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The developmental state and economic policy in Turkey

ALI H BAYAR

Most states of the Third World have shared a vision of where they would like to go, of how they hope their countries will appear in the future. The problem is getting there. What strategy should be employed? And who will implement it? Answers to these two questions are not straightforward. The interaction of state policy and the process of economic development is a complex one. Even if we can find several features common to different countries, there is no universal and ahistoric model. The road each country takes is shaped by numerous factors specific to it. The choice and the sequences of the strategy are always constrained by available resources, the relative gains and losses that will be incurred by different classes and ideological factions, by the structures and social forces inherited from the past, by the country's regional and international position, interests and allies. We should also mention international markets and financial flows, whose importance has been dramatically growing in the recent past. Finally, the state cannot implement all elements of a policy. It must rely on some other forces and agencies: domestic capitalist sector or foreign capital, for example. The choice of the development strategy is then constrained by the strengths and weaknesses of these (partially) external forces available to implement it.

The autonomy of the state in developing countries with respect to domestic social classes and its sovereignty with respect to core developed countries and to international markets is also an open question. In some cases or stages of development, the state may be powerful and autonomous enough to choose the forces (agencies) to rely upon to implement its policies. But in some other cases or phases, forces (domestic or foreign) may impose themselves upon the state. A given development strategy may also set into motion a process that virtually creates new powerful class actors who finally dominate the state. The increasing strength of the Turkish bourgeoisie, emerging out of the decades of statist policies, is an excellent illustration of this phenomenon.

Turkey also provides a good case to examine the points mentioned above. The developmental state experience is three quarters of a century long in this country. It is therefore possible to analyse the role of the state as an architect of structural transformation and its changing position in different stages of development.[1] The point of departure of the paper will be the emergence of the national state and the Turkish paradigm. Part three will be devoted to the 1950s, a period of rapidly

Ali H Bayar is at the Université Libre de Bruxelles, Avenue F D Roosevelt, 50 CP 135, B-1050 Brussels, Belgium

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expanding capitalism. Part four will analyse the planning and import substitution policies in the 1960s and 1970s.

Parts five and six are devoted to the radical changes of the 1980s. The year 1980 was indeed a turning point in the political economy of Turkey. It marked the beginning of an attempt to shift the economy away from the course set at the founding of the republic in 1923. The military regime installed by the *coup d'état* of September 1980 introduced a fundamental reform programme of economic liberalisation in order to shift the economy's centre of gravity from the public to the private sector, giving greater freedom to the market. The economic and political reforms introduced in the 1980s have contributed to major economic, political and social transformations which have also led the country to greater instability and uncertainties in the 1990s.

2. The Period 1923–1950: from laissez-faire to statism

The new Turkish Republic, which emerged from World War I in 1923, was a one-party state. The Republican People's Party (CHP) ruled for almost 30 years. It was composed of an alliance between a secular, modernising, statist elite (the military and the bureaucracy) on one hand, and the traditional, conservative and provincial local notables on the other. During the first years of the Republic, the Kemalist regime was primarily preoccupied by political and cultural reforms in order to consolidate its newly born revolutionary power and to make Turkey a modern Western country. Education was secularised, Islamic legal codes were replaced by Western codes, the Latin alphabet was adopted in place of the Arabic one, etc.

Issues of political economy played a minor role in the first years of the Republic. As Keyder points out, the Turkish state of the twenties was exemplary in its non-interventionist stance.[1a] One reason was that various provisions of the Lausanne Treaty constrained the ability of the government to formulate an economic development strategy. Although the Republic was exempted from payment of war reparations, it was nonetheless held responsible for the large commercial debt of the Ottoman Empire. Turkey was also forced to maintain the Ottoman tariff schedule until 1929. These concessions undermined the government's ability to adopt trade policies in line with the needs of the country.

