies and corporate collapses triggered an unravelling of the Anatolian holding companies. For those who are genuinely trying to prosper and survive, there remain the two problems of management and finance. Thus, the only safeguard has been the perceived trust of successful entrepreneurs. The lack of legal supervision and the ease of gathering enormous amounts of money from investors opened ample avenues for opportunists and swindlers. There was also no effective way to differentiate honest ventures early from the fake holding companies initiated by swindlers. For instance, Jet-Pa was established with a promise of industrial growth and wealth generation, but went bankrupt after managers swindled the assets. There are holding companies that have collected savings but invested in nothing. Failure of these opportunist ventures, especially Jet-Pa, which had one of the largest number of shareholders, interrupted capital inflow to the system. Second, some of the companies grew very rapidly, even more rapidly than they expected. But the same performance and speed could not be generated through investments by holding companies. Yet again, without skilled directors and in the absence of any oversight, the Anatolian holding companies suffered from managerial incompetence as well as abuses.25

As in the late 1970s, worsening economic conditions in 2000 exposed inefficient companies to final collapse first and many Anatolian holding companies have been among these. At the time of writing, most of the initial 200 holding companies are either insolvent or about to become so (see also Odabaşı, 2001). This occurred as Turkey was entering another period of economic and political instability with the recent collapse of the public finance regime. The deep economic and political crisis damaged almost every business and many companies went bankrupt. Despite the secrecy and lack of clear information surrounding these companies, there is enough evidence to suggest that Anatolian holding companies were under stress even before the economic crisis.

After the loud and disastrous collapse of Jet-Pa, which was believed to have collected money from around 25,000 people for its non-existent companies and businesses, several shaky companies such as Endüstri Holding, Kimpaş Holding, Büyük Anadolu Holding, and Investment Holding were in trouble. The business collapses extended to the most successful business group, Ihlas Holding which established and supported many other holding companies. The bankruptcy of Ihlas damaged the entire finance network of its companies and individual investors together with its geographically diverse business network. Kombassan had to sell several bad investments, such as Hit & Miss and Faisal Finance, with big unspecified financial losses (our interviews, April 2001; Odabaşı, 2001). Islamic holding companies also lost their political patronage as the Welfare Party and its successor, the Virtue Party, were closed down by the Constitutional Court due to their anti-secular behavior.26

5. ANALYSIS: POLITICAL DISCONTINUITY AND THE ETHICS OF GAMBLING

Our findings illustrate that the dramatic mortality rate of Anatolian holding companies is associated with widespread managerial incompetence and abuses. The lack of institutional and regulatory structures gave way to opportunistic investments and business transactions manipulated by short-term interests. As with the failures of the special account scheme and the bond market, the resulting high mortality should be seen in the context of failures to create sustainable capital markets and regulatory regimes for business growth.

The critical question for Anatolian holding companies was why investors did not discipline managers. Although in the 1970s investors had certain legal rights, in practice institutional channels to intervene were almost completely closed to small shareholders. First of all, since share owning was not a common phenomenon and there were no clear information channels to encourage shareholders to use their rights, shareholders had no idea how to participate in decision-making processes. For many their
share was merely a long-term investment with regular annual gains as dividends.

Second, the geographical distance between shareholders and the companies inhibited them from joining board meetings and observing managerial practices. Third, zero or very low returns on the shares of industrial investments did not attract workers to pursue their interests and reinvest. But, managers, who were in control and had better information about the future returns of the company, increased their shares. Thus, many companies faced management buy-outs. Therefore, the ownership structure of the surviving workers’ companies changed and became companies owned by the managers and board members, as in the case of Russian privatization schemes (Blasi & Shleifer, 1996; Fenkner & Krasnitskaya, 1999). Even had the investors used all the rights defined by Alchian and Demsetz (1972) at zero cost, there were no effective ways to receive information about the firms in order for the owners to assess managerial performance. Intermediary institutions, which could have acted on behalf of shareholders, were never fully established.

