11

Neoliberal Policies and Globalization

THE GLOBAL RECESSION THAT FOLLOWED the OPEC-led increase in oil prices in 1973 brought about the end not only of a long period of expansion but also of Keynesian-style macroeconomic management and welfare state policies in the developed countries. The shift to neoliberal policies around the world began in the 1970s as the Bretton Woods system was disintegrating and the developed economies on both sides of the Atlantic Ocean were searching for policies to deal with the combination of stagnation and inflation. The Thatcher government in the United Kingdom and the Reagan administration in the United States led the movement toward greater emphasis on markets in both macro- and microeconomic policy. The new policies began to reduce the barriers in the way of trade and even more importantly the controls on international capital flows. These changes ushered in a new era known as the second wave of globalization after the first wave during the century before World War I (Rodrik 2011, pp. 89–206; Eichengreen 2008, pp. 134–227).

The large trade surpluses of the oil-exporting countries created new liquidity and lower interest rates in the international markets during the 1970s. Rather than slow down their economies in response to the increase in oil prices, many developing countries attempted to take advantage of the new liquidity and borrowed large amounts in order to extend the ISI-related boom. This strategy could not be sustained for long, however. The rapid escalation of the outstanding debt and growing difficulties of servicing and repayment in many developing countries gave the IMF and the World Bank renewed power to bring about long-term structural changes in these economies and their linkages with the world economy (Haggard and Kaufman 1992, pp. 3–37).

While obstacles to international capital movements were removed in many countries, both developed and developing, the obstacles in the way of international labor movements remained in place. At the same time, legal and technological changes weakened the labor unions and more generally the bargaining capacity of labor in many countries. As a result, the benefits of economic

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growth in the new era were distributed unequally between capital and labor. In addition, the growing volume of international capital movements introduced a new source of instability, not only to national economies, but for the entire global economy as well. The Asian crisis at the end of the 1990s created difficulties for many developing countries and demonstrated the risks associated with financial globalization. The global economic crisis that began in 2008 led to a sharp decline in output followed by slow recovery in the developed countries. GDP per capita levels for the developed countries as a whole were lower in 2015 than they were in 2007. The impact of the crisis on developing countries was more limited, however.

Turkey's encounter with neoliberal policies and globalization began with the new policy package launched in January 1980 in response to the severe economic crisis at the end of the 1970s. But the initial changes in formal policies and institutions were only part of the story. The distribution of benefits from the enforcement of the new policies and institutions was not always in line with the distribution of power and changing politics. The new policies and institutions interacted with existing institutions, the changing distribution of power, as well as domestic politics, and changed over time. The end result was rather different than what the original policies and institutions were supposed to achieve. Of the new policies, trade liberalization, the emphasis on exports, and lifting of restrictions on international capital flows remained mostly intact. Perhaps the most important area where major differences emerged between what the new economic policies intended in theory and what actually happened in practice concerned the role of the state in the economy. The market-oriented economic policies were supposed to reduce the interventionism of the state in the economy. More than three decades later, the role of the state in the economy remained strong. While some important changes occurred in the relationship between the state and the private sector, the government continued to have power and discretion to decide the winners in the new era.

This chapter and the next will examine the era since 1980 in terms of four subperiods (table 11.1). This chapter will begin with global and national political developments and examine how they led to changes in economic policies and institutions in Turkey as well as the consequences of these changes. The next chapter will review Turkey's record in economic growth, income distribution, and human development in both absolute and relative terms. It will also evaluate the role of institutions and institutional change in economic development since 1980.

In the first subperiod, which covers 1980–87, the new economic policies aimed to replace the interventionist and inward-oriented model that prevailed since the 1930s with one that relied more on markets and was more open to

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TABLE 11.1. A Periodization of Economic Trends, 1980–2015

Subperiod	Average Annual Growth Rates					Level of GDP per Capita at the End of Subperiod
	Population	GDP	Agriculture	Manufacturing	GDP per capita	1980 = 100
1980–1987	2.4	5.6	0.7	8.7	3.1	124
1988–2002	1.7	3.2	1.4	4.0	1.5	155
2003–2007	1.4	6.9	0.4	8.1	5.4	202
2008–2015	1.4	3.3	2.5	2.8	1.9	234
1980–2015	1.6	4.1	1.1	5.6	2.5	234

Source: Author's calculations based on the official national income series in Turkey, Türkiye İstatistik Kurumu (Turkish Statistical Institute), 2014.

international trade and capital flows. With the help of the military regime, which reduced wages and agricultural incomes, significant increases were achieved in exports of manufactures during this period. The achievements of the new policies in other areas were limited, however. The second subperiod, 1987–2001, was characterized by a great deal of political and economic instability. The repression of domestic politics during the military regime had led to fragmentation on both the right and left of the political spectrum. As a result, the 1990s witnessed rivalries between large numbers of parties and series of short-lived coalitions. One important outcome of political instability was the loss of fiscal discipline and the sharp rise in budget deficits, leading to very high rates of monetary expansion and inflation as well as high levels of public borrowing and debt accumulation. Macroeconomic instabilities were exacerbated by the decision to fully liberalize the capital account in 1989. As a result, large fiscal deficits combined with financial globalization resulted in stop-go cycles of international capital flows for more than a decade.

Turkey's experience with neoliberal policies entered a new phase with the economic program of 2001 and the rise to power of the Justice and Development Party (JDP) the following year. The new program prepared in the aftermath of a severe economic crisis differed from earlier programs reflecting the Washington Consensus. It explicitly recognized the role played by institutions and independent regulating agencies and was supported by a series of reforms and new legislation. The 2001 program also placed a great deal of emphasis on fiscal discipline and macroeconomic stability which were embraced by the JDP. It would be best to divide the JDP era into two, however. The earlier years through 2007 were characterized by improvements in both political and economic institutions supported by Turkey's candidacy for EU membership as

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well as growing liquidity and low interest rates in global financial markets. In the more recent period since 2008, in contrast, the JDP and its leader, Recep Tayyip Erdoğan, moved to consolidate their power and establish an increasingly authoritarian regime. Along with growing political polarization, political as well as economic institutions deteriorated steadily. The ensuing decline in both the domestic and international investments significantly reduced the growth rates (Şenses 2012, pp. 11–31).

Washington Consensus Policies

In the face of a great deal of political instability during the 1970s, coalition governments in Turkey had tried to avoid dealing with the root causes of the economic problems by relying on the remittances from workers in Western Europe and short-term borrowing with unfavorable terms. By the end of the decade, the political difficulties were compounded by a severe economic crisis. Against the background of import and output contraction, commodity shortages, and strained relations with the IMF and international banks, the newly installed center-right minority government of Süleyman Demirel announced a comprehensive and unexpectedly radical policy package of stabilization and liberalization in January 1980. Turgut Özal, a former chief of the State Planning Organization, was to oversee the implementation of the new package. While the Demirel government lacked the political support necessary for the implementation of the package, the military regime that came to power after the coup in September of the same year endorsed the new program and made a point of appointing Özal as deputy prime minister responsible for the economy. Özal thus made his mark on Turkey's economy during the 1980s, first as the architect of the January 24 decisions, later as deputy prime minister during military rule, and as prime minister after his party won the elections in 1983. With the experience he had acquired at the World Bank during the 1970s, he had first-hand knowledge of the new economic policies and, once in power, made radical decisions toward opening the economy.

The aims of the new policy package were threefold: to improve the balance of payments and to reduce the rate of inflation in the short term and to create a market-based, export-oriented economy in the longer term, thus putting the economy on an outwardly oriented course, a sharp turn from the previous era of inwardly oriented growth and industrialization. The package began with a large devaluation of the lira followed by continued depreciation of the currency in line with the rate of inflation, greater liberalization of trade and payments regimes, elimination of price controls, substantial price increases for the products of the state economic enterprises, elimination of many of the government subsidies, freeing of interest rates, subsidies, and other support

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measures for exports, and promotion of foreign capital (Arıcanlı and Rodrik 1990a, pp. 1343–50; Arıcanlı and Rodrik 1990b).

Bringing about reductions in real wages and the incomes of agricultural producers in order to improve fiscal balances and competitiveness in international markets was an important part of the new policies. The parliamentary government of Demirel had little success in dealing with the labor unions as strikes and other forms of labor resistance, often violent, became increasingly common in the summer of 1980. After the coup, the military regime prohibited labor union activity and brought about large reductions in labor incomes. The government's purchase programs for agricultural crops were also scaled back and agricultural prices remained significantly lower during military rule.