In the 1920s, the Republic's initial strategy was to rely on private-sector initiative and to avoid taxing the peasantry in order to finance industrial growth. The 1924 constitution declared private property and free enterprise to be the basic principles of the state. Atatürk emphasised that national sovereignty had to be rooted in economic independence, and that an industrial base was vital for it. But the national private sector was unable to undertake such a big resource mobilisation. It was too weak financially, too close to a commercial, rather than an industrial sector, and too concerned with short-term profit to be the agent of structural transformation. On the other hand, there was no foundation on which to build an ambitious economic programme. The decline of the Ottoman Empire and the war had left the economy in deep disorder. The infrastructure was devastated. Railways, most banks and industrial firms were owned by foreigners. The country lacked national entrepreneurs and technicians. The Ottoman Empire, with its strong central state apparatus had discouraged capitalist development.[2] Because of its Ottoman past, Turkey had the privilege of never having been colonised. Nevertheless, this privilege came with neither highly developed industries, a significant capital accumulation, nor with a well developed infrastructure. Given this context, the new Turkish state had little alternative but to assume the primary responsibility for capital accumulation.

The Great Depression of 1929 and the expiration of the restrictions of the Lausanne Treaty altered the government's early liberal approach to the economy. With the sharp decline in the price of agricultural commodities, Turkey's main source of foreign exchange collapsed. The Great Depression came to be regarded as evidence of the failure of the laissez faire system, a failure which the USSR had escaped thanks to state controls. Thus, mainly for pragmatic reasons, the government began to assume direct responsibility for economic development. In addition to its regulatory role, the state began assuming the task of producing goods. This was the promulgation of statism.

The authoritarian one-party state was particularly well suited to statism. Nevertheless, a short and limited experiment with multiparty democracy in 1930 followed the introduction of the statist policies. The emergence of the Free Party, which vigorously defended liberal economic policies opposed to the Republicans' interventionist approach, intensified the political struggle and debate. The Free Party was banned five months after its foundation. The conclusion reached by the Republicans was that the way out of the depression was through autarchy and rapid industrial development and that there was no room for political contest on this road.

The statist approach found expression in Turkey's first five-year plan, drawn up in 1933. The plan provided for the establishment of a number of state-owned economic enterprises (SEEs) in iron and steel, textiles, paper, ceramics, glass, and chemical products. Two state-owned banks (Sümerbank and Etibank) were set up to provide finance for public enterprises. Both banks soon became holding companies with large responsibilities in the public enterprises.

The second five-year plan was adopted in September 1938, just before Atatürk's death. Over 100 new enterprises were planned. The first efforts at industrial deepening were projected. The Zonguldak-Karabük region was slated to become a heavy-industrial-growth pole, built around coal, steel and cement, and serviced by its own Black Sea port. A major effort was to be made in power generation, basic chemicals, engineering, and marine transport. Part of the plan was to disperse industry in order to benefit backward areas, especially Eastern Anatolia, as well as for strategic reasons. World War II interrupted the second five-year plan, and a period of severe privation ensued. The government introduced strict controls on the private sector.

This 'big push' strategy of the 1930s had some inevitable effects. The government ran a growing deficit, the result not only of public investments, but also of an oversized bureaucracy. The civil service, not including military personnel, numbered 127 000 employees in 1938 and 184 000 in 1945. About 35% of the budget went into their salaries.

Statism helped to fuse the ruling party and the state, but it was far from being a cohesive ideology. Two different interpretations of the notion were continuously debated within the ruling party.[3] The hard-liners, organised around the monthly review *Kadro*, argued that, since the Turkish Revolution was not a class-based movement, the outcome ought to be different from socialism and capitalism. The emerging new system would have little or no class conflict. Statism was the means to achieve such a harmonious arrangement. They argued that the state should involve itself in all aspects of the society. The moderates, led by Celal Bayar (who became President of the Republic between 1950 and 1960), interpreted statism as a transitory phase designed to supplement and strengthen the industrial structure in which the state's endeavours would later be supplanted by the private sector. Atatürk was rather ambiguous. However, he sided with the moderate group on several occasions, especially by appointing Bayar to the Ministry of Finance in 1932 and later to the Prime Ministership.

The application of statism was *ad hoc*, concentrating solely on the creation of an industrial base. Agriculture was totally excluded. In a country where 80% of the population was involved in agriculture, this narrow statist focus was, from both political and economic perspectives, an error. Later the Republicans would pay the price for their neglect of agriculture.