Although never openly admitted, the first experience in the 1970s envisaged an insider-controlled corporate structure (see Table 4). In this model, institutional ties more than the rights of small or individual shareholders were given weight for long-term economic interest and business stability. Through the creation of the Turkish Industrial Bank and others, the government wanted to create the setting for such a mechanism whereby small investors would be integrated into corporate mechanisms through financial and intermediary institutions tightly controlled by the state. This was clearly influenced by the German model of corporate governance. Why then could the success of the insider control model, as seen in Germany, not be replicated in Turkey? The creation of an institutional web and their legal bases was urgently needed but the social democrat government could not carry out this institution building and impersonal trust could not be created with this half-hearted commitment.

The 1990s experience emerged under the patronage of Islamic politics in an even worse institutional and legal vacuum than the earlier period as neither the legal system nor the initiators were willing to adjust the institutional and regulatory environment for the needs of new capital formation. Its main actors however were informed about the earlier experiment with the workers’ companies. Islamist business propaganda was based on a romantic assumption: Islamic businesses, by avoiding corrupt, un-Islamic business practices, were embarking on a new economic rejuvenation and just society. In this system investors had none of the legal rights necessary (Alchian & Demsetz, 1972) but more investors were attracted and trust supported through direct contacts between investors and their agents in social networks of kinship, family and religious ties. Thus, the system was solely based on personal trust among investors, entrepreneurs and managers with no legal guarantees. Many entrepreneur managers were opportunists who abused their positions, disguised under the moral facade of religion. The reason behind this vast abuse was again the lack of legal guarantees and institutional provisions, which could have tamed the managers’ irresponsibility and investors’ ignorance. The gap between reasoning and gambling was so wide that many investors simply trusted managers who claimed to be “one of them” and faithful, or because they promised high returns from moral businesses. There was no need to invent excessively tricky ways to perpetrate fraud. Especially after the initial success of pioneers such as Kombassan, the appetite for good returns increased among those who wanted to invest their savings in business, whether moral or not.

Misperceptions about Islamic finance led to the belief that “the dynamism in Islamic finance and businesses is held back by state control and it was going to lead to a new economic rejuvenation in the Islamic world” (Khalaf, 2001; see also Warde, 2000). As in other Islamic countries, emerging Islamic populism provided an appropriate tool for a romanticized and liberating notion of Islam for justice and fairness (Afrasiabi, 1995). Likewise, the Islamist businessmen and their groups in Turkey, on the one hand, enjoyed the state incentives and benefits but on the other hand disregarded formal legal obligations and procedures. The intensified political polarization and “victimization” also benefited the Islamic party and the holding companies. Instead, they relied on an internalized moral system and Islamic persuasion which worked well in reducing transaction costs and facilitating business expansion along the lines of different Islamic networks and their affiliates. These networks grew fast as many small businessmen saw the opportunity to grow and feel secure within them. For example, MUSIAD rapidly grew from small beginnings in 1990 to reach a
Table 4. Comparisons between the first and second wave Anatolian holding companies

<table>
<thead>
<tr>
<th>First wave in the 1970s</th>
<th>Second wave in 1990s</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Years of closed economy and import substitution</strong></td>
<td><strong>Years of liberal export-led economic growth</strong></td>
</tr>
</tbody>
</table>

**Institutional guarantees and legal frameworks**
- Strong government support
- Strong institutional role assigned
- New institutions created but dominated by the State Planning Organization
- Incomplete regulatory regime
- Investors exposed to any abuse or loss

**Involvement of financial institutions and institutional investors**
- High involvement of State Banks
- High involvement of State Planning Organization (DESIYAB, Turkish Development Bank, Sanayi Yatırım Bankası, İş Bank, Ziraat Bank)
- No involvement of state banks
- Low involvement of private banks
- Mainly Arab Islamic banks

**Developmental rhetoric and ideals**
- Industrialization through social democracy
- Wealth creation through wide spread ownership
- Diffuse industrialization to small towns
- Industrialization through Islamic welfare
- Wealth creation through moral business
- Just order for small towns and small and medium-sized enterprises

**Source of capital**
- Savings of Turkish workers abroad
- State institutions and entities
- Savings of public workers and bureaucrats
- Local businessmen and other investors
- Savings of Turkish workers abroad
- Savings of local merchants and business families
- Small and medium-sized enterprises

