ECONOMIC GROWTH AND STRUCTURAL CHANGE IN TURKEY 1960–88

After almost five decades of industrialization—characterized, on the one hand, by considerable state intervention and, on the other, by protectionist import-substituting policies in domestic capital formation—in the early 1980s Turkey ostensibly entered a new era of export-led economic growth. Since 1960, the Turkish democracy has experienced a series of crises with astonishingly regular ten-year cycles of recurrence. The 1980 military intervention, however, brought about a radical attempt to restructure the economy, hardly comparable with the rather gradual changes in its recent economic history. Its ten years of experimentation with economic liberalization and structural adjustment provide us today with an adequate record to identify and discuss at least the salient features of this period by comparing the performance of the economy in different years.

The purpose of the study is to offer a fairly general discussion of the patterns of development in Turkey between 1960 and 1988 by contrasting the 1960–80 period with the postliberalization era of the 1980s and analyze the dynamics of economic growth and the concomitant mutation the economy underwent during these years. It also strives to demonstrate that, despite some salutary effects, these liberalization attempts and structural adjustment policies failed to remedy some of the most important structural problems of the Turkish economy. We do not claim, however, to have captured the sociopolitical correlates of this complex transformation, nor to have given a *histoire raisonné* of this dichotomous period from an economic perspective. Much of the analysis elaborated in this study concentrates on the macro developmental aspects of the Turkish experience, without losing sight, insofar as possible, of the historical specificity of the underlying processes.

The article is organized as follows. The first section focuses on the 1960–78 import-substitution period and investigates the dynamics of growth and structural change by striving to identify the demand and supply side determinants of economic growth. The second section reviews the new developments in the Turkish economy in relation to the stabilization and structural adjustment programs introduced in 1980. The third section gives a brief evaluation of the results obtained in light of the continuing internal disequilibria and the drastic changes in the distribution
of income. Finally, the last section concludes with some remarks regarding the character of the post-1980 period and the salient features of the Turkish economy.

**IMPORT-SUBSTITUTING STRATEGIES AND ECONOMIC GROWTH, 1960–78**

After a period of postwar expansion, the Turkish economy showed sluggish growth and trade imbalances during the years between the mid-1950s and the beginning of the 1960s. Annual growth rates of industrial production averaged 4.3 percent in the second part of the 1950s, while that of agriculture remained only at 1.8 percent. Exports and imports fell below their 1953 levels and did not recover until 1960. It is during this period that comprehensive protectionist measures were introduced to overcome the persistent deficits in the balance of payments, together with price control programs to curtail inflation. Although the origin of strong state intervention in the economy dates back to the early 1930s, one can argue that a stronger orientation toward import-substituting development strategies and interventionist development programs generated a revival of interest in the stagnant economic conditions of this period, despite the official policy of the government that preached laissez-faire and free competition. In sharp contrast to the pre-1960 years, however, the 1960s enjoyed a vigorous economic recovery together with high growth rates in GNP. More specifically, the growth rates of GNP were 6.4 percent (1963–67), 6.7 percent (1968–72) and 7.2 percent (1973–77) during the three successive five-year-plan periods. These growth rates, compared to those of fifty-five countries that are within the same income category, appear to be higher than their overall average rate of 6 percent per annum.¹

With the implementation of the three five-year development plans, the economy continued to expand throughout this period, thanks to the unprecedented growth in the manufacturing and service sectors. The growth rate of agriculture, although relatively modest, stayed consistently above that of the population, with an average of 3.3 percent per annum. In the early 1970s, record high workers’ remittances (originating mostly from the Turkish guest workers in Germany) together with the aggressive investment plans of the government enabled the domestic output to keep on growing for a few more years, until the end of 1976, when the oil crisis threw the economy into a deep recession. Throughout the rest of the decade, Turkey struggled with severe balance of payments difficulties coupled with rising inflation. By the end of the 1970s, the Turkish economy found itself in a full-fledged economic crisis accompanied by political instability and social unrest.

Concomitant with these developments, the economy underwent a far-reaching transformation in its structure during the same period. While the share of agriculture in total output (at 1968 prices) declined from 38.4 percent in 1962 to 23.3 percent in 1977, that of the industrial sector (including manufacturing, mining, energy, and construction) rose rapidly from 22.3 percent to 31.5 percent.² Nevertheless, this economic expansion, it is argued, did not give rise to the “expected” outcomes, when the results obtained are compared to the international norms of the same period.³ First and foremost, the growth in manufacturing did not succeed in generating adequate employment opportunities to absorb the labor force released by the shrinking agricultural sector. Second, compared to other developing coun-
tries in the same income category, the share of agriculture in GNP continued to remain relatively high, which hampered the growth of total factor productivity. Third, in spite of this impressive growth record of output, the share of total gross savings in gross domestic product (GDP) at 1968 prices did not show any substantial improvement and remained stagnant throughout this period (see Table 1).

Fourth, international comparisons also reveal that exports remained well below those of other developing countries with similar characteristics. Last but not least, one should also point to the continuing dominance of the public sector over domestic industrial production throughout this period, despite all the incentive programs directed to the private sector.

During the 1960–78 period, two major and interrelated developments are discernible in the expansion of the Turkish economy. One is the impact of five-year development plans on industrialization and capital accumulation. The other is the end of the “easy” stage of import substitution and the beginning of its “complex” stage, characterized by the replacement of imported intermediate and capital goods, consumer durables, and the domestic production of related technologies. While much of Turkey’s economic growth in 1947–53 was made possible by a rapid expansion in agricultural production and exports under relatively liberal trade policies buttressed by the Korean boom, the main thrust of the planning years originated from inward-looking import-substituting programs that relied heavily on public investments in both manufacturing—through State Economic Enterprises (SEEs)—and infrastructure and resulted in a steady growth of domestic total demand.