After Atatürk's death in 1938, the hierarchy of the Republican People's Party was more and more unable to manage its internal divisions. After World War II, Ismet Inönü allowed the formation of other political parties. The newly founded Democratic Party championed the cause of free enterprise and won about a seventh of the votes in the 1946 general elections. Four years later the Democratic Party won a parliamentary majority and came to power.

3. The 1950s: expanding capitalism

The initial years of Democratic Party rule were characterised by high growth rates. GDP growth exceeded 10% per annum for the first three years of the new government. As promised, the Democratic Party government emphasised the development of agriculture, which grew at an annual rate of 11.5% from 1950 to 1953. Taxes on agriculture were eliminated, an ambitious mechanisation programme was started and an extensive road building programme was undertaken with the help of US aid. The country's infrastructure grew rapidly, with real public investment expanding at an annual rate of 30% from 1950 to 1953. By integrating the villages with the major urban centres, the road programme enabled the peasantry to market their produce. The commercialisation of agriculture developed especially in Western Turkey.

The Democrats lacked a consistent policy and expected the economy to develop once the private sector had been freed from the confines of statism. Although the private sector did demonstrate an unprecedented flurry of activity, the result expected by the new government did not materialise and the Democrats had to increasingly rely on the SEEs to make up for the lack of private investment. On the other hand the Democrats used the SEE outlay as a means of halting any erosion in their electoral base. This policy increased inefficiencies in public sector activity. Expansive policies and the political use of SEEs led to high fiscal deficits which were covered to a large extent by Central Bank credit. After 1953 inflation accelerated as a result of excessive growth in the money supply.

By 1958 the economy plunged into a crisis so serious that Turkey was unable to borrow any funds from abroad. In August 1958 the government adopted a stabilisation programme which included a *de facto* devaluation, liberalisation of the import regime, increases in SEE prices, restraint on government expenditures and a ceiling on Central Bank credit.

When the austerity programme was introduced, support for the Democrats' government was already crumbling because of high inflation, shortages and increasing repression of political opposition. Political unrest continued to expand after the stabilisation programme was introduced. A group of military leaders took power on 27 May 1960 in order to restore political stability and complete the stabilisation programme that the government was preparing to abandon in the hope of winning political support.

4. The 1960s and 1970s: planning and import substitution

Like the 1950s, the 1960s began with a determination to correct the mistakes of the previous regime. In the 1950s, the aim had been to give greater scope to the private sector in agriculture and industry. In the 1960s, the aim was to accelerate economic development by import substitution and central planning which inevitably reassessed the role of the state in the economy.

Until the 1960s, Turkey's experience with import substitution policies had been limited. By the end of the 1950s a strong coalition of interests emerged which believed that the solution to Turkey's chronic problems lay in industrialisation. A new class of industrial bourgeoisie had flourished during Democrat Party rule. Industrialists, the military and civilian bureaucrats became strong supporters of import substitution industrialisation (ISI) believing that it would reinforce their role and place in society.

The 1960 military coup symbolised a dramatic break with the past. ISI was institutionalised through central planning. The growth record was impressive under the first two five-year plans (1963–1967 and 1968–1972). During this period industry's share in GDP rose from 16.2% to 22.6%. Public investment and public consumption grew rapidly. The emphasis on heavy, capital-intensive industry increased the role of SEEs as well. But the increasing rate of investment by SEEs and the large salary increases granted by the government to buy political support caused a dramatic rise in SEE deficits which were financed by government transfers and external borrowing. This led to severe problems similar to those Turkey had had to face in the late 1950s. External debt became problematic, money supply grew rapidly because of the financing of government deficits, the currency became overvalued. The Turkish lira was devalued by 66% in 1970 but without any stabilisation programme. Political quarrels hampered the government's ability to deal seriously with the growing economic problems. In 1970 and 1971 political and social unrest amplified and erupted in violence. The military intervened on 12 March 1971, forcing Prime Minister Demirel to resign.