From the very beginning, the January 1980 program benefited from the close cooperation and goodwill of the international agencies, especially the IMF and the World Bank as well as the international banks. One reason for this key support was the increasingly strategic place accorded to Turkey in the aftermath of the Iranian Revolution. Another reason was the close relations between Özal and the international agencies and the special status accorded to Turkey. For most of the decade Turkey was portrayed by these agencies as a shining example of the validity of the stabilization and structural adjustment programs they promoted and enjoyed their goodwill. In economic terms, this support translated into better conditions in the rescheduling of the external debt and substantial amounts of new credit.

After the shift to a restricted parliamentary regime in 1983, Özal was elected prime minister as the leader of the new Motherland Party he had formed. He launched a new wave of liberalization of trade and payments regimes including reductions of tariffs and quantity restrictions on imports. These measures opened domestic industry further to the competition from imports especially in consumer goods. However, the frequent revisions in the liberalization lists, the arbitrary manner in which these were made, and the favors provided to groups close to the government created a good deal of uncertainty regarding the stability and durability of these changes. The response of the private sector to import liberalization was mixed. While export-oriented groups and sectors supported the new measures, the ISI industries, especially the large-scale conglomerates whose products included consumer durables and automotives, continued to lobby for protection of their industries. As the new regime gained permanence and the protectionism of the earlier era was dismantled in the following years, however, industry turned increasingly toward exports.

One of the more important new policies was the liberalization of the financial sector and opening it to the outside world. The exchange regime underwent fundamental changes and many transactions involving foreign exchange

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that previously were the monopoly of the Central Bank were opened to commercial banks. In addition, the government allowed all citizens to open and maintain accounts in foreign currency in the domestic banks. This new policy aimed at and succeeded in drawing the large foreign currency balances of the public from "under the mattress" into the banking system. In the longer term, however, this move made currency substitution away from the lira or "dollarization" easier. Because of the decline in the effectiveness of monetary policy, it became harder to deal with inflation in later years.

The liberalization of the financial markets took place gradually. In the earlier era, the nominal interest rates on domestic deposits had been determined by the Central Bank, usually below the rate of inflation. The transition toward the determination of interest rates by markets was complicated and involved a number of crises. From 1985 onward, important changes aimed at deepening the financial markets were also undertaken. Through auctions, the Treasury started selling bonds to banks and private individuals. In later years, the government would begin to make extensive use of this facility, thus straying further away from fiscal discipline. In addition, with the new flexibility gained in the exchange-rate regime, private banks were able to secure new credit from international sources, both private and public. These innovations, in a country where the savings rate had always remained low and an important share of investments was financed through external sources, created important opportunities on the one hand, but also introduced new risks (Arıcanlı and Rodrik 1990a, pp. 1343–50; Arıcanlı and Rodrik 1990b).

The most notable success of the new policies was the increase in exports. From very low levels of $2.3 billion and 2.6 percent ratio of GDP in 1979, export revenues rose to $8 billion in 1985 and $13 billion or 8.6 percent of GDP in 1990 (figures 11.1 and 11.2). Most of the increases were caused by the rise in exports of manufactures whose share in total exports rose from 36 percent in 1979 to 80 percent in 1990. Textiles, clothing, and iron and steel products ranked at the top of the list of exports (Turkey, Turkish Statistics Institute, 2014). The growth in exports was achieved primarily by reorienting the existing capacity of ISI industries toward external markets. In the early years, the exporters were supported by a steady policy of exchange-rate depreciation, by credits at preferential rates, tax rebates, and foreign exchange allocation schemes. The latter mechanisms amounted to a 20–30 percent subsidy on unit value, although their magnitudes gradually declined during the second half of the decade. In the early stages, the export drive also benefited from the war between Iraq and Iran as Turkey exported to both countries. After the end of the war, however, the European Community's share in Turkey's exports returned to 50 percent and remained at that level until the end of the century (Barlow and Şenses 1995, pp. 111–33; Waterbury 1991, pp. 127–45; Arslan and van Wijnbergen 1993, pp. 128–33; also see figure 11.6 below).

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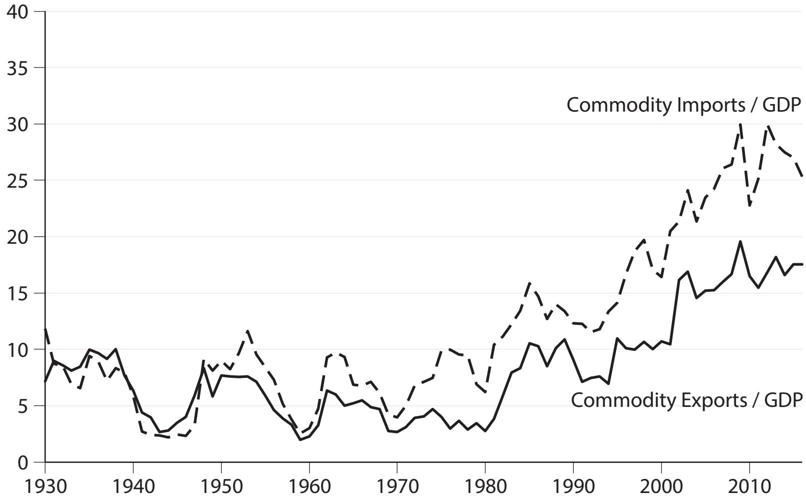

FIGURE 11.1. Share of Foreign Trade, 1929–2015 (Ratios of Commodity Imports and Commodity Exports to GDP in percent). Source: Official series from Turkey, Turkish Statistical Institute 2014.

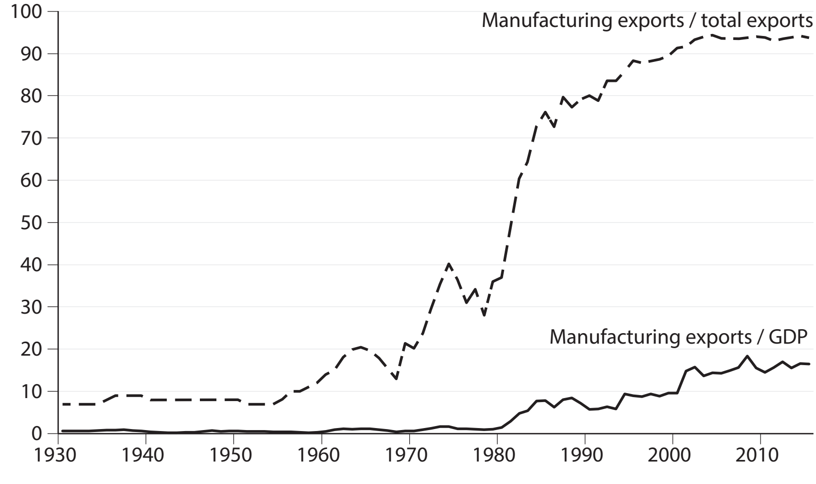

FIGURE 11.2. Shares of Manufacturing Exports in Turkey, 1930–2015 (percent). Source: Official series from Turkey, Turkish Statistical Institute 2014.

Aside from the export performance, however, the impact of the new policies on the real economy was rather mixed. Most importantly, the new policies were not able to mobilize high levels of private investment. In the manufacturing industry, high interest rates, steady depreciation of the currency which raised the cost of imported capital, and the unstable political environment

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were the most important impediments. Most of the increase in exports of manufactures was achieved with the existing industrial capacity. The same concerns adversely affected foreign direct investment as well. Some foreign capital flowed into the banking sector thanks to the liberalization of banking and finance, but in other areas, foreign direct investments remained limited, as was the case in earlier periods (Boratav, Türel, and Yeldan 1996, pp. 373–93; Arıcanlı and Rodrik 1990a, pp. 1347–48).

Politics largely determined in which sectors, and to what extent, the new economic policies would be implemented. After military rule ended and a new multiparty political regime was established, albeit with many restrictions, the government decided to pursue policies that were politically beneficial or less costly, while staying away from policies or measures that appeared politically more difficult. For example, one of the priorities of the 1980 program was the privatization of state economic enterprises. Many of these companies had accumulated large losses during the 1970s. Initially, it was decided that they would be privatized after their balance sheets were improved. The privatization process was littered with technical, legal, and political obstacles, however. Those standing against privatization did not just include the workers, but also the politicians who had no intention of abandoning the control they exercised over these firms.

Reducing labor and agricultural incomes was one of the most fundamental elements of the January 1980 program. Both the military regime and the Motherland Party followed policies that kept wages and agricultural prices low until 1987, taking advantage of the political and other restrictions imposed by the military regime. The burden of the new policies was thus placed squarely on the shoulders of groups that could not make their voices heard and were not sufficiently organized. The closure of the unions by the military government and the introduction of new laws that eroded their power played important roles in the decline of wages. The agricultural sector, which provided employment and income to about half of the labor force, was also all but ignored by the Motherland Party. As a result, the agricultural sector showed the lowest rates of output increase during the postwar era, averaging only 1.4 percent per year for the decade and failing to keep pace with population growth for the first time in the twentieth century.