On the foreign-trade front, however, the performance of the economy was far from impressive. Except for the 1971–74 period, during which the dollar value of total exports more than doubled, due to the 1970 devaluation of the Turkish lira (TL) and the accompanying export-promotion measures, the share of manufactured exports in total exports did not show any spectacular improvement. Between 1962 and 1970, it remained around 18 percent of total exports, whereas for the 1970–78 period it fluctuated around 32 percent. Finally, it should be mentioned that the 1963–70 period corresponded to a “positive” import substitution mostly financed by domestic savings, and the 1971–77 period can be defined as a “negative” import-substitution era, which gave rise to increasing current account deficits over time.

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**TABLE 1 Sectoral distribution of investments and savings**

<table>
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<tr>
<th></th>
<th>Growth Rates (%)</th>
<th>Shares in GDP at 1968 Prices (%)</th>
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<td>Total gross investment</td>
<td>8.5 7.2 15.3</td>
<td>15.8 17.4 17.9 26.1</td>
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<tr>
<td>Total gross savings</td>
<td>12.7 5.2 8.8</td>
<td>12.3 16.4 15.4 16.7</td>
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<tr>
<td>private</td>
<td>11.9 3.6 12.2</td>
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<tr>
<td>public</td>
<td>13.7 6.8 6.9</td>
<td>5.6 7.8 7.9 7.4</td>
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*Sources: State Institute of Statistics, State Planning Organization.*
### TABLE 2  Population and employment characteristics

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<tr>
<td>Total population (million)</td>
<td>28.9</td>
<td>32.7</td>
<td>37.1</td>
<td>42.0</td>
<td>2.5</td>
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<td>Active population (million) I</td>
<td>16.4</td>
<td>18.5</td>
<td>21.2</td>
<td>23.9</td>
<td>2.4</td>
<td>2.8</td>
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<td>Labor force (million) II</td>
<td>13.1</td>
<td>13.9</td>
<td>15.0</td>
<td>16.2</td>
<td>1.1</td>
<td>1.6</td>
<td>1.6</td>
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<td>Participation rate (% II/I)</td>
<td>80.1</td>
<td>75.0</td>
<td>70.6</td>
<td>67.7</td>
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<tr>
<td>Total employment (million)</td>
<td>12.6</td>
<td>13.2</td>
<td>13.9</td>
<td>14.7</td>
<td>0.9</td>
<td>1.0</td>
<td>1.1</td>
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<tr>
<td>in agriculture</td>
<td>1.4</td>
<td>1.7</td>
<td>2.0</td>
<td>2.2</td>
<td>4.0</td>
<td>3.3</td>
<td>1.9</td>
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<tr>
<td>Unemployment (million)</td>
<td>1.0</td>
<td>1.1</td>
<td>0.9</td>
<td>0.7</td>
<td>—</td>
<td>—</td>
<td>—</td>
</tr>
<tr>
<td>Unemployment rate (%)</td>
<td>11.1</td>
<td>12.1</td>
<td>13.3</td>
<td>13.1</td>
<td>—</td>
<td>—</td>
<td>—</td>
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<tr>
<td>Workers abroad (thousand)</td>
<td>13.0</td>
<td>204.0</td>
<td>634.0</td>
<td>815.0</td>
<td>73.4</td>
<td>25.5</td>
<td>5.2</td>
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Sources: State Institute of Statistics, State Planning Organization.

In order to investigate the contribution of different factors to economic growth, one can decompose the proportional increase in total value added by using a neoclassical aggregate-production-function approach. Based on the aggregate data for the 1963–75 period, the results obtained by Chenery et al. indicate that the growth rate of total aggregate output amounted to 6.4 percent and the rate of increase in capital and labor were 6.82 percent and 1.02 percent, respectively. While the share of capital in total aggregate output was 55 percent, that of labor stood at 45 percent. Finally, the rate of technological change was found to be 2.23 percent. These figures demonstrate that more than half of the 6.4 percent average annual growth rate of value added was due to capital accumulation. On the other hand, technological change accounts for almost one-third of the growth rate of output. The contribution of labor growth was the most modest one, which may seem to be paradoxical in view of high population growth rates in Turkey during this period. As we shall try to explain below, this situation is directly related to the emergence of a highly capital intensive manufacturing sector in the economy. In light of these findings, we can now turn to a more detailed analysis of these factors.

Since 1955, the average growth rate of population in Turkey has been approximately 2.5 percent per annum. This high and gradually rising growth rate of population was due to an increase in birth rates and a decrease in death rates, mainly as a result of improved nutrition and the diffusion of health facilities during these years. In spite of the family-planning programs introduced in the five-year plans, progress has been marginal in this area. Meanwhile, a very rapid rural–urban migration increased the urban population share from 18.8 percent in 1950 to over 40 percent by 1978. Table 2 summarizes the changes in population characteristics, labor force, and employment levels for the years 1962–77.

As can be observed from the figures in Table 2, the growth rate of the labor force has remained consistently below that of the economically active and total population. This can be explained by the rising proportion of the young, the rapid increase in the school population, and the growing number of workers emigrating abroad. Parallel to this rapid population growth, the sectoral distribution of the
labor force has undergone a radical change during the same years. As the proportion of the labor force in agriculture fell from 77 percent in 1962 to 61.8 percent in 1977, the corresponding share of the manufacturing sector rose from 7.2 percent to 11 percent and that of the service sector increased from 15.1 percent to 25.6 percent. Given the marginal character of most of the jobs created in the service sector (in terms of factor productivity growth), these results point to the fact that the growth in manufacturing has not been able to absorb the growing labor force in the economy.