After the devaluation of 1970 exports increased dramatically in 1971 (15%) and 1972 (30%). The inflow of emigrant workers' remittances was also boosted. As a result, the current account produced a surplus in 1971 and 1972. The improvement of the balance of payments and the political stability imposed by the military intervention raised the confidence of foreign creditors, who resumed lending to Turkey on a massive scale. The foreign exchange flow concealed for a while the macro-economic imbalances and the underlying structural problems of the country. The third five-year plan period (1973–1977) was one of remarkable growth, especially in the industrial sector (14.2% per year). But with real GDP growth of 7% per year between 1973 and 1977, and investment growing at a rate of 13.8%, reliance on foreign borrowing grew substantially. This policy was not sustainable. The growth boom began to abort in 1977 as foreign lenders became worried about the size of Turkey's rapidly growing external debt.

During the 1973–1977 boom, the inflation rate averaged about 20% (four times the average rate in the 1960s). Inflation continued to accelerate even after the 1977 slowdown to hit 100% in 1980. Oil shocks and public sector deficits were the source of continuous inflation in the 1970s. Income inequality increased dramatically because of the sharp decline in real wages as inflation began to accelerate after 1977. Labour market developments were also highly problematic in the 1970s. Labour supply continued to increase but the European labour demand for Turkish immigrant workers declined sharply because of economic slowdown. As a consequence the number of unemployed grew by 5.4% per year between 1973 and 1977, and by 10.3% during the period 1977–1980. GDP growth rate declined to 0.3% per annum in the same period. Turkey thus entered into a period of heavy stagflation. Until 1980, however, the government was unable to implement an efficient stabilisation programme.

5. The 1980s: from import substitution to liberalisation

By the end of the 1970s it was clear that Turkey needed a new strategy. The Demirel government decided to implement a major long-term restructuring programme designed to dismantle the import substitution policy and to transform the inward-orientated political economy into an export-driven one. On 24 January 1980, the Demirel government announced the new programme which represented a radical departure from past policies and practices. The first measure to be announced on 24 January 1980 was a devaluation of the Turkish lira by almost 49% (from 47 TL per dollar to 70 TL per dollar). The devaluation was a first step into a 'crawling peg' nominal exchange-rate regime.[4] This was one of the major requirements of the stand-by agreement signed by the government with the IMF. Other measures included export incentives and the liberalisation of import regulations and foreign capital inflow. Price controls were abolished and the prices of SEE products were repeatedly increased in order to reduce public deficits. Interest rates were also freed.

As a result of tight monetary policy interest rates increased dramatically. The credit squeeze affected small and medium-sized enterprises deeply, as well as middle and low-income consumers. Depressed domestic demand and rising inventories increased pressure on the private sector to export, even when undergoing a loss.

Despite the initial support received by the government from most of the private sector and from foreign creditors for the 24 January programme, the

Demirel government was facing an impasse at the political level and was unable to survive long enough to implement the programme, which needed time and a strong rule. However, the 1970s were a period of great political instability in Turkey. Five elections were held, but no party achieved a majority. Power shifted back and forth five times between the two major political parties (Republican People's Party and Justice Party) which set up fragile coalitions with the neo-fascist National Action Party and/or the fundamentalist National Salvation Party. The result of political instability was something close to anarchy. About 5000 people were killed by acts of terrorism between 1977 and 1980. The acceleration of inflation in this period brought a dramatic increase in income inequality which contributed to civil disorder.[5] The Turkish population lost confidence in all the traditional parties. In addition to the political violence and the gloomy economic conditions, Parliament had been deadlocked since April 1980 over the election of a new President of the Republic to replace Korutürk, whose term had expired. The government had also been unable to push through the tax reform bill it needed to make up budget deficits. The parliamentary crisis hit a peak when the fundamentalist National Salvation Party, with the centre-left Republican People's Party, forced votes of no confidence on individual ministers of Demirel's minority government. The first to succumb was the Minister for Foreign Affairs. The military took power on 12 September 1980 before the next scheduled vote targeting the Finance Minister. The military junta dissolved the Parliament, exiled or arrested the party leaders and forbade all civilian political activity. Thousands of left-wing activists were arrested and tortured. The generals, allied to civilian technocrats, muzzled the labour unions and the universities with the usual violence, cut social outlays, and pushed through an export-led growth strategy.