The new policies were thus given support from two corners during the 1980s—repression of labor and agricultural incomes by the military and generous foreign capital inflows by the international financial institutions. Despite the decline in wages and agricultural prices paid by the government as well as the volume of price support programs, however, public sector deficits, high rates of monetary expansion and inflation continued. The annual rate of inflation declined from 90 percent in 1980 to 30 percent in 1983 but remained around 40 percent in the following years (Rodrik 1990, pp. 323–53).

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One investment program that was pursued energetically by the government was the large Southeast Anatolia Project originally planned in the 1960s. It envisaged the building of a number of interrelated dams on the Euphrates River, including hydroelectric plants and irrigation of 1.6 million hectares in the plain of Harran, which would double the irrigated area under cultivation in Turkey. This large and expensive project stood apart from all other rural development schemes since the end of World War II. For a long time, however, the project was designed and implemented without sufficient understanding or concern for the needs of the local population. In response to the rise of Kurdish nationalism in the region, governments in Ankara attempted to redefine the project as an integrated regional development program seeking to improve the social and economic fabric of a large and poor region. The project then began to include large investments in a wide range of development-related sectors, including transportation, urban and rural infrastructure, as well as agriculture and energy. The absence of a shared vision between the planners and the intended beneficiaries, the local Kurdish communities, has seriously limited its benefits, however (Mutlu 1996, pp. 59–86; Çarkoğlu and Eder 2005, pp. 167–84).

Along with trade and capital account liberalization in the new era, governments also began to support the tourism sector as an important foreign exchange earner and employment provider. Beginning in the 1980s, allocation of state lands and long-term loans with low interest rates from public banks attracted large-scale investments in the sector by domestic entrepreneurs. As tourism evolved further in the 1990s, these private companies began to adopt the low-cost, labor-intensive, all-inclusive holiday packages organized by international tour operators as the leading product in the sector. These packages were offered by hundreds of hotels and holiday villages of various sizes along the southern and southwestern coastline. Turkey received 40 million tourists and ranked sixth in the world in 2014. Total international tourism receipts were close to $30 billion, about 3 percent of GDP, and ranked eleventh in the world in the same year (World Tourism Organization 2016, pp. 8–11). Tourism thus provided significant amounts of full-time and part-time employment at different skill levels but remained vulnerable to global or regional economic downturns as well as international and domestic political events, including terrorism.

Return of Political and Economic Instability

The restrictions the military regime placed on the politicians of the 1970s were lifted after a referendum and they returned to active politics in 1987. With the transition to a more open electoral regime, the opposition began to criticize both the deterioration of income distribution and the arbitrary manner in

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which Özal and his Motherland Party implemented the new policies. The protests and resistance movements that began among public sector workers and continued with the miners of Zonguldak in 1989 showed that the period of repression imposed by the military government was being left behind. In the longer term, the fragmentation on both the center-right and center-left of the political spectrum between the old and new politicians fueled a good deal of instability. Under short-lived coalition governments, budget deficits soared and public sector debt accumulated. Between 1987 and 2002, Turkey thus went through a very difficult period, marked by intertwined political and economic crises. Like the other military coups launched ostensibly to restore political stability, the 1980 coup thus became the cause of long-lasting political and economic instability.

In response to the more competitive political conditions after 1987, the Motherland Party government and the coalition governments that replaced it beginning in 1991 responded with populist policies. They sharply raised wages in the public sector as well as the prices of agricultural products and broadened the scope of the state's purchase programs for agricultural crops. Through public banks, they extended cheap credits to small businesses as well as agricultural producers. In addition, the prices of products sold by state economic enterprises began to lag behind inflation. These policies rapidly widened the budget deficit. In addition, state economic enterprises including public banks began to record huge losses. The expanding war with the Kurdish PKK which began in 1984 in the southeast continued to place new burdens on the budget (Kirişci and Winrow 1997; Aydin and Emrence 2015).

In August 1989, as macroeconomic balances began to deteriorate, Özal and the Motherland Party decided to further liberalize the exchange-rate regime and remove the restrictions on inflows and outflows of capital including foreign borrowing by the Treasury. With the infamous decree number 38, financial globalization acquired a legal framework. The basic aim of the decree was to ease the difficulties that the public sector was facing with financing its budget deficits, even if only in the short term, and to widen the room for maneuver of the government. After the decree, high domestic interest rates and a pegged exchange-rate regime attracted large amounts of short-term capital inflows. Private banks rushed to borrow from abroad in order to lend to the government at high rates of interest. Public sector banks were directed by the governments to finance part of the deficits. In the longer term, the decision to liberalize the capital account without achieving macroeconomic stability and creating a strong regulatory infrastructure for the financial sector proved to be very costly. As the economy became increasingly vulnerable to external shocks and sudden outflows of capital, the 1990s turned into the most difficult period in the post–World War II era (Akyüz and Boratav 2003, pp. 1549–66;

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Demir 2004, pp. 851–69; Gemici 2012, pp. 33–55). Turkey's economy continued to struggle with large current account deficits and macroeconomic stability in later periods as well. In fact, one can argue that full liberalization of the capital account or financial globalization has not interacted very well with Turkey's domestic institutions.

Another method used to finance the rapidly widening budget deficit, as was the case in earlier periods, was printing money. As the money supply began to increase, inflation, which was brought under control only partially during the 1980s, began to pick up pace again. Annual rates of inflation rose at the end of the 1980s and fluctuated between 50 percent and 100 percent during the 1990s (figure 11.3). One important factor that reinforced the link between public sector deficits and inflation was the introduction of foreign exchange deposit accounts in 1984 as part of the policies of financial liberalization. By reducing the demand for domestic money, this measure increased the inflationary impact of the public sector deficits.

It was not easy to follow the rise of public sector deficits and outstanding debt from the official series at the time since large parts of the deficits and losses were transferred to the balance sheets of the public sector enterprises during this period. Moreover, the full cost to the public of the pillaging of the assets of the public banks could be estimated only after the 2001 crisis. It is now possible to put together an approximate account of the rise of the outstanding debt of the public sector in relation to the size economy. Figure 11.4 shows that the total domestic and foreign debt of the public sector rose dramatically from about 40 percent of GDP in 1990 to 90 percent in 2001.

Along the way, measures that would have increased the resilience of the economy to internal and external shocks were pushed aside. Virtually no progress was made in the privatization of the state economic enterprises. Both workers and politicians remained opposed to privatization. Moreover, attempts to sell some of the large state enterprises were accompanied by scandals involving leading politicians. The sale of some of the smaller public sector banks resulted in large losses for the state sector as these banks were stripped of their assets by the well-connected buyers, and the full guarantees on bank deposits made the public sector responsible for their large losses. These large losses were all added to outstanding public debt after 2001 (Tükel, Üçer, and Rijckeghem 2006, pp. 276–303; Akın, Aysan, and Yıldıran 2009, pp. 73–100).

The large public sector deficit and the rapidly rising public sector debt made the economy very vulnerable to external as well as internal shocks. A negative event in the global economy or politics or the perception that the public sector deficit was becoming unsustainable could trigger large outflows of short-term capital, raise interest rates, depreciate the currency, and lead to a recession. These stop-go cycles of capital flows were repeated four

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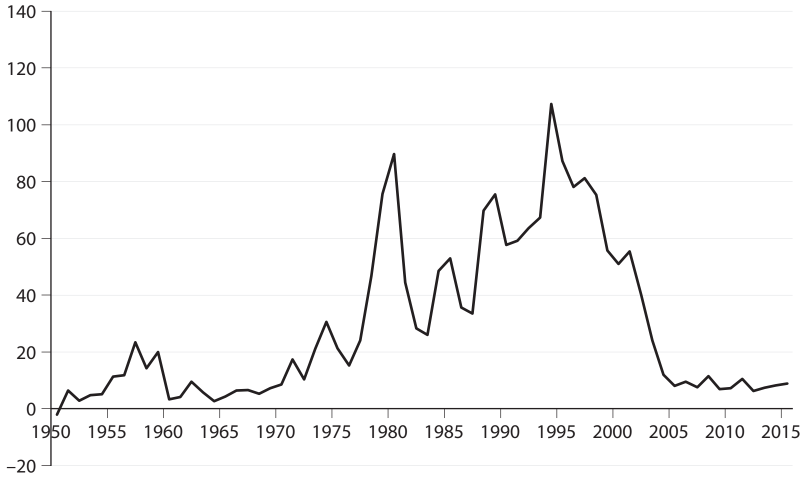

FIGURE 11.3. Annual Rate of Inflation in Turkey, 1950–2015 (percent).
Source: Official series from Turkey, Turkish Statistical Institute 2014.