The fact that structural and disguised unemployment remained quite high despite the rapid pace of industrialization can be partly explained by the relatively low growth rate in manufacturing, compared to that of some southern European countries such as Spain, Portugal, and Greece. Yet, the highly capital-intensive structure of Turkish manufacturing is a factor that cannot be discounted. Undoubtedly, high tariff and quota regimes, together with unrealistic exchange-rate and interest-rate policies, are the major causes behind this nonoptimal capital intensiveness of the manufacturing sector. This process is well epitomized by the following statistics: in 1976 constant prices, while a TL 373,000 investment per job was needed in the 1963-67 first five-year-plan period, this amount rose to TL 772,000 in the second five-year plan.

As to the accumulation of capital and investment patterns, one can distinguish two subperiods in 1963-79: the 1963-73 period, during which capital accumulation relied to a large extent on domestic savings; and the post-1974 period, when reliance on foreign financial resources increased substantially to continue to sustain economic growth. With the implementation of the first three five-year plans, the proportion of gross fixed investments in GNP rose rapidly from 15.8 percent in 1962 to 26.1 percent in 1977. However, while there has been some increase in gross domestic savings, their growth rates have remained consistently below those of investments, with the divergence between them becoming more pronounced toward the end of the 1970s. The sectoral distribution of investments and savings, as well as their growth rates, are given in Table 1.

The reasons behind these dismal saving ratios are complex. Suffice it to say here that their causes should be sought in the structure of income distribution and the characteristics of capital and assets markets together with the introverted nature of oligopolistic holding companies in Turkey. Furthermore, the analysis of the sectoral distribution of investments reveals that the manufacturing sector absorbed the largest portion of total investment, followed by the construction, transportation, and communications sectors. Meanwhile, investments in the areas of health and education showed a steady decline.

Moreover, in order to complete our discussion of the supply-side factors affecting economic growth, we must also consider the impact of technological change. Indeed, the introduction of new technologies into domestic production, skill deepening, and modern production-management techniques greatly contributed to productivity growth during these years. For instance, Krueger and Tuncer show that for the 1963-76 period, total factor productivity increased at an average rate of 2.10 percent per annum in various branches of manufacturing, the most successful ones being the tobacco, rubber, metal, and textile industries. An interesting result
that transpires from the same analysis pertains to the performance of the public sector. They found that total factor productivity growth in the public manufacturing sector was around 2.65 percent, whereas that of the private sector was only 1.84 percent. One can therefore argue that, despite their chronic deficits and losses, the public sector has made important contributions to productivity growth during these years.

Finally, another issue that should be addressed in this context is the nature of the import-substitution process. By the end of the mid-1960s, the "easy" stage of import substitution—during which the domestic production of most consumer nondurables and of their intermediate products was achieved utilizing mostly unskilled labor—came to an end. Because these products were mostly labor intensive and did not require large-scale production for efficient operations, they were well suited to the conditions in Turkey.\textsuperscript{14} Yet, in the 1970s the Turkish economy was already in the "complex" stage of import substitution where the domestic production of most consumer durables—which started in the mid-1960s in the form of so-called assembly industries—and the production of intermediate and capital goods was at stake. Because the production of these goods depends critically on the implementation of high technology and the use of highly skilled labor, the deficiencies in labor training, technology adaptation, and management had very strong negative effects on efficiency and productivity growth. Indeed, the sharp drop in total factor productivity growth from 3.2 percent (1963–67) to −1.18 percent (1973–76) in manufacturing is, beyond the oil-price shocks of this period, attributable to the characteristics of this new phase of import substitution. This period reveals as well the increasing dependence of domestic production and investment on imported intermediate and capital goods.

The industrialization process that gained momentum after the 1940s has also deeply affected the composition of domestic demand. As the proportion of manufactured goods in total demand continued to rise throughout these years, the share of foodstuffs in consumer products declined sharply. One also observes, during the same period, a steady expansion in the demand for investment goods, as well as the strengthening of sectoral interlinkages. A more careful examination of the statistics reveals that the increase in final demand has been the overwhelming force behind economic expansion. The decomposition results given in Table 3 also demonstrate that the contribution of exports to the growth of GNP was very modest at the beginning of the planning period and tended to increase between 1968 and 1973. The
impact of the oil crisis in 1974 is visible as well, in the abrupt decline of the effects of exports on output growth. Moreover, despite the heavy emphasis of the third five-year plan on import substitution in intermediate and capital goods, these figures shed light on the declining importance of import-substituting policies and appear to vindicate our contention that these policies became gradually ineffective in promoting the domestic production of consumer durables and investment goods (the second phase of import substitution).

In connection with the demand-side sources of economic growth, another point that needs to be stressed is the particular nature of the excess-capacity phenomenon and its relationship to economic growth. In fact, a casual look at the growth patterns in the Turkish economy is sufficient to reveal that the emergence and exhaustion of the excess capacity in infrastructure, as well as in manufacturing, is indeed at the very heart of the cyclical growth the economy has experienced since the late 1940s. Without going into the details, the story can be told, in a highly stylized fashion, in the following way.