The year 1980 was the beginning of the radical transformation of Turkey's political economy from its ISI orientation to a more open system. Reform of the trade regime was the core of the programme.[6] The first element of the reform was the devaluation of the TL and a commitment to a flexible exchange rate policy. The second element was the promotion of exports through tax rebates, export credits, and other subsidies. The third element of the trade reform was import liberalisation. The import regime was changed radically at the end of 1983 with the announcement that any item other than those specifically banned or subject to licensing could be imported freely. Quantitative restrictions were removed and tariffs were lowered from an average of 19% to 12%.

Devaluation of TL and trade reforms had a strong effect on Turkey's foreign trade. In 1981 the dollar value of exports rose by 62% and in 1982 by 25%.[7] In 1981 manufacturing exports doubled in dollar value. The following year they increased by a further 50%. The share of manufacturing exports in total exports rose to 80% in 1987 from 36% in 1980. The strong export performance enabled Turkey to expand its imports which grew by 15% per year between 1980 and 1985.[8]

One of the main problems in the late 1970s was inflation, which was boosted by the monetisation of public deficits. The new strategy aimed to deal with inflation in two ways. First, taxes were raised, public expenditures were reduced and SEE product prices were increased. A value-added tax was introduced in

1984. The second element was financial deregulation which began with the liberalisation of interest rates in order to encourage savings and reduce the velocity of money circulation. As a consequence of these policies, inflation fell to 36.6% in 1981 and to 32.8% in 1982.[9] However, rising public deficits in 1984 led to monetary expansion and to an increase in the inflation rate in the following years (48.3% in 1984 and 55% in 1987).

External debt also continued to grow after the military takeover. Even more alarming was the changing structure of the foreign debt, as short-term debt; which had been reduced from 25% of the total in 1979 to 10% in 1982, started to rise, reaching 23% in 1987. The over-dependence on short-term financing led to a crisis of confidence. Expectations of devaluation produced a large gap (20%) between the official exchange rate and the black market rate. By the end of 1987 a mini-crisis developed in the exchange market. The government initiated a restrictive monetary and fiscal policy to reduce both internal and external imbalances. The stabilisation programme succeeded in reducing the gap between the official and the unofficial exchange rates, but inflation could not be contained and it reached 70% in 1988.

Another failure of the military rule was the substantial increase in unemployment. Moreover, real wages continued to fall dramatically after the September 1980 military coup, considerably aggravating income inequalities.[10]

No significant progress was made towards privatisation. While the market began to play a greater role in allocating resources, government intervention remained omnipresent.

6. Restructuring the political system in the 1980s

The officers responsible for the 1980 *coup d''etat* had clearly intended their efforts to be long-lasting. If the post-1980 regime had all the trademarks of an authoritarian state, it was the intentional result of a complex process of social engineering. The military junta had an ambitious plan for restructuring the political institutions. The government and the parliament established in accordance with the 1961 constitution were dissolved and replaced by the National Security Council (NSC). The Council was made up of the Chief of the General Staff and the Commanders-in-Chief of the Army, Air Force, Navy and Gendarmerie. The Council assumed legislative and executive power. On 15 October 1981 the NSC appointed a 160-member Consultative Assembly. The day after, the military junta dissolved all political parties and confiscated their belongings.

The junta was particularly opposed to the previous 1961 liberal Constitution and the political structures it had engendered. The military leaders imposed a new constitution in 1982 and a new electoral system. They intended to create a more stable order less prone to polarisation. The bicameral parliament was replaced by a unicameral one. The powers of the President were considerably enhanced. The executive was seriously reinforced at the expense of the legislative and the judiciary. After the introduction of the new Constitution in November 1982, Kenan Evren, the Chief of Staff automatically became President of the Republic for seven years and the other members of the junta formed the Presidential Council, which functioned as an upper house.

The 1982 Constitution severely restricted individual freedoms. Freedom of the press was removed *de facto* from the constitution. Following the new constitution religion courses became compulsory in primary and secondary schools.[11] Universities lost their autonomy when the military leaders set up the Higher Educational Institution in order to centralise all decision making in Turkish universities.

New restrictions were also introduced on the activities of trade unions and associations. The new Constitution required unions to abstain from all political activity, prohibited them from supporting or receiving any support from political parties. As a supplementary measure of government control, unions were required to deposit their funds in state-owned banks. These restrictions, along with brutal military repression, curbed the unions' power in industrial relations and in public life. Professional organisations were also forbidden from supporting political parties or receiving support from them. In addition, they were put under the supervision of ministries and were required to maintain their headquarters in the capital, Ankara.