**Locational and sectoral choices**
- Primarily inner Anatolian towns
- Incentive priority areas
- Manufacturing (consumer and intermediate prod.)
- Inner Anatolia with center in Konya
- Incentive priority areas of inner Anatolia
- Major metropolitan cities
- Manufacturing and service (especially retailing)

**Rights of investors**
- No open market for trading shares
- Nontradable
- Limited information through public institutions
- No open markets for share trading
- Limited informal trading
- Information limited to managers’ discretion

**Managerial control and performance**
- De facto unlimited control rights
- Incomplete legal and institutional regulation
- Vague notion of state guarantees
- Managerial actions unaccountable
- De facto unlimited control rights
- No legal and institutional regulation or control
- Islamic value system and norms
- Managerial actions unaccountable

**Initiators and main actors**
- Technocrats
- Social Democrat Party and its leadership
- Workers’ and townspeople associations
- State owned institutions and banks
- Supported by German and Dutch governments
- Small business owners and local entrepreneurs
- Islamist party politics and its leadership
- Islamist charities & business groups (MUSIAD)
- Workers’ associations abroad
- Pious foundations and Milli Görüş

membership of 3,000 firms by 1997 (Çokgezen, 2000). But, this outpouring of faith neither prevented abuses nor solved complicated problems of businesses.
MUSIAD, as the only major representative of Anatolian holding companies, recently changed its strategy and tried to safeguard the viability of the system through self-regulation. In March 2000, 18 multiownership companies were invited by MUSIAD to solve information problems with investors and block opportunistic individuals who threaten the reliability of the system. In this meeting, the MUSIAD representatives and the directors of the companies involved decided to discipline businesses to prevent the abuse of Islamic beliefs. MUSIAD members agreed that errant companies would not use Islamic symbols in their commercials and promotion activities, and they also would contact the Capital Market Board regularly to explain their problems and needs. Two well-known, fraud-stricken companies, Jet-Pa and GAP Holdings, were expelled from membership while Endüstri Holding was forced to resign because of their reluctance to comply with the association (Özler, 2000).

We identify three interlinked factors that hindered the genesis and the development of a viable capital market reform and regulatory institutions in Turkey. They also persistently undermined impersonal trust in economic life.

(a) Populist politics

Populist–clientalist cycles moving around a slippery political center have created discontinuity in politics and law making. Governments with no respect for fiscal prudence persistently followed populist policies while the political center shifted between right and left with little policy determination. This made the policy framework a highly contested arena with more conflictual relations than consensus-based approaches among law makers. Thus, the regulatory environment for capital markets has been incomplete and suffers constant political turmoil. During 1970–2000, Turkey had three military interventions during which the political focus shifted from socialist ideals in the 1970s to right-wing liberalism in the 1980s and then to the politicization of Islam in the 1990s. The political uncertainty and shaky coalitions throughout the 1970s and the 1990s failed to produce a coherent institutional and ideological justification for the survival of Anatolian holding companies within the context of a broader capital market reform. Neither the determination of the Turkish political elite nor the public commitment lasted long enough to build the necessary institutions and laws. Instead, the inappropriate legal and institutional structures failed to reward success, regulate the market and punish the abusers. Therefore, institutions that meant to be invigorating the process ended up functioning as decommissioning and bankruptcy agencies (Balci, 1996).

(b) Lax oversight under the single leader tutelage system

Over the years, single leader tutelage in party politics nurtured incompetent leadership structures. This favored clientalist relations with certain narrow, albeit changing, business interests rather than creating viable long-term regimes. Alper and Öniş (2001) identify single-leader tutelage in party politics as the major reason behind the short-term electoral focus in Turkey. Turkish political leaders have traditionally hung on to their power for decades despite their electoral and policy failures. This leadership structure nurtured conformist relations among the top policy makers close to party leaders, their business allies and the bureaucrat elite. The socialist ideals of the Republican People's Party favored workers and inefficient state enterprise as part of its clientalist relations, while the Islamist Welfare Party favored inner Anatolian businessmen against its cosmopolitan enemy, big Istanbul-based conglomerates. Thus, political ruling parties used state assets and policy making as tools to deliver goods to their favored clients. That is why the business community also failed to produce self-monitoring institutions, except the rather late attempt by MUSIAD in the 1990s.