In the course of the industrialization process, the state appears to be periodically compelled to initiate extensive investment projects in both infrastructure and key primary and intermediate products industries, which eventually give rise to the formation of excess capacity in the economy. Subsequently, due to expansionary policies, on the one hand, and to a certain extent to the existing favorable trade conditions, on the other, aggregate demand starts to rise and exhausts this excess capacity over time. Consequently, the boom periods often correspond to the years during which the excess capacity produced in previous years is being used up gradually, whereas the crises seem to emerge in the aftermath of the excess-capacity exhaustion. Meanwhile, the same phenomenon is observable in manufacturing. Independent of the fluctuations in domestic demand, there seems to exist an “autonomous” excess capacity in manufacturing that goes beyond optimal excess-capacity levels. It is possible to argue that there are two major reasons behind this maladjustment process. One is the relatively low domestic prices of imported capital goods, determined mostly by import-substituting policies. The second is the oligopolistic-monopolistic character of these industries. In this context, one can point to three key variables that determine simultaneously the relative prices of capital (investment) goods in Turkey: real effective exchange rates, import restrictions, and real interest rates. Under the fixed-exchange (multiple) rate regime, effective exchange rates applied to capital-goods imports declined steadily from the beginning of the 1950s onward. In the 1960s, by means of credit-rationing policies, selective credits were channeled to various branches in manufacturing with practically nonexistent or negative real lending rates. It is no wonder that during the 1963–76 period there was a 6.3 percent annual average increase in manpower utilization in the manufacturing sector, whereas the capital stock grew at an average rate of 12.8 percent per annum. This observation is particularly striking in view of the high unemployment and population growth rates that prevailed in the economy, which hindered any spectacular increase in per capita income.

Furthermore, from a microeconomic viewpoint, the existence of the excess capacity in manufacturing can be attributed to the oligopolistic-monopolistic structure of these markets. As is well known, since the level of production does not correspond to the minimum level of average cost, in such markets output is below
competitive levels and the price is above these levels, which gives rise to the buildup of unused capital stocks. It should be emphasized here that we are not talking about the classical version of the excess-capacity theorem that is applicable to monopolistically competitive markets. Rather, it is the small-group case concerning competition among a small number of oligopolistic firms that is relevant in the case of Turkey. Hence, the excess-capacity phenomenon is not about the existence of too many firms producing differentiated products but rather pertains to the behavior of oligopolistic firms that create more capital than they need for their own production—both as a barrier to entry and as a response to the aforementioned import-substituting policies.

CRISIS, STABILIZATION POLICIES, AND ECONOMIC RESTRUCTURING

The Turkish economy entered the 1970s with rapid growth, a current-account surplus, and a relatively high rate of inflation. Record-high workers' remittances together with increasing export revenues enabled the government to continue with its ambitious investment projects and rapid-growth targets. This performance was interrupted by the first oil crisis in 1974, but the reluctance of the government to adjust to the new international environment and to pass the deterioration in the terms of trade on to domestic prices of oil and other imported intermediate products created strong internal and external imbalances over the rest of the decade.

In the second part of the 1970s, Turkey had to resort to short-term foreign borrowing to finance current-account deficits in the face of falling workers' remittances and stagnant export proceeds. With rapidly declining exchange reserves, rising import bills, and debt-servicing payments, the Turkish economy was thrown into a full-fledged payments crisis, which brought about a total collapse of its credit worthiness in international markets.

From 1978 onward the government introduced a series of stabilization programs under the protection of the International Monetary Fund (IMF) that centered around various contractionary measures and export-promotion policies. Accordingly, the Turkish lira was devaluated twice (23% in March 1978 and 44% in June 1979), and stronger export-tax-rebate schemes were introduced to improve the trade balance. Moreover, some debt restructuring was achieved under the auspices of the Organization of Economic Cooperation and Development (OECD), and this was accompanied by a new syndicated loan. These stabilization and adjustment packages did not, however, succeed in reversing the declining performance of the economy. The growth of real GNP continued to decline and became negative during 1979–80. While inflation gathered momentum and reached an unprecedented triple-digit rate in 1980, unemployment soared to 14.8 percent. This economic crisis, compounded by political and social unrest, prepared the ground for the third military intervention in the history of the republic.

The stabilization and adjustment programs introduced on 24 January 1980, under the aegis of the IMF, the World Bank, and OECD were designed to curb inflation and circumvent the balance of payments difficulties in the short run and to restore equilibrium and economic growth in the long run. Financial assistance was provided by these international institutions as well as by bilateral donors, and hap-
pened to be one of the largest operations of its kind: between 1980 and 1985 the IMF made available $1.7 billion in special drawing rights (SDR) under a series of stand-by arrangements, and the World Bank extended $1.6 billion in structural adjustment loans. It is possible to argue that although initially these programs left an impression of déjà vu in Turkey, it shortly became apparent that these policies were aimed at achieving a radical break with the inward-looking, import-substituting development strategies of the past.16

A voluminous literature exists on the description of these policies.17 Therefore, it suffices here to say that most of these programs may be studied under the following four headings: (1) short-run stabilization packages aimed at curbing inflation and alleviating payments difficulties; (2) liberalization of the domestic-pricing mechanism; (3) rationalization of the public and financial sectors; and (4) promotion of exports and foreign trade in general. The developments in these four areas will be sketched seriatim.

As far as the stabilization programs are concerned, these policies sought to curb inflation and remedy-payments difficulties by eliminating the excess demand in domestic markets, which is consistent with the spirit of orthodox IMF anti-inflationary measures. In practice, this implied a drastic reduction in the Central Bank credits extended to the public sector, hence a sudden drop in public investments and spending. During the initial years of the program, contractionary demand-management policies depended heavily on monetary programs. Since the use of open-market operations is limited by the lack of developed money and capital markets in Turkey, these contractionary programs had to rely on credit reduction and interest-management operations. Accordingly, as Central Bank discount rates as well as reserve requirements on time and sight deposits were adjusted upward, interest rates were deregulated to arrest financial disintermediation, which emerged as a result of negative real interest rates.18

To strengthen the anti-inflationary effects of these fiscal and monetary measures, further steps were taken to introduce various comprehensive structural reforms into commodity and factor markets. Consequently, in 1980 private-sector prices were freed and those of basic commodities and services provided by state monopolies and SEEs were substantially adjusted upward. Agricultural subsidies were reduced and support lists were redefined. Yet, similar liberalization attempts did not follow in the reorganization of the labor markets. Instead, the military rule banned a large section of the trade-union movement and established the High Arbitration Council (Yüksek Hakem Kurulu) to handle most wage determinations and labor disputes.19 As a result of these policies and the continuing inflation, real wages declined from TL 100 in 1979 to TL 74.0 in 1985, and unemployment soared to 16.3 percent in 1985 in the face of this economic contraction.