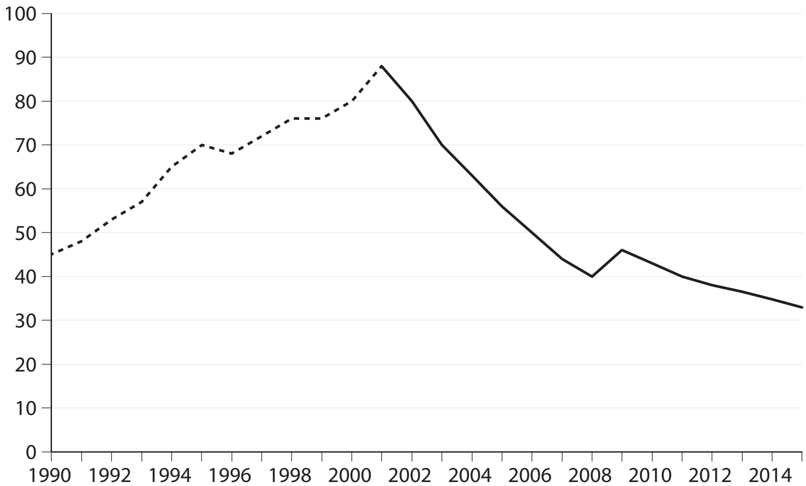

FIGURE 11.4. Public Sector Debt Stock / GDP, 1990–2015 (percent).
Source: Based on official series from Turkey, Ministry of Development 2017.

times, in 1991, 1994, 1998 and 2000–2001, the last of which was the most severe. Even though GDP per capita continued to rise during these years, the trend rate was significantly lower than both the earlier and later periods (figure 11.5).

High rates of inflation and high real interest rates made income distribution increasingly more unequal during the 1990s. The more organized groups

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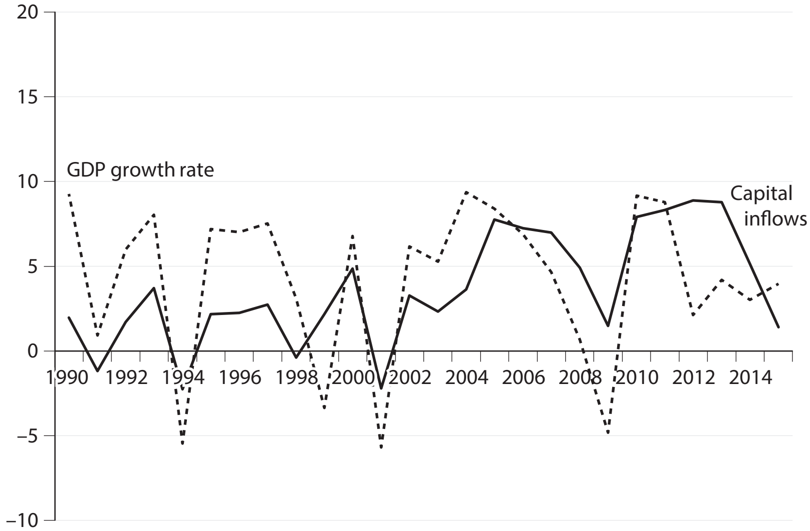

FIGURE 11.5. Capital Inflows and GDP Growth, 1990–2015 (as percentage of GDP). Source: Official series from Turkey, Ministry of Development 2017.

were able to develop some protection and shield themselves to some extent. Organized workers benefited from collective wage agreements, agricultural producers from support purchases, and small business owners from low-interest credit. Middle classes relied on bank accounts in foreign currency and those with larger cash assets lent to the government at high rates of interest. Not all sections of society were equally successful against inflation, however. With the added impact of the war in the Southeast and forced migration of large numbers of Kurds from rural to urban areas, income distribution deteriorated sharply (Yükseker 2009, pp. 262–80).

Crisis and Another Program

By the end of 1999 it was clear that the macroeconomic balances were not sustainable. Negotiations with the IMF led to a new stabilization program with a pegged exchange-rate regime as the key anchor to bring down inflation. Stability programs supported by the IMF were launched several times during the 1990s, but their implementation was soon abandoned in each case. There were major questions about the design and implementation of the new program. While the program included a plan to reduce the large deficits in public finances and deal with the large losses accumulated by public banks as well as the problems of the private banks, it remained to be seen whether these measures would be adopted by the government.

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Even though some progress was made toward reducing the budget deficit, many of the measures envisaged in the program could not be implemented because the coalition government led by Ecevit could not muster the necessary political will. The IMF's insistence on a managed rather than floating exchange rate also contributed to the crisis. After a smaller crisis at the end of 2000 was met with some support from the IMF, the large deficits of the private and public banks resulted in a major crisis at the beginning of 2001. The government was forced to abandon the exchange-rate anchor after watching outflows of approximately $20 billion within a few days. The lira was then allowed to float and lost half of its value against major currencies within a few months. As interest rates rose and the banking sector collapsed, GDP declined by 6 percent in 2001 and unemployment and urban poverty increased sharply (Akyüz and Boratav 2003, pp. 1549–66; Öniş 2003, pp. 1–30; Kazgan 2005, pp. 231–54; Van Rijckeghem and Üçer 2005, pp. 7–126; Özatay 2009, pp. 80–100).

Kemal Derviş, who was working as a high-level official at the World Bank, was invited to Turkey in early 2001 to prepare a new program and secure international support for it as minister in charge of the economy. The new program, prepared with the support of the IMF, contained stabilization measures as well as long-term structural and institutional reforms. For long-term macroeconomic stability, the program aimed to build budget surpluses for years to come in order to reduce the large outstanding public sector debt. It also aimed to insulate the public sector enterprises and especially the banks legally and administratively against the encroachment of the governments. Furthermore, instead of trying to control the inflation by managing the exchange rate and limiting the depreciation of the lira, a strategy that turned out to be very costly in the previous period, the new program adopted a floating exchange-rate regime.

The 2001 program also contained elements that differed significantly from those in the previous programs prepared with IMF support after 1980. In fact, it has been argued that the program reflected the post–Washington Consensus principles (Öniş and Şenses 2005, pp. 263–90). Instead of establishing the macro balances and leaving the rest to the markets, it accepted that the markets, left to their own devices, could produce undesirable outcomes and needed to be regulated. The program thus envisaged a new division of labor between markets and the state. The regulation and supervision of specific markets was being delegated to newly established institutions, which were intended to be independent from the government. For this reason, the program needed to be supported by a series of structural reforms and new laws. Some of the other legislative changes were designed to prevent governments from using for its short-term goals the public sector, particularly the public

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banks, and more generally increase the autonomy of the Central Bank. To what extent these regulations would be effective and whether and to what extent the new institutions would be independent from the political authorities would be determined more by how the laws would be implemented over time, rather than by the laws themselves (Sönmez 2011, pp. 145–230).

The new program also sought to restructure the banking sector after all the turbulence it experienced during the 1990s. Both public and private sector banks that had gone bankrupt would be dismantled and the outstanding debts of the public banks would be assumed by the public sector and spread out over time. In addition, contrary to the lax practices of the 1990s, the program envisaged closer supervision of the banking sector. A Banking Regulation and Supervision Agency which was to function independently of the government was set up for this purpose (Tükel, Üçer, and Rijckeghem 2006, pp. 276–303; Akın, Aysan, and Yıldıran 2009, pp. 73–100). After the Justice and Development Party (JDP) came to power on its own following the elections of 2002, it decided to continue to implement the new program with the support of IMF.

Customs Union and the EU Candidacy

Turkey's relations with the European Union go back to the Ankara Agreement of 1963, which had anticipated eventual membership in what was then called the Common Market. The Common Market and later the European Community was Turkey's most important trading partner, accounting for approximately 50 percent of its exports and more than 60 percent of its imports during those decades (figure 11.6). Little progress was made toward membership, however. During the military regime and its aftermath, Turkey remained far from fulfilling the political criteria for membership and the application for candidacy made by Prime Minister Özal was rejected in 1987. The coalition governments of the 1990s thus sought to at least take economic relations one step closer by signing the Customs Union agreement in 1994. With the agreement, the two sides eliminated the customs duties in the trade of manufactured goods between Turkey and the EU and aligned customs tariffs on imports from third countries with the levels applied by the EU. Trade in agricultural goods was left outside the customs union.