All these changes were intended to depoliticise society, reduce the influence of organised opposition, and increase the state's ability to monitor and control their activities.

After the adoption of the constitution in November 1982, the National Security Council took a second step to allow a gradual and controlled recovery of political activities by announcing on 24 April 1983 the law governing the formation of political parties. The dissolved party leaders were banned from political activity for 10 years and were also banned from expressing their opinions either orally or in writing. The law equally banned all former parliamentarians from any political responsibility for the following five years. The junta reserved the right to examine lists of the founders of the new political formations and to decide on eventual replacements for those who were considered unacceptable by the military. The NSC allowed itself the power to veto not only the founders and officials of new parties, but also their candidates for the coming elections.

Determined to stop the proliferation of small parties and the resulting instability, the military tried deliberately to create a two-party system. To ensure the emergence of a two-party system, electoral provisions were crafted to favour larger parties. A party was required to win at least 10% of the vote at the national level in order to get a representative elected. While 15 new parties were set up after the adoption of the new Political Parties Law, one of the parties (the Great Turkey Party supported by the former Prime Minister Demirel) was dissolved by a military decree and 11 others were denied the right to register for the polls as a result of the junta's vetoes. According to the new Election Law, to be allowed to register for the polls a political party was obliged to have at least 30 founders who were not vetoed by the NSC. The Junta vetoed 453 out of 750 party founders. As a result only three political parties were allowed to register for the polls: the Nationalist Democracy Party (MDP), headed by the retired army general Turgut Sunalp, the Motherland Party (ANAP), headed by the former Vice-Premier of the ruling military government, Turgut Özal and the Populist Party (HP) headed by the former under-secretary of the same government, Necdet Calp. All three parties shared similar views laid down by the military junta. But the generals did not trust even the candidates announced by these three parties and vetoed 89 HP candidates, 81 from ANAP and 74 from MDP.

The elections were held on 6 November 1983. The two parties directly inspired or organised by the military, HP and MDP, lost. ANAP obtained 45% of the votes and Turgut Özal, the former Vice-Premier of the military government, became the new Prime Minister. A civilian government was formed in December 1983, but the military junta continued to hold great influence through the Presidential Council.

7. The 1990s: increased instability and uncertainties

Macro-economic performance in Turkey in recent years has been characterised by strong, but uneven, growth and persistently high inflation. To stimulate growth, an expansionary fiscal stance was pursued by the ANAP government in the period leading to the 1987 elections. The immediate inflationary impact of the expansionary demand policies was limited, however, by the decline in oil prices and price restraints imposed on public enterprises. In 1988, cuts in public investment reduced the public sector borrowing requirement, but the fiscal tightening was not sustained. In spite of a sharp reduction in growth, following the adjustment of public prices after the elections, inflation accelerated to 70%. The 1989–1990 anti-inflationary strategy relied on a tightening of monetary policy, but the lack of fiscal adjustment resulted in only a short respite from inflation.

Economic performance in 1991 was influenced by three major events: the Gulf war, the mid-year change in Government and the October parliamentary elections. These events increased uncertainty, depressed economic activity and created instability in the foreign exchange and financial markets. Electoral considerations climbed to the top of the policy agenda and the fiscal deficit widened because of high increases in agricultural support prices and in public sector wages. The public deficit climbed to 17% of GDP and inflation rose to 70% for the year. The spillover of domestic imbalances into the external sector was cushioned by the slowdown in economic activity, which lowered the trade deficit, and substantial Gulf crisis-related grants that contributed to improving the current account. Led by an expansion in private consumption, which had its roots in the large wage increases granted in the second half of 1991, the economy rebounded in 1992, increasing by 6.4%. A record 28.7% increase in imports, along with a disappointing increase in exports of only 4.3% resulted in a rapid deterioration in the foreign balance. The recovery of investment was, however, mild, as uncertainty over the future course of economic policy persisted, and inflation remained unabated.