The most comprehensive and probably the most radical steps have been taken in the foreign-trade sector of the economy, and they have been quite instrumental in promoting exports and hence alleviating current-account deficits. Ostensibly, these efforts also marked the end of inward-looking development strategies and the beginning of export-led growth. The major developments in this period can be summarized under two categories: first, reforms and programs aimed at trade liberalization and export promotion; second, the concomitant exchange-rate policies
directed at restoring external equilibrium and expenditure switching. As a first step toward dismantling the existing trade restrictions, the quota list was abolished in January 1981; advanced-deposit requirements on industrial imports were reduced, and tariff exemptions on imported intermediate products were granted. Furthermore, in an effort to promote exports, export credits were introduced and export-licensing requirements were eliminated. Yet, with the growing practice of the "fictitious exports" (i.e., over invoicing), export credits were ended in 1984 and were replaced by direct subsidies in 1985. Indeed, the Turkish export miracle owed much to the active exchange-rate policies of this period. After a 33 percent nominal devaluation of the Turkish lira in 1980, multiple-exchange rates were abolished and a flexible-exchange-rate regime was established. In 1984, commercial banks were allowed to determine their exchange rates within certain limits set by the Central Bank. Finally, in August 1988 exchange-rate determination was totally left to market forces by means of the newly established Foreign-Exchange Market.

THE POSTLIBERALIZATION ERA

From the debt crisis, which has plagued much of the Third World since the early 1980s, Turkey has emerged as the "paragon of export-led growth" and an inspiring example of stabilization and liberalization. In sharp contrast to Latin American countries, its rapid convalescence made it possible to restore its credit worthiness in international markets and regain relatively high growth rates. In the words of one economist, Turkey presented "the single most important case of a 'life after debt'." After more than a decade of economic stabilization and structural adjustment, however, it is possible to argue that the results of these programs left much to be desired. Some of the most relevant statistics describing the performance of the Turkish economy during the 1979–88 period are given in Table 4.

The reduction of inflation from its peak rate of 104 percent in 1980 to 28 percent in two years, the restoration of positive growth rates, the elimination of foreign-exchange bottlenecks, and especially the unprecedented growth in exports are, without doubt, remarkable results that deserve much praise in appreciating the effects of these programs. Yet, an objective evaluation of these policies would be incomplete without taking into account the overall performance of the economy in other areas as well.

First, as can be observed from the growth rates of GNP in Table 4, this success story ought to be qualified in a number of ways. It is true that economic growth owed much to these policies in the aftermath of the payments crisis: from 1981 onward, the growth rate of real GNP increased steadily and reached a peak value of 8.1 in 1986, declining later to 4.1 in 1988. However, one should also note that for the 1980–88 period, the average annual growth rate has been 4.61 percent, which is well below rates observed between 1963 and 1972 (6.6%) and those during the 1972–77 period (7.2%). Indeed, the post-1980 growth rates should be viewed in the context of the worldwide stagflation of this period and should be contrasted with the failure of many Latin American economies that, despite similar attempts, have not succeeded in arresting sharp declines in their GNPs. Yet, one should be reminded of the fact that none of these countries benefited from external financial
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<td>3.3</td>
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<td>5.1</td>
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<td>Implicit GNP deflator(^a)</td>
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<td>40.5</td>
<td>46.8</td>
<td>45.0</td>
<td>36.9</td>
<td>34.2</td>
<td>74.7</td>
</tr>
<tr>
<td>CB credits to public sector(^a)</td>
<td>72.6</td>
<td>71.0</td>
<td>35.2</td>
<td>5.5</td>
<td>12.8</td>
<td>-4.1</td>
<td>62.1</td>
<td>38.0</td>
<td>71.4</td>
<td>45.9</td>
</tr>
<tr>
<td>Tax revenue(^c)</td>
<td>18.4</td>
<td>16.9</td>
<td>18.1</td>
<td>17.9</td>
<td>16.7</td>
<td>12.9</td>
<td>13.8</td>
<td>15.2</td>
<td>15.5</td>
<td>13.9</td>
</tr>
<tr>
<td>Merchandise exports(^c)</td>
<td>2.3</td>
<td>2.9</td>
<td>4.7</td>
<td>5.7</td>
<td>5.7</td>
<td>7.1</td>
<td>7.9</td>
<td>7.5</td>
<td>10.2</td>
<td>11.7</td>
</tr>
<tr>
<td>External debt at year end(^d)</td>
<td>15.8</td>
<td>16.2</td>
<td>16.9</td>
<td>17.6</td>
<td>18.4</td>
<td>21.3</td>
<td>25.3</td>
<td>31.2</td>
<td>38.3</td>
<td>37.7</td>
</tr>
<tr>
<td>Real wage index(^e)</td>
<td>100.0</td>
<td>68.8</td>
<td>79.5</td>
<td>75.0</td>
<td>79.7</td>
<td>78.5</td>
<td>74.0</td>
<td>75.9</td>
<td>67.8</td>
<td>56.9</td>
</tr>
<tr>
<td>Unemployment rate(^f)</td>
<td>13.6</td>
<td>14.8</td>
<td>15.2</td>
<td>15.6</td>
<td>16.1</td>
<td>16.1</td>
<td>16.3</td>
<td>15.8</td>
<td>15.2</td>
<td>14.4</td>
</tr>
</tbody>
</table>