The EU share in Turkey's foreign trade did not increase after the signing of the customs union agreement because the tariff levels between Turkey and the EU had been declining since the 1980s and they were quite low in the early 1990s. Nonetheless, the EU remained Turkey's largest trading partner by a substantial margin. As economic stability returned after 2001, Turkey began to expand its external trade, including trade with the EU. Turkey's exports to

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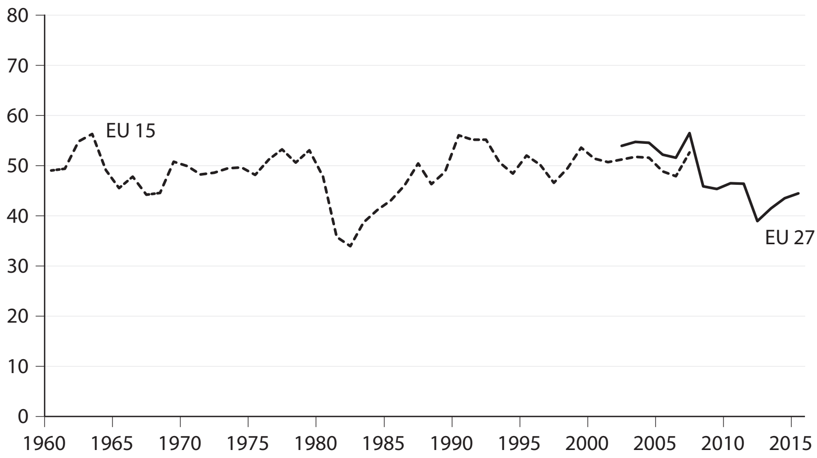

FIGURE 11.6. EU's Share in Turkey's Exports, 1960–2015 (percent).
Source: Official series from Turkey, Turkish Statistical Institute 2014.

the EU began to rise rapidly and multinational companies producing in Turkey, especially in the automotive industry, began to use Turkey as a production base for export both to the EU and other countries. In the more labor-intensive sectors such as textiles, exports to the EU also increased initially but they declined after the EU lifted restrictions imposed on China.

The customs union arrangement brought important benefits to Turkey's economy and especially to its manufacturing sector. At the time the customs union agreement was signed, the government and the political establishment thought that Turkey would soon become a member of the EU and would be included in the decision-making. However, as Turkey continued to remain outside the decision-making structures of the EU in later years, the inability to influence tariffs related to imports from third countries, especially those from East Asia, it began to impose costs and limit the benefits of the Customs Union arrangement (Yilmaz 2011, pp. 235–49; Antonucci and Manzocchi 2006, pp. 157–69).

The public saw the benefits of EU membership more in economic than in political terms and expected that after membership, per capita incomes would rise rapidly toward EU averages. The economic difficulties of the 1990s and the crisis of 2000–2001 thus served as a powerful reminder of the economic benefits of EU membership and created considerable pressure on the politicians to proceed with political reforms. The coalition governments thus gathered a good deal of political will around the turn of the century and stood behind the reforms, including important political and social amendments to the military regime constitution of 1982. As a result, the EU brought

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up, for the first time, the possibility of formally accepting Turkey as a candidate for membership.

Early JDP Years

While the secular parties struggled with rising political and macroeconomic instability as well as the many demands of a rapidly urbanizing society during the 1990s, the Islamist political parties focused on local organization and local government delivering urban services. They were often set back by the military and the judiciary but returned with perseverance. In the process, they moderated their policies and improved their political skills. The emergence of an Islamic bourgeoisie seeking economic integration with the West also helped them reshape their political goals and ideology.

The depth of the economic crisis in 2001 generated strong reactions from the public, not only against the political parties in power, but against all the parties that had been in charge of the economy during the previous decade. In the general elections held in 2002, all of them were voted out of the parliament. While those parties paid dearly for more than a decade of political and economic instability, the Justice and Development Party, formed by a group of politicians who had split from the Islamist movement, was able to exploit this opportunity and came to power by itself with only 34 percent of the national vote. The weaknesses of the secularists and the strengths of the Islamist movement thus precipitated JDP's ascent to government.

At the time JDP won the elections, Turkey's relations with the EU were making significant progress. The new party had been established by politicians who had pursued Islamist policies in parties led by Necmettin Erbakan and opposed Turkey's membership in the EU for many years. Before the elections of 2002, however, the new party began to differentiate itself from Erbakan's positions. Once in power, JDP continued to support Turkey's membership in the EU and the political reforms. Turkey was formally accepted by the EU as a candidate for membership in 2004. The IMF and the EU emerged in this period as the two external anchors reinforcing the stabilization of the economy and the long-term transformation of the institutional framework (Öniş and Bakır 2007, pp. 1–29; Yılmaz 2011, pp. 235–49).

In its early years in power, JDP appeared to pursue democratization and the Westward-oriented goals of Republican modernization. The party hoped to expand the room for Islam and religious freedoms more generally with its goals of democratization and EU membership. With this agenda, it was able to build a broad coalition. In its first five years in power, JDP also pursued policies that were more pro-private sector than any of the earlier governments. As a result, it received the support of major businesses and industrialists in

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Istanbul as well as the more conservative businesses and industrialists across the country.

The JDP governments led by Recep Tayyip Erdogan also embraced the 2001 program supported by the IMF. Fiscal discipline, which was a key element of that program, became a key priority for JDP governments for achieving macroeconomic stability. Indirect taxes on gasoline and consumer goods were raised sharply. Another important contribution to lowering the public sector deficits came from privatizations. Earlier attempts at privatization had not made much progress because of legal and political obstacles, but JDP pursued them even at the cost of abandoning goals such as long-term productivity, efficiency, competition, and protecting the interests of the consumer (Atiyas 2009, pp. 101–22; Ökten 2006, pp. 227–51). As a result, the government was able to maintain large public sector surpluses before debt payments which averaged 6 percent of GDP until the global crisis of 2008–2009. Thanks to these surpluses, the ratio of public sector debt to GDP was reduced from approximately 80 percent in 2002 to 40 percent in 2008 (figure 11.4).

These large budget surpluses enabled the JDP government to bring inflation under control and below 10 percent annually for the first time since the 1960s (figure 11.6). The restoration of macroeconomic balances and the start of accession negotiations with the EU also paved the way for significantly higher levels of foreign direct investment. Also supported by growing global liquidity, foreign direct investments, which had remained very low since the 1920s, rose sharply from less than $3 billion annually before 2004 to $20 billion annually during 2005–2007. Because an important share of these investments took the form of acquisitions of existing local companies, however, their contribution to job creation remained limited.

Macroeconomic stability combined with strong increases in exports as well as the favorable global economic environment of growing liquidity and low interest rates led to large increases in GDP per capita. The accumulation of excess capacity and pent-up demand during the previous fifteen years of low economic growth also helped economic performance during the early JDP years. From 2003 through 2007, GDP increased at an annual rate of 6.9 percent and by a total of 40 percent. GDP per capita increased at an annual rate of 5.4 percent and by a total of 30 percent (table 11.1). Both of these annual rates were well above the long-term trend rates for Turkey and for developing countries as a whole since the end of World War II. Economic growth and lower debt payments thanks to declining public sector debt soon enabled the government to raise spending on infrastructure investment, health care, and education. JDP was thus able to deliver significant material benefits to its constituents not only through the increases in incomes but also higher levels of

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government spending in these areas. These benefits continued to support JDP at election time in later years.

While the economy recovered and incomes increased, the economic policies of JDP did not evolve beyond the institutional regulations and the fiscal discipline included in the 2001 program. The JDP governments did not develop their own long-term perspective on industrialization, growth, and employment creation (Taymaz and Voyvoda 2012, pp. 83–111). As a result, the economy had already begun to slow down before the onset of the global crisis. An important cause of the slowdown was the considerable appreciation of the Turkish lira due to short-term capital inflows and the loss of competitiveness of domestic production in international markets. Rising levels of global liquidity and the appreciation of the lira also encouraged importation of more inputs rather than their production locally, and even encouraged some firms to shift their production abroad to lower cost locations. Combined with a declining savings rate, the balance-of-payments deficit began to widen. Nonetheless, the economic recovery and growth achieved in its first five years in power allowed JDP to increase its share of the vote to more than 46 percent and secure a larger majority in parliament in the 2007 elections (Akçay and Üçer 2008, pp. 211–38; Öniş 2009, pp. 21–40).

Political and Economic Deterioration after 2007

The global crisis of 2008–2009 caught Turkey's economy on a slowly declining trend. Because the previous crises were still fresh in everyone's minds, the first impact of the crisis proved severe. In the initial months, large declines were recorded not just in exports, but also in investments and consumption. However, the banking sector had behaved more cautiously after the 2001 crisis, and the supervision and monitoring of the sector had been well managed. As a result, the banking sector remained resilient and the impact of the crisis was short-lived. In addition, the tight fiscal policies followed in the previous years had reduced the public sector debt ratio. Both monetary and fiscal policy could be relaxed for a few years to soften the impact of the crisis, an option not available to many other countries. By 2010, production and employment had returned to their pre-crisis levels, even if that was not yet the case for exports. However, as the economic problems faced by the European Union, which accounted for 50 percent of Turkey's exports, and the political problems in the Middle East deepened in the following years, Turkey's exports began to stagnate as well (figure 11.1).