(c) Gambling incorporated into social norms

The culture of gambling has been engraved in social and behavioral norms in Turkey as in many other economies where high risks are embedded in social and economic life and where there is legal opacity and pervasive corruption. This is why, despite periodic abuses, individuals still maintain their faith in investing with the mentality of a gambler. Acceptance of fuzzy legality means that individuals or even groups tend not to put pressure on the system to change or seek fair play since retaining both legality and illegality potentially offers more benefits through circumvention when necessary. Thus, when living on the margins of legality and illegality becomes an accepted social norm, individuals aim to maximize their interests by circumventing regulations and formal
contracts. The fuzzy legality of more than 70% of urban housing in Turkey is a day-to-day symbol of this way of living and thinking. Individuals learned that by circumventing and disrespecting zoning and planning regulation they maximized their gains. Punitive measures rarely come in force. Trusting connected individuals rather than abstract procedures and institutions is another aspect of gambling. Thus, as Anatolian holding companies illustrate, in the absence of respect for regulation and trust in institutions, the collective motives follow the path of conformity and “gambling of trust” (Luhmann, 1979). This explains why investors, who all hoped to be free-riders, did not put pressure on the system toward creating viable institutions and regulatory regimes. Yet, paradoxically many individuals acknowledge the unfair nature of law enforcement and unequal treatment in the society. Nevertheless, the public desire for fairness is often overcome by individual habits of circumvention and risky gambling under the protection of political clientalism.

6. CONCLUSION AND POLICY RECOMMENDATION

Our paper illustrates that in the 1990s norms and internalized moral values of Islam created initial trust among investors just as the ideological appeal of socialism lured their counterparts in the 1970s. But this trust needed to be secured for sustainable business success within an impersonal capital regime and its institutions. The first wave of Anatolian holding companies illustrates how regulation failed to promote impersonal trust and the second shows how societal obligations and moral grounds fell far short of the guarantees necessary for the survival of these companies in the absence of responsible institutions. In consequence, the damage of this demise has not only been financial but moral also.

Why then were the lessons of the special foreign exchange deposits and later banker scandals not used to prevent similar disasters in the 1970s and the 1990s? Why did Turkish governments persistently fail to develop a viable finance regime? As we have illustrated, principal agent theory and institutional and regulatory perspectives fail to help us to understand this aberrant economic behavior. We identified three reasons for this failure to develop viable capital market reform and regulatory institutions in Turkey: populist–clientalist political culture; lax oversight in the party system of single leader tutelage; and the mentality of gambling. Consequently, widespread abuses and the mismanagement of politicians, law enforcement agencies, and managers led to the final failure of alternative capital formations.

These findings hold implications for many developing economies and emerging democracies in which there are similar abuses and lack of credible law enforcement and institutional regimes to govern economic development beyond narrow group interests and patronage relations. The vicious circle of this self-destructive relationship between social norms and politics embedded in economic transactions hinder economic development and social justice in many developing countries. Protecting and nurturing narrow group interests through populist policies inhibit the scope of businesses and wealth creation as well as impersonal trust in the economy. In such environments where policy formation is entrenched and fuzzy legality is embedded in social and behavioral norms, how can a change emerge for the better? This vicious circle can best be broken by conscious policy efforts that will also nurture a collective understanding of the need to create and implement common rules of the game. But this will not emerge easily when such behaviors are deeply embedded in social and economic life. Catastrophes and external forces are another source of change.

Turkey has reached the turning point where the old system has become a major liability, as revealed by responses to the recent chain of disasters and external forces. The 1999 Istanbul earthquake unveiled the catastrophe of semi-legality as badly constructed housing areas were flattened, contributing to the tragedy of over 20,000 deaths. Those individuals who dodged building regulations, officials who learned to ignore illegality, and politicians who made “legalizing illegality” as part of their populist–clientalist politics have all paid the price. The second disaster was the worst economic crisis in Turkey’s modern history when in 2001 thousands of businesses closed down and the whole banking regime collapsed. These catastrophes deeply affected public sentiment as everybody who had benefited from the lapses of legality and opportunism suddenly became net losers.