Notes: \(^a\)Annual percentage change; \(^b\)after tax six-month time deposit rate; \(^c\)percentage of GNP; \(^d\)in billions of U.S. dollars; \(^e\)based on the Social Security Institute data and Consumer Price Indices; \(^f\)percentage of domestic civilian labor force.
supports commensurate with the ones Turkey managed to receive during this period. It seems therefore fair to calibrate the growth performance of the Turkish economy by saying that it has been a success relative to the failure of other debt-ridden developing economies. It is also important to recognize that external financial support played a crucial role in pulling the economy from the acute payment crisis. In addition, another point that needs to be addressed is the nature and determinants of growth in this period. The growth success of Turkey in the post-stabilization era is due mainly to the reduction of consumption and the shift of government expenditure from public consumption to investment. In other words, in contrast to other high-debt countries, in the aftermath of the debt crisis Turkey adopted a growth-oriented debt strategy rather than relying on sustained high surpluses in the noninterest account to keep the debt–output ratio under control. In fact, the estimation results of Anand, Chhibber, and van Wijnbergen demonstrate that the government, by reducing consumption, succeeded in maintaining output growth at the expense of external targets and that public investment has played an important role in the strong-growth performance of the economy. It is therefore possible to argue that, despite various privatization and liberalization attempts, the role of the public sector did not wither in the post-1980 period.

Second, although impressive by any standard at the beginning of the crisis period, these anti-inflationary policies did not fare well during the rest of the decade. From 1981 to 1988 the average rate of inflation (the rate of change in the implicit GNP deflator) remained around 40.5 percent per annum and once again accelerated during 1988. What are the reasons behind this failure? How should one tackle the problem of sustained inflation in the face of relatively contractionary policies? Although the determinants of inflation change over time and its analysis is far from being facile, it can be briefly pointed out that, in general, the failure of these policies stems from a neglect of the supply-side effects of these programs and to a certain extent from the insistence on a strict monetarist explanation of inflation that tautologically blames it on the growth in nominal money balances. Recent economic research shows that contractionary policies may fuel rather than dampen inflationary tendencies. For instance, restrictive monetary policies and devaluations may increase the price level while decreasing output, hence triggering a stagflationary process in a developing economy. In other words, inflation cannot be curbed by reducing the growth rate of the money supply and the value of the Turkish lira vis-à-vis other foreign currencies. In the absence of well-developed capital markets, long-term investment plans of domestic firms depend critically on the availability of official and private bank credits, which are bound to decline as a result of contractionary monetary policies. On the other hand, due to the strong import dependence of the manufacturing sector, depreciation of the Turkish lira tends to increase the domestic cost of imported inputs, which in turn validates the price hikes in manufacturing, thereby contributing to overall inflation.

Moreover, casual empiricism suggests that even the relationship between aggregate demand and inflation is far from being direct. In fact, after a peak rate of 60 percent (consumer price index) in 1985, inflation slowed down gradually until 1987. During the same period, however, domestic demand was continuously increasing. In this context, one can point to the price structure of Turkish manufacturing to better understand the dynamics of inflation in Turkey. Clearly, the
estimation results of the following equations demonstrate that price increases in this sector are particularly sensitive to the changes in imported input prices, the variations in the supply of industrial credits, as well as the capacity-utilization levels.

\[
\frac{\dot{p}_t}{P_t} = .4259 + .4347 \left( \frac{\dot{W}}{W} \right) + .3316 \left( \frac{\text{PMTL}}{\text{PMTL}} \right) - .4050 \ CUI - .4156 \left( \frac{\text{CRS}}{\text{CRS}} \right)
\]

\[
R^2 = .8905 \quad DW = 1.557
\]  

\[
CUI = -.0541 + .9580 \left( \frac{\text{MINT} \times \text{EXRM}/\text{PMTL}}{\text{KI}} \right) + .1190 \left( \frac{\text{YD}}{\text{KI}} \right)
\]

\[
R^2 = .7372 \quad DW = 1.07
\]  

In Equation 1, \( \frac{\dot{p}_t}{P_t} \) denotes the proportional rate of change in the price index for manufacturing; \( \left( \frac{\dot{W}}{W} \right) \), \( \left( \frac{\text{PMTL}}{\text{PMTL}} \right) \), and \( \left( \frac{\text{CRS}}{\text{CRS}} \right) \) are, respectively, the proportional rates of change in wages, the domestic price index for imported inputs, and the supply of industrial credits. \( CUI \) is the capacity-utilization index for the manufacturing sector. In Equation 2 \( \text{MINT} \) and \( \text{EXRM} \) stand for, respectively, the imports of intermediate products in \$U.S. and the average nominal-exchange rate for manufactured goods (TL/$). The numerator of the first ratio in Equation 2 simply gives the real value of imported intermediate goods in Turkish lira. \( \text{YD} \) and \( \text{KI} \) denote disposable private national income and the fixed-capital stock in manufacturing. The figures in parentheses are the \( t \) statistics.25

In light of these estimations, one can argue that imported input prices as well as capacity-utilization levels and the availability of credits strongly determine the price variations in the manufacturing sector. It is also important to note that the level of capacity utilization is negatively related to price increases. This is explained by Equation 2, which demonstrates that the capacity-utilization index is more strongly influenced by the availability of imported intermediate products than by domestic-demand pressures.

In addition to these results, the decomposition analysis of Conway shows that, for the 1980–83 period, devaluation alone contributed to inflation by an average of 58.4 percent in Turkey. For the whole 1973–83 period, increases in imported input prices, external inflation, and devaluation appear to explain as much as 63.2 percent of the rate of inflation.26 Consequently, it is not possible to ignore the impact of those stabilization policies on the price level.