Even more importantly, the formal negotiations for Turkey's membership in the EU began in 2005. At about the same time, however, center-right

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governments came to power in Germany and France and they soon began to openly oppose Turkey's membership. This shift in the positions of the two key countries was an important turning point in Turkey's relations with the EU. The EU anchor had underpinned important political reforms after 1999 and had also contributed to the economic recovery after 2001. As that anchor began to weaken and the goal of EU membership became increasingly uncertain, JDP's willingness to continue with the political reforms as well as long-term changes in economic institutions began to wane.

Domestically, the secular elites in the judiciary and the military attempted to close down JDP in 2007 at a time when it was actually in government. The final vote in the Constitutional Court was close and JDP avoided closure by a single vote. After the national elections in 2007, defeating its rivals and consolidating its power became the single most important goal for JDP and its leader, Prime Minister Erdoğan. Many of the earlier alliances were dismantled as he pursued an increasingly narrow path toward greater power in later years. Using a good deal of fabricated evidence and the network of the Muslim cleric Fethullah Gülen inside the judiciary and the police, the JDP then launched a wave of court cases against the military, accusing its leadership of plotting against the government and putting them on the defensive. The government soon began to control large segments of the media and curtail civil liberties. It moved to dispose of the checks and balances in the political system and undermine the separation of powers between the executive, legislature, and judiciary. A referendum in 2010 presented as legal reforms for EU membership allowed JDP and Erdoğan to undermine and eventually eliminate the independence of the judiciary. While society and politics were becoming increasingly polarized, the rising levels of employment and incomes as well as the increases in the access to health care, education, and other government services during the early JDP years helped the party maintain its popular support.

Turkey's slide toward authoritarianism continued after Erdoğan was elected president by popular vote in 2014. As he struggled to change the constitution and move from a parliamentary to a presidential system, the civil war in Syria and the return of military conflict in the Kurdish areas added to the political and economic difficulties. In foreign policy, the JDP had attempted to be more active in the Middle East. Peaceful relations with its neighbors in the region appeared to provide economic as well as political benefits. However, unrealistic expectations about a leadership role in the Middle East after the Arab Spring backfired badly, drawing Turkey into a ruinous civil war in Syria. One result was the arrival of three million Syrian refugees shortly after 2011. Another reversal of policy with major consequences took place on the Kurdish issue. For many years during the JDP era, the Kurdish conflict had

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edged toward a peaceful resolution. After the PKK refused to support Erdoğan's plans for a presidential system, however, tensions escalated very quickly in 2015. Once again, the southeast turned into a zone of conflict as the security forces and the PKK inflicted large casualties on each other as well as the civilian population. Tourism, which had emerged as an important sector of the economy since the 1980s, was deeply hurt by the outbreak of these conflicts and the associated incidents of terrorism inside Turkey.

Since 2007, politics and the drive to consolidate power have been the main priorities for JDP and Erdoğan. After the strong performance in the earlier years, the economy has been seriously damaged by the growing political conflict as well as the slide toward authoritarian rule. As the JDP government moved to control the economy more closely after 2007, the regulatory agencies established as part of the 2001 program came under increasing pressure and their autonomy was soon eliminated. Similarly, the Central Bank was forced to adjust its stance under pressure from the government. It soon abandoned its goal of lowering the inflation rate further and began to pursue more accommodative monetary policy. The annual rate of inflation which had declined to 6 percent in the aftermath of the global crisis thus began to edge up toward 10 percent (Gürkaynak and Sayek-Böke 2012, pp. 64–69; Acemoglu and Üçer 2015). Because the JDP governments maintained fiscal discipline even after the stand-by agreement with the IMF came to an end in 2008, they were able to avoid the economic crises like those of the 1990s. Fiscal stability was not sufficient to maintain the high rates of growth, however.

As JDP moved to consolidate its rule, supporting business groups close to the party and the government emerged as a leading goal of economic policy after 2007 and especially after 2010. Business groups close to JDP were increasingly favored in tenders launched by the central government as well as the local governments, in large-scale energy, infrastructure and housing projects, in the allocation of credit by public and private banks and other areas. For example, the procurement law which sought transparency and competitiveness and passed with the support of the World Bank in 2002 was amended more than 150 times during JDP rule in order to adapt it closely to the needs of the government and the public agencies. In addition, an increasing number of industries and activities were exempted from the law over time (Çeviker Gürakar 2016; Buğra and Savaşkan 2014, pp. 76–81). As the political fight between the JDP and the network of the Islamist cleric Gülen intensified after 2012, property rights of the political opponents of the government declined, rapidly raising questions about how far the slide toward authoritarianism would continue and which other groups may be threatened in the future.

Rising political tensions and steady deterioration of the institutional environment after 2010 sharply reduced private investment. The stagnation in

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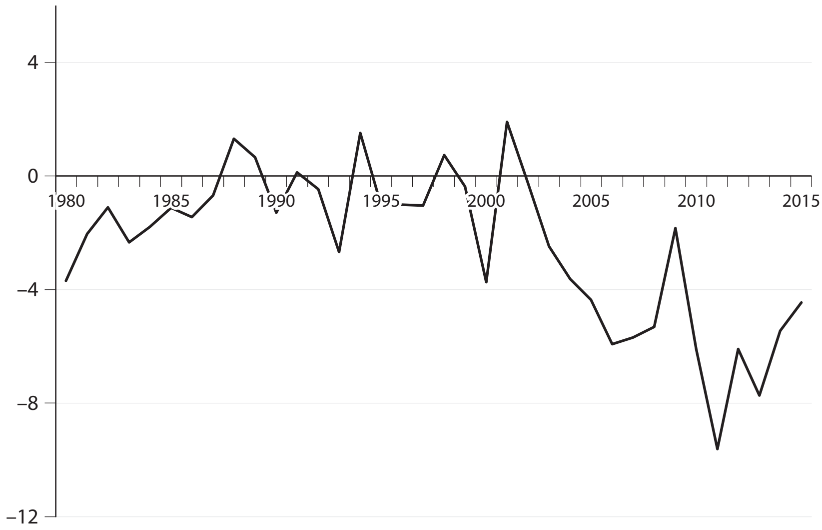

FIGURE 11.7. Current Account Balance, 1980–2015 (as percentage of GDP). Source: Official series from Turkey, Ministry of Development 2017.

European markets, the civil war in Syria, terrorism, and the sharp decline in tourism revenues have also contributed to the economic slowdown. As a result, annual growth rates of GDP declined from an average of 6.9 percent during 2003–2007 to 3.2 percent during 2012–2015. The unemployment rate in the urban economy increased from 10.5 percent at the end of 2011 to 12.3 percent at the end of 2015.

Another important long-term economic problem has been the steady decline in the savings rate from 24 percent of GDP in 1998 to 18 percent in 2007 and 13 percent in 2015. Current account deficits widened as a result and the private sector had to secure large sums from abroad every year in order to finance its investments (figure 11.7). Foreign direct investments, most of which came from the EU countries, could finance only a fraction of the deficits. Foreign direct investments, which increased to $20 billion per year or more than 3 percent of GDP along with Turkey's EU candidacy during 2005–2007 declined during the global crisis and with the fading of Turkey's candidacy. They averaged $13 billion or about 1.5 percent of GDP during 2010–2015. Thanks to the high levels of liquidity in the international markets in the aftermath of the global crisis, financing the rest of the current account deficits was not a problem early on. The banking sector was able to borrow record amounts from the international banks and direct most of these funds to the private sector and use the rest to finance private consumption. As quantitative easing by the Fed-

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eral Reserve began to end, however, Turkey's economy looked increasingly vulnerable. During the difficult 1990s, the large public sector deficits had been the major problem for the economy. Economic policy during the JDP era eliminated the public sector deficits but shifted them, in effect, to the private sector. Large current account deficits as well as the rising levels of indebtedness of the private sector thus made Turkey's economy increasingly fragile during the later years of the JDP era.

In response to lower rates of growth and rising levels of unemployment, the government tried to keep interest rates low and support the construction sector as well as private consumption. Given the high rates of urbanization and growing demand for real estate, the construction sector appeared especially attractive to the government for creating domestic demand. In addition, changing the existing rules on urban plans and allowing higher densities of construction was usually a safe and low-tech method for ensuring that specific firms and individuals would benefit directly and quickly. Accommodative monetary policy kept the construction boom going. The shopping malls and the growing number of housing and office building projects rising in big cities thus became symbols of an economic model based on consumption and construction funded by external borrowing.