The GDP growth rate increased by no less than 7.3% in 1993. But further growth in the public deficit, accompanied by a loosening of monetary conditions, resulted in a surge in domestic demand and a sharp deterioration in the current account position.[12] Increasing recognition of the unsustainability of this policy stance, coupled with a sharp downgrading in Turkey's credit rating in international capital markets, contributed to an exchange market crisis in the first months of 1994, during which the Turkish lira depreciated by almost 60%.

On 5 April 1994, the government announced a new package of stabilisation measures and structural reforms. The strategy underlying the programme placed primary emphasis on fiscal adjustment, supported by structural reforms intended to scale back the role of the public sector in the economy. The performance of the Turkish economy under the adjustment programme has been mixed, in part reflecting uneven implementation of the reform package. Domestic demand declined by 12% during the year and real GDP declined by 6%. Prices rose at unprecedented rates during 1994, with wholesale and consumer prices increasing by 149% and 125%, respectively.

The inability to control inflation has been a striking characteristic of Turkey's economic performance in recent years. After a highly successful disinflation effort that brought the annual rate from a three-digit level in 1980 to about 30% in 1986, inflation again turned upwards.[13] The overall image is of unbalanced growth and uneven policy performance. Short-lived attempts to reduce inflation have resulted in fluctuations in growth. In the absence of measures targeted to correct its fundamental causes, inflation has remained stubbornly high. The lack of regular adjustments in public sector prices raised the variability of inflation and contributed to public deficits. Large administered price adjustments were followed by lengthy periods during which prices were kept constant until pressure built up for another round of price increases. The result was a high degree of relative price variability.

While demand and supply factors, such as oil shocks or volatility in agricultural harvests, have contributed to changes in the inflation rate, they do not account for the persistence of inflation. Because sustained inflation cannot persist without continued monetary expansion, the relevant question is, what are the causes of such expansion? There is a large body of evidence supporting the view that inflation in Turkey results from financing the requirements of the public sector. In this respect, inflation can be seen as the residual tax that fills the gap between government outlays and the resources obtained through taxes and domestic or external borrowing. The fiscal deficit is the main cause of sustained inflation,[14] but its immediate impact on prices depends on how it is financed. When fiscal expansion is financed by external borrowing, as in 1987, or domestic borrowing, as was the case in 1990, the inflationary impact is smaller than when money creation is a major source of financing.

8. Conclusion

Macro-economic policy in Turkey has not been aimed at the traditional targets of price stability and full employment. Instead, monetary and fiscal policies followed the goal of economic growth and industrialisation. Growth has been the first priority of every government in Turkey since the founding of the Republic in 1923. In pursuit of that goal, the government has assumed an important role in the economy as a provider of goods and services and as a manager of incentives to the private sector. In pursuit of these goals, however, public revenues have invariably fallen short of expenditure. The government has therefore been forced to borrow either from abroad or from the Central bank. The outcome has been economic and political crisis with rising inflation and an accumulation of external debt.

Economic crises have been the force for change in Turkey.[15] Import substitution was formally adopted in the early 1960s in response to the laissez faire policies of the 1950s which had culminated in economic crisis and military takeover. When this policy failed and the country confronted another economic and political crisis in the late 1970s, it was replaced by one which advocated free trade, flexible prices and privatisation. Since the military coup of September 1980 the government's participation in the economy has changed. Public investment has shifted from manufacturing towards infrastructural activities, especially in transportation, communications and energy. Neoliberal reforms were quite effective in diverting the existing capacity from import substituting industries to exports. However, as the Turkish experience since 1980 shows, export-orientated policies cannot sustain growth without a strategic plan designed to complement market-orientated reforms. This needs a broader long-term strategy of industrial restructuring.

Up to now Turkey has failed to achieve a stable multiparty system, and chronically suffers from a series of coalition governments whose component interests are so diverse that no coherent economic policy can be implemented in a sustainable way.[16] The capacity of ruling groups to impose their conception of national interest on everyone else has been weak. In Turkey, as in most developing countries, class consciousness has for a long time been amorphous and therefore class alignments have been fluid. Governments have possessed substantial decision-making autonomy, but have lacked the effective power to implement them. This imbalance is one of the key elements of Turkey's political economy. As a result of the instability of political coalitions, the time horizon of policy decisions has become increasingly short. This, in turn, amplifies the instability, deepens the crisis and prepares the field for new attempts of radical solutions, such as military takeovers or fundamentalist reactions.