External change factors came with the International Monetary Fund whose financial
loan linked to economic and financial reforms became crucial for Turkey’s economic recovery and for the EU membership requirements. Turkish voters threw out all long-established parties and their leaders as none managed to enter the parliament in the November 2002 elections. The two-party parliament, and the government, led by the reformed Islamist party, declared EU membership as the main goal of Turkey and their leader, Tayyip Erdoğan, declared an end to the populist and clientalist political regime. It is too early to make a conclusive statement whether this will bring deep cultural and behavioral changes to the business community, or even to politics. But there is more hope than ever and many reforms are already being pushed forward. In this favorable climate there is the possibility of reinvigoration of Anatolian holding companies as well. Before that happens, policy reforms should include the following.

The bank-centered finance model has failed to initiate industrial growth and the diffusion of economic activities to localities in Turkey. Despite its relative success, the Anglo-Saxon open market model is also not appropriate for long-term investments and geographically diffused industrialization in developing countries such as Turkey. A more regionally decentralized micro venture system set between bank-centered and stock market-led models, such as the Anatolian holding companies, can be a reliable alternative for entrepreneurial development and, especially, for diffusing industrialization. Encouraging local development through savings schemes such as Anatolian holding companies is also crucial to unleash local resources for development where industrial capital mobility is minimal and disparity among regions immense. It can also promote small and medium-sized firms. This model, however, ought to be structured along solid legal and institutional definitions and guarantees.

First and foremost, however, Turkey needs a new company law regime and capital markets regulation which will recognize these new formations and define property rights, especially of small investors. Such regulation needs to provide a legal base for bond-like “papers” issued by the holdings and should also restrain entrepreneurs from malpractice. This will increase the reliability of company records. Furthermore, intermediate institutions that would reduce informational asymmetry between the managers and investors should be established. Independent regulatory and professional bodies should also be allowed to investigate the operation of the companies and their reports ought to be made public. The companies should be obliged to make their auditing reports and company information available to the public. An independent shareholders association can also monitor company performance on behalf of the intermediary institutions. Intermediate institutions can also provide a stock exchange where stocks are traded in local and regional economies.

These reforms however will only be successful if the regulation and institution-building process creates institutional credibility and impersonal trust in the market for the emergence of wider and more complex relations. A high degree of political endorsement and administrative determination are crucial components of this law-making and enforcement. Social norms will evolve along new institutional structures and incentives in due course if punitive measures are in place for abusers and if the further advantage of increasing market growth can be demonstrated to a wider set of societal forces.

NOTES

1. The terminology used in the 1970s referred to worker’s companies (İşçi Şirketleri), worker’s investment companies (İşçi Yatırım Şirketleri), townsmen companies (Hemsıryat Şirketleri) and people’s companies (Halk Şirketleri) according to the form of initiation. In this article we call multiship ownership companies “Anatolian holding companies” to refer to holding companies with over 100 shareholders, as defined by Turkey’s State Planning Organization.

Anatolia is the land mass of Turkey excluding Thrace (Trakya), the European part of the country. The term is also commonly used to refer to the heartland, motherland and soul of indigenous Turkey. Today the term “Anatolia” has also been used in many contested cultural, historical and religious connotations and symbols ranging from the mother queens of the Hittites to Ottoman Turkish Islamic culture.

2. There has been a growing number of works concentrating on issues related to the separation of ownership and control in the process of establishing
capitalist enterprises through privatization and restructuring in transition economies. See Frydman et al. (1996), Kogut and Spicer (2002), and Shleifer and Vasilev (1996).

3. Before the recent revival of Keynesianism in the wake of the US-led global economic crisis, many believed that open market capitalism is taking over insider-controlled corporate regimes. In Europe, the successful bid of Vodafone, a telecommunication company, over Mannesmann has become the recent symbol of this wave. This conversion now seems to be unlikely for the foreseeable future (see Economist, 2000, February 12).

4. For example, the World Bank has recently begun looking at corporate governance and regulatory regimes as part of its development and poverty reduction programs. The need for a common regulatory regime for liberal economic integration has intensified the European Union’s search for a common policy ground for company law and corporate governance. Lannoo (1999) identifies four trends in European corporate governance which require new institutional and regulatory frameworks at the supranational policy level: these are the growing role of institutional investors, integration of capital markets, shareholder activism and the privatization of state assets.