Agriculture in the Neoliberal Era

During the ISI era after World War II, Turkish agriculture was regulated by support price policies, subsidies for agricultural inputs, commodity boards, and a protectionist trade regime. Commodity boards and other public agencies were also expected to develop quality standards for food and agricultural products and ensure that the growers and producers complied with them. As a result, farmers enjoyed considerable security and managed to remain relatively immune to market fluctuations. Along with the neoliberal restructuring of the economy under the auspices of the IMF and the World Bank, various measures were introduced with the aim of reducing government support programs and more generally government interventionism in agriculture and liberalizing food markets. Although its pace was slow due to political instability during the 1990s, restructuring gained momentum during the JDP era with the enactment of an economic reform package with strong terms for further liberalization of the farming sector. The agreements signed with the IMF and the World Bank after the crisis of 2001, Turkey's candidacy for EU membership, and the commitments made by the government for WTO membership played key roles in this shift. As a result, agricultural support policies for many commodities were largely discontinued, subsidies for agricultural inputs and

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credits were generally removed, most of the state agricultural enterprises were privatized, and the trade regime in agriculture was liberalized to a significant degree. This restructuring had the effect of shifting power and responsibility in marketing and quality management of agricultural products from public bodies to private institutions. It also increased the power and profile of the large international companies in domestic markets. The scope of this deregulation process has been wider and its intensity has been stronger in Turkey than in many other developing countries (Aydın 2010, pp. 149–87; Keyder and Yenal 2011, pp. 60–86).

In addition, relaxation of import controls has led to swift commercialization and internationalization not only in the seed sector but also in other input markets such as fertilizers, chemicals, and pesticides. On the output side, big international retailers and food manufacturing firms have been heavily engaged in organizing flexible procurement networks that stretch across Turkey as well. The role played by retailing and wholesaling firms, market brokers, and supermarket chains, all of which acted as intermediaries between the direct producer and the consumer, have thus increased in recent decades. These firms have better access to relevant information networks and have been more flexible in their procurement and marketing strategies.

These far-reaching changes have presented new opportunities as well as challenges for the small and medium-sized farmers. For the grain, pulses, and sugar beet farmers of the Anatolian interior, the options have been limited. Their crops were not labor-intensive and the sunk costs made it harder to switch. These farmers also had relatively stable family populations and there was not much excess labor to employ in additional household income-earning strategies. In contrast, in the coastal regions, especially in Mediterranean and Aegean villages, opportunities from market-oriented, labor-intensive agriculture were often combined with employment and incomes elsewhere. The farming of fresh vegetables and fruits has become the most dynamic agricultural activity in these regions in recent decades, contributing to the rise in the value added. The annual value of fresh produce has recently exceeded one-quarter of the total value of crop production. Turkey is currently among the top ten producers of tomatoes, cucumbers, eggplants, and onions in the world. Vegetables and fruits began to lead agricultural exports as well. More than half of Turkey's agricultural exports have been in fruits and vegetables in the last decade. The European Union countries, Russia, and some Middle Eastern countries have been the main markets for vegetable and fruit exports. Small and medium-sized producers in the more commercialized regions have combined income from these often labor-intensive agricultural activities with employment opportunities provided by tourism and seasonal employment in other sectors (Keyder and Yenal 2011, pp. 60–86).

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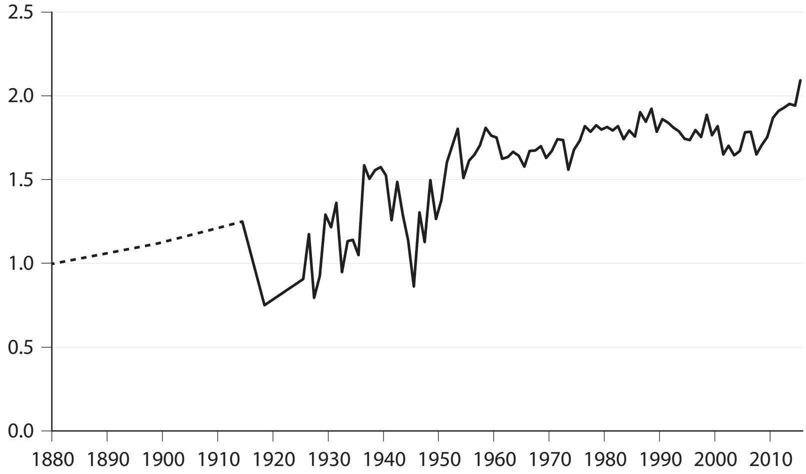

FIGURE 11.8. Agricultural Value Added per Population in Turkey, 1880–2015 (index in constant prices; 1880 = 1,0). Source: Based on national income and population series discussed in chapter 2 for the Ottoman era; national income accounts and population series from Turkey, Turkish Statistical Institute 2014 for the period since 1923.

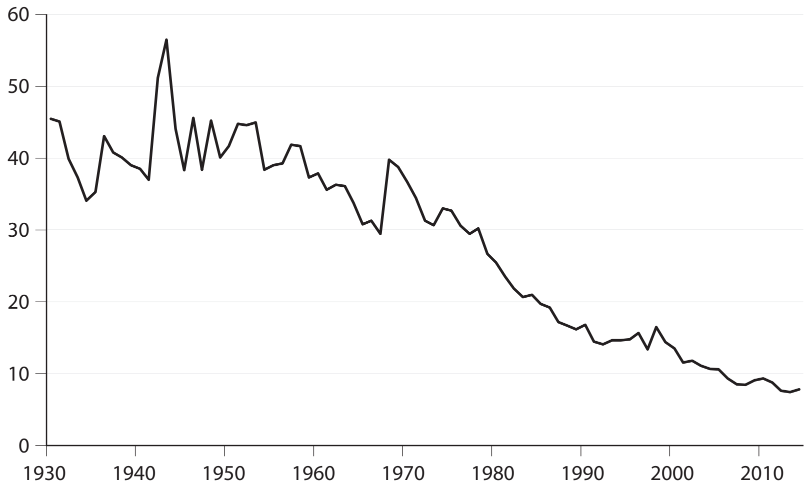

FIGURE 11.9. Share of Agriculture in GDP, 1930–2015 (in current prices and percent). Source: Based on national income accounts from Turkey, Turkish Statistical Institute 2014.

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Turkey was a relatively underpopulated country and had plenty of uncultivated land during the nineteenth century and until the 1960s. As a result, it was not very difficult or expensive to increase agricultural production until the 1970s. These increases in output ensured that agricultural output could grow faster than population and meet the increasing per capita demand for food and also account for a large share of total exports (figure 11.8). However, land and labor productivity increased rather slowly during that period (Pamuk 2008, pp. 375–96; Imrohoroglu, Imrohoroglu, and Murat Üngör 2014, pp. 998–1017). In the new era since 1980, the adoption of neoliberal policies, the pressure from international agencies, and the decline in the share of the agricultural population have combined to lead to the elimination of many of the government support programs for agriculture. Increases in the value of agricultural output slowed and began to lag behind population increases after 1980. With the introduction of more labor-intensive crops, however, total agricultural output began to increase once again in the last decade (figure 11.8). Share of agriculture in total employment declined from 50 percent in 1980 to less than 20 percent in 2015. Most of these men and women are employed as unpaid workers in the more than 3 million small and medium-sized family farms. Share of agriculture in GDP similarly declined from about 25 percent in 1980 to less than 8 percent in 2015 (figure 11.9). Average incomes in agriculture continued to remain well below those in the urban economy.

Spread of Industrialization after 1980 and Its Limits

Manufacturing employment and value added in Turkey expanded rapidly, at rates close to 9 percent per year during the 1960s and 1970s (tables 9.1 and 11.1; figures 11.10 and 11.11). The manufacturing sector had a number of important shortcomings, however. It remained inward-oriented, and exports of manufactures remained very low. Geographically, industry remained concentrated in the Istanbul region, and more generally, in the northwest corner of the country. The industrial elites of that era remained strongly dependent on the government, seeking subsidies and tariff protection. They were also opposed to economic integration with Europe for fear that they would not be able to compete with the products of European industry.

After the severe economic crisis at the end of the 1970s, more market- and export-oriented economic policies were adopted beginning in 1980. The balance sheet of Turkey's policies during the era of globalization is rather mixed, however. Perhaps the most successful aspect of the new policies was the drive for exports of manufactures. Total exports increased from less than $3 billion in 1980 to $13 billion in 1990, $28 billion in 2000, and $160 billion in 2015. This rise is in part due to the decline in the value of the dollar against other leading

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currencies, but it also reflects a major expansion in the volume of exports. The ratio of commodity exports to GDP rose from less than 3 percent in 1980 to 16 percent in 2010. The increase was achieved almost entirely because of exports of manufactured products. Share of manufactured goods in total exports rose from 35 percent in 1980 to more than 95 percent in 2010. Equally important, a large share of Turkey's exports were directed to the European Union during this period. The share of the EU in Turkey's total exports has been above 50 percent since 1980 (figures 11.1, 11.2, and 11.5).