Furthermore, another subject pertinent to the discussion of inflation in Turkey is the rationalization and performance of SEEs. The prices of various final and intermediate products produced by the SEEs have been adjusted in an effort to rationalize production and eliminate losses. This would reduce the burden of SEEs on the government budget and hence alleviate the pressure on the Central Bank to finance the deficit through money creation. However, since many of the SEE products are intermediate goods used by public and private firms in manufacturing, these price hikes affect the price level in this sector and therefore contribute to inflation in general. We should parenthetically point out here that, abstracting from
the intricacies of public-enterprise economics, it may be rational to determine the output prices on the basis of the cost of production and productivity. Yet, it is also true that efficiency cannot be achieved through mere price adjustments in a monopolistic market. In other words, without changing the micro structure of SEEs, it is not possible to attain high efficiency and the optimal allocation of resources.

A thorough analysis of inflation in Turkey that also incorporates its political economy is more complex and goes beyond the confines of the cursory discussion given earlier. For instance, the inflation tax on domestic-currency holdings is a major source of government revenue and hence cannot be omitted in the investigation of the determinants of sustained inflation. This point is particularly important in view of the growing debt burden that requires new sources of financing. On the other hand, there is (perhaps paradoxically) the counterpressure of the IMF that requires the borrowing countries to reduce inflation to enhance their repayment capacity. The opposition (or support) of different social strata to the persistence of sustained inflation—with its effects on the domestic terms of trade and the redistribution of income—is another dimension that should be taken into account.

Probably the most spectacular results of the liberalization programs have been in the area of foreign trade. During the 1980s, Turkey witnessed an unprecedented export boom by international and domestic standards whereby total exports rose rapidly from $2.9 billion in 1980 to $11.7 billion by the end of 1988. This was accompanied by a drastic change in the composition of exports: in five years, the share of manufactured products in total exports increased from 36 percent in 1980 to 80 percent by the end of 1985. Apparently, a number of factors contributed to this export drive: the fast depreciation of the Turkish lira, various export incentives in the form of tax rebates and direct export credits, the Iran–Iraq war, and, finally, the sudden drop in domestic demand. Whether there really was an export “miracle” and, if so, which of these factors has been the most important driving force behind this miracle has been a matter of debate among economists. Some economists have attributed this export boom to the liberal use of export incentives. Others have drawn attention to Turkey’s exchange-rate policy. For instance, Celasun and Rodrik argue that Turkey’s export success had little to do with either the incentive regime or exchange-rate policy, but was mostly a consequence of its geographical location and the Iraq–Iran war. Arslan and van Wijnbergen, on the other hand, hold the view that this export boom can be explained by the trade reforms and the macroeconomic policies Turkey followed during this period. Nonetheless, one point is now clear: Turkey has not yet succeeded in penetrating into the world export markets as, for instance, Taiwan and Korea did in the 1960s and 1970s. In fact, the share of Turkish exports in the total exports of non-oil developing countries to industrialized economies increased from 1.1 percent in 1977 to only 1.6 percent in 1988.

There exists a vast literature on the nature and possibility of export-led growth in developing economies. In the case of Turkey, given the overwhelming impact of domestic demand on economic growth, among other things, one has every reason to have mixed feelings about the euphoria of export-led growth. In this context, Yeldan’s CGE (Computable General Equilibrium) analysis demonstrates that Turkey can achieve a superior growth performance over the export-led growth
strategy by adopting a program based on domestic demand and sectoral interlinkage promotion policies.31

Another important point that should be addressed in this context is the impact of these stabilization and liberalization programs on the distribution of income. Not only did these policies not succeed in bringing about any improvement in terms of income distribution, they made it even worse by reducing both the share of wage earners and the agricultural sector in national income by almost 50 percent in just eight years. While the results of various studies reveal that the personal distribution of income did not substantially worsen in Turkey during this period (see, e.g., the CGE model estimations of Celasun32), the total collapse of wages and salaries caused the functional distribution of income to deteriorate rapidly in the course of these years. Table 5 summarizes this trend in the distribution of income in Turkey between 1975 and 1988. As one can observe from these estimates from 1978 to 1988, while the share of profits and rental income rose from 38.15 percent to an unprecedented level of 70.2 percent, that of wages and salaries declined from 35.19 percent to 14.00 percent. A similar collapse can be seen in the share of the agricultural sector.33 Apart from the equity and welfare implications of this state of affairs, it is possible to argue that the worsening of income distribution will further render any future improvement in domestic savings impossible, a factor crucial for any prospective balanced growth of the Turkey economy.34

Finally, another new development that needs to be taken into account in evaluating the performance of the Turkish economy in the post-1980 period is the growing external debt. In spite of the export boom and the improvement of the current account, external debt continued to grow and reached $37.7 billion in 1988, or 53 percent of GNP. What is at stake here is not so much the potential risks associated