5. The assumption is that the stock price of a firm managed poorly will fall and the firm will become open to potential takeovers. After the takeover, new owners will fire the incumbent managers who are responsible for the bad performance. Second, if a firm is financed by bonds or loans, poorly performing firms will have difficulties in raising additional capital and finally face bankruptcy. The threat of losing their jobs either after a takeover or bankruptcy will stimulate managers to better managerial performance.

6. Micheal Lewis devotes a long article in the New York Times Magazine (27 October 2002) defending the market boom and corporate strategies that aimed to deceive investors. He even goes as far as defending the recent stock market scandals as part of a bigger economic picture in which only transfers from one person to another occurred.

7. Gearing ratio (total liabilities/total assets) is another indication of this bank-centered corporate governance in Turkey: Japan (0.62), USA (0.28) and Turkey (0.64).

8. These transferable foreign currency accounts are known as DCM [Döviz Çevirebilir Metodu].

9. During the mid to late 1980s, the ÖZal government issued many investment bonds while special government account schemes mushroomed with little coordination and accountability. With the build-run-transfer schemes, the range of government bonds was extended into new sectors. For example, in 1987 the government issued promissory notes of revenue share called GAP-A valid for six years and allocated a proportion of the revenues of the Keban Dam in South-eastern Turkey for this purpose (Üçer, 1996).

10. Cevher Özden, known as banker Kastelli, was the biggest and most popular banker who managed to cultivate a popular and respectable image through his charitable activities and extensive advertizing. Mr. Özden traded savings bonds issued by the governments prior to 1970 and lost his business after the abolition of this trade by the government. But he returned to money trading using a "ponzi method." With over 200,000 customers, he traded the bonds at high interest rates and became much bigger than many established banks. Constant fresh capital in his "ponzi model" enriched him and his customers until the total loss of credibility and frantic panic in the market in 1982. Following the collapse of market bankers, Kastelli fled abroad and was arrested in Tunisia in 1982. But after serving only a seven months prison sentence, he was released (Günlük, 1983; Yıldırım, 1998). Despite these scandals Kastelli later initiated a housing construction business and even managed to collect funds from individual investors.

11. The daily newspapers during this period were full of stories about the market bankers, their past glory and current disgraceful state. Several bankers committed suicide, some were murdered and many were physically attacked by investors who had lost their life savings. Many families were impoverished, broke up, and suffered psychological stress. The homicide rates increased. Many small and medium-sized businesses that used market bankers also went bankrupt.

12. According to this study covering the period during 1968–2001, the ratio of the informal shadow economy to GDP per capita realized on average 45%. But while this rate was around 36% during 1968–90, with the deepening economic crises the gap jumped to 59% during 1990–2001 (Hürriyet, 2002, 7 January).

13. Van Renselaar and Van Velzen (1975) indicate that in mid-1970s Turkish migrants had DM 5 billion marks placed in German banks, or DM 6 billion including accounts in other European countries (p. 103).

14. Some private firms did attempt to sell shares to small investors abroad. But migrants showed little
enthusiasm for these initiatives (Van Renselaar & Van Velzen, 1975, p. 136). Such companies typically were under the control of founder families with whom the migrants had no association or familiarity.

15. According to time series data from the Turkish Central Bank, 1 US dollar was equal to about 13.8 Turkish lira in 1975. With the massive depreciation of Turkish lira over the years, this amount jumped to circa 1.6 million Turkish lira per 1 US dollar.

16. Our interviews with technocrats and company managers who were involved in the Anatolian holdings in the 1970s also confirmed the widespread managerial abuses and incompetence alongside liquidity problems. Some of these agents were later involved in the second wave of Anatolian holding companies in the 1990s as middle rank managers.

17. For example in one such worker’s company, Yibitas, the managers share rose from 3% to 50% in the initial stage of establishment (Cumhuriyet, 1981, 2 October).

18. Açikel (1996) eloquently explains the socio-psychological dimensions of political and ideological changes in the history of the Republic with what he calls the Turkish–Islamic synthesis.