These increases in exports of manufactures were accompanied by the rise of new industrial centers after 1980. Industrialization thus gained momentum in provinces like Tekirdağ, Kırklareli, Sakarya, Balıkesir, Eskişehir, Manisa, and Içel because of their proximity to the centers of the import-substitution period such as Istanbul, Bursa, Kocaeli, İzmir, and Adana. In addition, manufacturing value added, employment, and labor productivity also increased faster in the new industrial centers of Denizli, Konya, Kayseri, Gaziantep, Kahramanmaraş, and Malatya than in the centers of the earlier era (Filiztekin and Tunalı 1999, pp. 77–106). The share of these new centers in Turkey's manufacturing exports has also been rising, although it is not easy to determine their exports from the official statistics. Nonetheless, the rate of growth of manufacturing value added has remained below 6 percent per year in the era since 1980, distinctly lower than the earlier period.

The industrial enterprises in these emerging centers were mostly small to medium-sized family firms with limited capital. They began production in the low-technology and labor-intensive industries such as textiles and clothing, food processing, metal industries, wood products, furniture, and chemicals. From the early stages, they have taken advantage of the low wages to turn to exports in the new centers. They also have been been employing workers with little or no social security or health benefits while local and national governments looked the other way. Low technology, the emphasis on labor-intensive industries, and low wages were all reflected in the productivity levels. Labor productivity in manufacturing in the new districts remained below the averages not only for the more established industrial areas such as the Istanbul region but also below the averages for the country as a whole.

The small and medium-sized enterprises in the new districts relied mostly on their own capital and informal networks. They often did not borrow from banks but tended to grow primarily through the reinvestment of profits, which perhaps explains their resilience in the face of the recurring boom and bust cycles especially during the 1990s. With time, these companies became increasingly more conscious of the importance of new technology. The more succesful enterprises, especially the larger companies, have been attempting to produce higher technology goods by adopting more up-to-date

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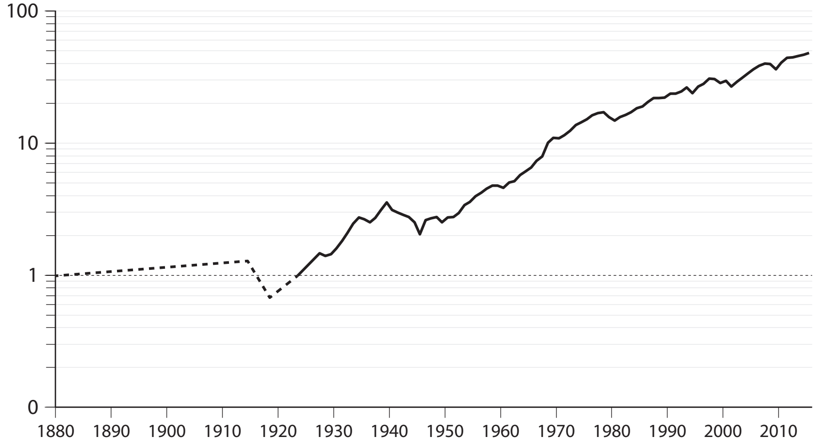

FIGURE 11.10. Manufacturing Value Added per Population in Turkey, 1880–2015 (index in constant prices; 1880 = 1,0). Source: Based on national income and population series discussed in chapter 2 for the Ottoman era; national income accounts from Turkey, Turkish Statistical Institute 2014 for the period since 1923.

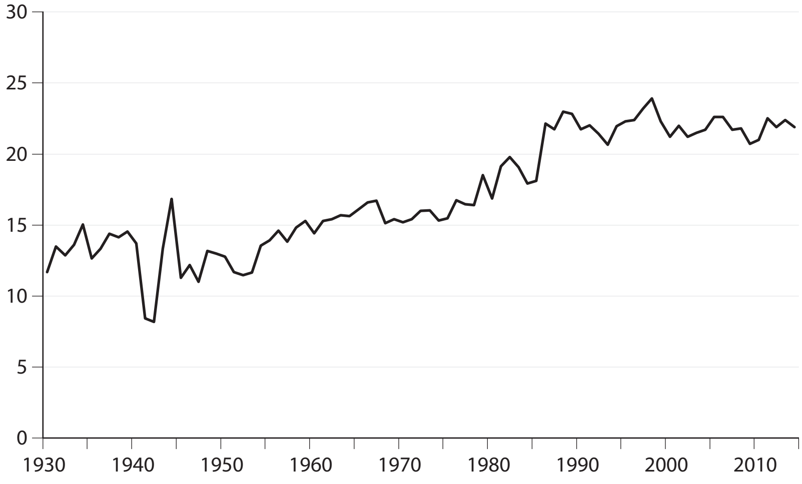

FIGURE 11.11. Share of Manufacturing Industry in GDP, 1930–2015 (in current prices and percent). Source: Based on national income accounts from Turkey, Turkish Statistical Institute 2014.

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technologies. The extent to which or how rapidly these firms would be able to move on to the production of goods with higher value added, making use of a better educated labor force with new skills and to achieve increases in labor productivity, remained a key question. Without significant increases in labor productivity and shift to goods with higher skill content and higher value added, these companies were soon forced to compete in the international markets, and even in the domestic market, with the manufactures from China and from other developing countries with lower wages.

The JDP governments after 2002 did not provide a new vision or develop long-term policies of support for these manufacturing enterprises. After the rapid economic recovery and export growth of the early years, the JDP governments led by prime minister and later president Erdoğan chose to focus on politics and consolidating their power. Creating a new stratum of businessmen close to the party became a leading goal of economic policy. For these political goals, greater emphasis on large scale housing and infrastructure projects seemed a more attractive alternative. The construction sector rather than manufacturing industry emerged as the most popular means for enriching the business groups close to the government and the party.

The limits of the new centers of manufacturing activity thus need to be emphasized as well. Three decades after the adoption of the new policies and greater export orientation of the economy, the new industrial centers remained limited in number, and their shares in the total industrial production, industrial employment, and exports have remained rather low compared to Istanbul and the Marmara region. In 2010, 64 of the top 100 companies and 360 of the top 1,000 companies in terms of sales were still located in the old industrial centers of the import-substitution period, such as Istanbul, Kocaeli, Bursa, Ankara, and İzmir. In contrast, only 7 of the top 100 companies and 120 of the top 1,000 companies were located in the new industrial centers. The rather slow rise of the new centers was also connected to the less than stellar performance of manufacturing in Turkey in recent decades. Turkey was also hurt in recent decades by what Dani Rodrik has called "premature deindustrialization," a tendency for manufacturing industry in developing countries to begin experiencing declining shares in employment and GDP at lower levels of GDP per capita than did today's developed countries decades earlier (Rodrik 2015). Share of value added of manufacturing industry in GDP in current prices rose above 20 percent for the first time in the 1980s but has not increased further, fluctuating around 22 percent since (figure 11.11). The term "Anatolian tigers" used frequently in the 1990s in connection with the new centers thus appears to be an exaggeration in retrospect. Nonetheless, the social and political implications of these new industrial centers deserve further attention.

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What a small number of Anatolian cities experienced in the decades after 1980 was a good example of industrial capitalism emerging in a predominantly rural and merchant society. The new industrialists were latecomers, both in their own regions and nationally. They were eager to establish themselves and take some power away from the earlier generation of business elites. In earlier years they had supported the Islamist parties led by Necmettin Erbakan, which were inward looking on economic issues and did not look beyond the Islamic world for international alliances. As Turkey's export-oriented industrialization proceeded and the customs union agreement established the EU as the leading market for Turkey's manufactures, their views began to change. After a group of politicians led by Recep Tayyip Erdogan broke off from Erbakan and moved to establish a new political party in 2001, the new industrialists offered critical support to JDP for its more moderate, outward-looking positions. The power of the big Istanbul industrialists was limited at the ballot box. In contrast, support coming from the owners and managers of small and medium enterprises from different corners of Anatolia proved to be more important on election day.

During its first term in office until 2007, JDP followed moderate policies and remained on track toward EU integration. It appeared friendly to large segments of the private sector and was supported by them in turn. Its export-oriented policies also received much-needed support across Anatolia from the business elites of these emerging regional centers. It thus appeared that an emerging middle class which benefited from globalization had played an important role in the rise of JDP as well as its market-oriented and pro-EU policies. Since 2007, however, both the political and the economic pictures have taken a turn for the worse. As the EU accession process ran into trouble and JDP moved to consolidate its power, few of the new or the old industralists or other businessmen raised their voices in response to the deterioration of the institutional environment and the rise of authoritarianism. Along with the stagnation in exports, share of manufacturing industry in GDP has continued to stagnate. The new industrial centers were also not able to make much progress toward higher-technology, higher value-added products.

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