Notes

1 For excellent detailed analyses see H J Bowkey, *The State and Industrialization Crisis in Turkey*, Boulder, Westview Press, 1990; Z Onis and J R Riedel, *Economic Crises and Long-Term Growth in Turkey*, Washington DC; The World Bank, 1993; A Richards and J Waterbury, *A Political Economy of the Middle East*, Boulder, Westview Press, 1990.

1a C Keyder, *The Definition of a Peripheral Economy: Turkey 1923–1929*, Cambridge: Cambridge University Press, 1981.

2 D Avcioglu, *Türkiye 'nin Düzeni*, Istanbul: Tekin Yayinevi, 1987; I Cem, *Türkiye 'de Geri Kalmisligin Tarihi*, Istanbul: Cem Yayinevi, 1989; B Lewis, *The Emergence of Modern Turkey*, Oxford: Oxford University Press, 1979; and S Yerasimos, *Azgelismislik Sürecinde Türkiye*, Istanbul: Belge Yayinlari 1989.

3 These two approaches can be related to the two types of state intervention and capital accumulation distinguished by Fitzgerald for Latin America. (E V K Fitzgerald *et al*, eds, *The State and Economic Development in Latin America*, Cambridge: Cambridge University Press, 1977); see also A Richards and J Waterbury, *A Political Economy of the Middle East*, Boulder, Westview Press, 1990. Both aim at structural transformation of the economy. They are not mutually exclusive and, as the Turkish case has shown, may oscillate over time. The first is a process whereby the state helps nurture or strengthen a private

sector. In this process of accumulation, the state transfers surpluses on its own operations to the private sector.

The second process of accumulation is one in which the state undertakes the resource mobilisation and infrastructure development functions, but also captures the surplus of its own activities, of a substantial portion of private sector profits and external rents in order to finance its own expansion. Here, the goal of the state is to dominate all aspects of resource allocation and to seize the commanding heights of the economy Turkey in the 1930s flirted with this strategy.

4 Between 1979 and 1986 the Turkish lira fell by 2000% against the US dollar in nominal terms.

5 M Celasun, 'Income distribution and domestic terms of trade in Turkey 1978–1983', *METU Studies in Development*, Vol 13, Nos 1,2, 1986, pp 29–94.

6 For details of the new trade policy, see S Togan, *Foreign Trade Regime and Trade Liberalization in Turkey During the 1980s*, Aldershot: Avebury, 1994.

7 The Iran–Iraq war played a major role in this boom. Nonetheless, exports to OECD countries grew also rapidly in the same period.

8 For analyses of the impact of trade liberalisation on imports see A Bayar, P M C de Boer, B Hobijn, C Martinez & T Pamukcu, 'Trade liberalisation and imports of manufactures in Turkey', paper presented at the Econometric Society European Meeting, Istanbul, August 1996.

9 110.2% in 1980.

10 Boratav, O Türel & E Yeldan, 'The Turkish economy in 1981–92: a balance sheet, problems and prospects', *METU Studies in Development*, Vol 22, No 1, 1995, pp 1–36.

11 In spite of their Kemalist and secular discourse, the military leaders promoted religion as a means of fighting left-wing ideas and movements. But this short-sighted policy favoured anti-secular movements. The Islamist Welfare Party became the largest party in parliament after the general elections of December 1995 and its president, Necmettin Erbakan became Prime Minister in the new coalition government in July 1996.

12 The foreign trade deficit established a record total of US$14 billion in 1993, an increase of 73% over that of 1992.

13 The inflation rate is expected to exceed 80% in 1996.

14 The huge cost of the war against the Kurdish guerrillas has been one of the main reasons for ongoing deficits.

15 Z Onis & J Riedel, *Economic Crises and Long-Term Growth in Turkey*, Washington, DC: The World Bank, 1993.

16 The new coalition formed in July 1996 by the Islamist Welfare Party of Necmettin Erbakan and the True Path Party of Tansu Ciller is the most recent example.