19. Çakır (1995) gives an elaborate account of Islamic groups and their intensified political and economic presence in Turkey during the 1980s and early 1990s. A notable organization, the Iskender Pasha School, has led a significant intellectual debate on Islam and industrialization through its thinkers and associated young graduates since the 1950s. Interestingly, among these graduates there have been high-ranking civil servants and politicians who occupied influential positions in government institutions and politics.

20. Mohammad Iqbal (1876–1938), Indian poet and philosopher, first played with the idea of Islamic economics as part of his search for Islamic reassertion but failed to develop a clear perspective on the issue. Other Islamic thinkers and even the pan-Islamists showed little interest in economics and offered no clear perspectives on Islamic economics until Mawdudi. As Kuran (1997a, 1997b) shows, the roots of intellectual development on Islamic economics goes back to the cultural concerns of Muslim identity in India before the partition of Pakistan led by Indian Muslim thinker, Sayyid Abu'l-Al'la Mawdudi (1903–79).

21. No one has promoted this image more than Mr. H. Bayram, the CEO of Kombassan, a Konya-based holding company. As a chief manager of over 40 companies, Mr. Bayram exemplifies the humble image of a preacher as well as an entrepreneur. Our interviews with Mr. Bayram and his associates in Konya highlighted their commitment to the industrialization of the inner Anatolian region, a region he saw as an arid land waiting for water.

22. Our informants confirmed that most of the money collected from Turks in Germany was brought into Turkey literally in suitcases, also in the form of gold jewels (see also the Special Report on Islamic Finance & Businesses, 1999).

23. Fettullahçi, Nakşibendi and Süleymançısı orders had their own business and finance groups both in Turkey and Germany. According to the study of the Turkey Research Center, Asya Finance supported many businesses that favored the moderate Fetullah Gülen group known as Fettullahçi while İhlas finance had ties with the Nakşibendi order and supported businesses associated with this group (Special Report on Islamic Finance & Businesses, 1999).

24. Their legality is related to their status as companies with various official permissions. In particular, they have been successful in obtaining investment incentives and tax rebates under the provision of priority development areas, which includes many inner Anatolian towns. They are also in serious breach of guidelines of the Capital Markets Board. The CMB does not recognize the shares and bonds issued by these companies. Certain companies have also been periodically accused of being anti-secular and fundamentalist by the military and nongovernmental organizations (NGOs) that promote secularism and Kemalism.

25. One of our interviewees, who had been the chief manager of one of the biggest companies at Kombassan, has revealed his shock at the degree of ignorance and incompetence in investment decisions. He argued that he could not cope with poor business understanding of top managers and entrepreneurs, most of whom never had any professional managerial experience prior to their positions at Kombassan.

26. Politics have been employed in order to protect and/or increase the financial gains. Fadıl Akgündüz, the founder of Jep-pa, managed to get elected from the town of Siirt to the Turkish Parliament in November 2002 in order to gain parliamentary immunity and cover up his scandals. The elections were cancelled, however, his immunity was lifted and he is on trial. Similarly, the
recent scandal of Kimpa ş shows that a former MP, as a member of the governing board, was involved in the wrongdoings of the company (Hürriyet, 2003, 1 April).

27. The Dutch and German governments were involved at various stages of this initiative as they were interested in return migration of Turkish workers to their home regions. In addition to Anatolian holding companies, many village development co-operatives were also established with the support of the German government (see Van Renselaar & Van Velzen, 1975). One can also see the obvious business opportunities recognized by Germany as many intermediate goods and much machinery were imported from there. A similar trade pattern, without German government involvement, repeated itself in the 1990s when many Anatolian holding companies used their channels of communication to obtain machinery and supplies from Germany.

28. Our forthcoming article entitled “Trust and market exchange: the case of Islamic companies” addresses these issues.

29. Bilgen and Özcan (1988) demonstrate how this fuzzy nature of ownership and control rights in urban planning became entrenched between opportunism and populism.

30. See Alexander (2002) for an interesting analysis of the notion of the “personal” state in Turkey.

31. This is being written during the invasion of Iraq and although it is difficult to foretell the full implications of this war on Turkey, it might inflict further economic problems and political instability in the region.

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