<table>
<thead>
<tr>
<th>Year</th>
<th>Profits and Rental Income</th>
<th>Wages</th>
<th>Agriculture</th>
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<tr>
<td>1975</td>
<td>37.73</td>
<td>31.51</td>
<td>30.76</td>
</tr>
<tr>
<td>1976</td>
<td>35.60</td>
<td>33.11</td>
<td>31.28</td>
</tr>
<tr>
<td>1977</td>
<td>34.07</td>
<td>36.81</td>
<td>29.12</td>
</tr>
<tr>
<td>1978</td>
<td>38.15</td>
<td>35.19</td>
<td>26.66</td>
</tr>
<tr>
<td>1979</td>
<td>42.88</td>
<td>32.79</td>
<td>24.33</td>
</tr>
<tr>
<td>1980</td>
<td>49.47</td>
<td>26.66</td>
<td>23.87</td>
</tr>
<tr>
<td>1981</td>
<td>52.15</td>
<td>24.68</td>
<td>23.17</td>
</tr>
<tr>
<td>1982</td>
<td>53.65</td>
<td>24.56</td>
<td>21.79</td>
</tr>
<tr>
<td>1983</td>
<td>54.69</td>
<td>24.78</td>
<td>20.52</td>
</tr>
<tr>
<td>1984</td>
<td>57.99</td>
<td>21.57</td>
<td>20.44</td>
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<tr>
<td>1985</td>
<td>62.02</td>
<td>18.84</td>
<td>19.08</td>
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<tr>
<td>1986</td>
<td>64.21</td>
<td>17.70</td>
<td>18.09</td>
</tr>
<tr>
<td>1987</td>
<td>65.40</td>
<td>17.00</td>
<td>17.60</td>
</tr>
<tr>
<td>1988</td>
<td>70.20</td>
<td>14.00</td>
<td>15.80</td>
</tr>
</tbody>
</table>

with short-run illiquidity or insolvency of the economy—at present, the secondary market quotation of Turkey’s debt does not seem to threaten its credit worthiness—but its repercussions in the domestic markets. First, there is the equity question. The recent experience of Latin American countries indicates that, in addition to exchange-rate adjustments, real-wage cuts in debtor countries are needed to assure trade surpluses and dollars earnings necessary to service foreign debt. The rapid deterioration of the functional distribution of income since 1980 (Table 5) demonstrates that indeed Turkey has been no exception to this rule. Second, there is the problem of inflation. In the face of growing internal and external debt, the inflation tax may become an attractive source of revenue for the government, which may erode the incentives to arrest inflation. Third, the existence of growing foreign debt makes domestic markets extremely sensitive to the external performance of the economy, namely the control of imports and the promotion of export growth. With regard to exports, the problem stems from the fact that the depression of domestic demand—to create the necessary surplus for foreign markets—becomes more difficult during a recovery period, and hence requires further steps toward export promotion. Given the ambiguous results as to the nature and the determinants of the recent export boom, it is not clear whether Turkey can afford enhancing its export capacity without jeopardizing its domestic equilibrium.

CONCLUSION

We have attempted in this study to give an overview of the patterns of economic growth and structural change in Turkey between 1960 and 1980 by contrasting the import-substitution era of the 1960s and 1970s with the export-led growth orientation of the post-1980s period. Some tentative conclusions can now be drawn as to the development prospects for the Turkish economy. First, the brief analysis of the sources of growth during the 1960s and 1970s revealed that domestic demand was indeed the most important driving force behind economic growth. Therefore, given the structural characteristics of the Turkish economy, it is not possible to discount the importance of domestic markets in terms of growth and get on the bandwagon of export-led development. This, of course, neither implies a plea for a return to export-discriminating policies nor a defense of neomercantilism. A more carefully designed long-term capital-formation program that emphasizes the sectoral interlinkages and domestic demand is needed in Turkey under current conditions.

Second, it should be recognized that in an economy integrated into the world markets, as the Turkish economy is, it is not possible to ignore the repercussions of external economic conditions and therefore avoid the necessary internal adjustments indefinitely. Both the recent maladjustments during the second phase of import substitution and the ensuing debt crisis have demonstrated that the need for necessary adjustment policies in the economy is crucial for the long-term growth prospects of the country. Third, in spite of all incentive programs adopted by the government, the private sector did not show much responsiveness to new investments and domestic-capital formation. Consequently, despite concerted efforts to dismantle the public sector, its decisive position remains almost as powerful as
ever in the economy—so much so that the label frequently used to depict the post-1980s developments such as “free-market orientation” becomes rather meaningless in terms of putting them into a historical perspective. (Needless to say, this is due to the sociopolitical and historical characteristics of the state and the entrepreneurial classes in Turkey.) This should not be construed as contending that nothing has changed and that plus ça change, plus c’est la même chose, but rather emphasizes our view that, given the stubborn nature of the underlying institutions, it is too early to characterize this period as a historically distinct phase of capitalist development in Turkey.

Finally, in closing we should point to a number of recent developments in the Middle East and the world economy that may strongly affect the performance of the Turkish economy in the 1990s. One such development concerns the new export markets and investment opportunities that have emerged as a result of the demise of the Soviet Union and other neighboring socialist economies. Because of its proximity to these countries and its export structure, Turkey may greatly benefit from this new environment. This may also alleviate the export losses incurred by Turkey as a result of the Gulf War. Moreover, the emergence of independent Turkic states in the former Soviet Union is already giving rise to closer economic cooperation between these countries and Turkey. Also, in the longer run, full membership in the European Economic Community, however remote it might be, offers another challenge to the Turkish economy. Yet, the expansionary effects of these new circumstances may be counterbalanced, on the one hand, by the deepening of the mild recession that has started to affect the industrialized economies since the beginning of 1990, and, on the other hand, by the intensification of protectionist sentiments in the United States and in some European countries.

NOTES

2Ibid., 2.
4These five-year development plans, their various shortcomings notwithstanding, should be contrasted with the previous planning programs that were, for the most part, motivated by short-term policy responses to existing internal and external economic conditions, devoid of any long-term view of industrialization. For an in-depth analysis of these five-year plans, see M. Durdağ, Some Problems of Development Financing (Dordrecht: D. Reidel Publishing Co., 1973); E. Güнце, “Türkiye’de Planlama’nın Dünü, Bugünü, Yarını,” ODTÜ Gelişme Dergisi, Özel sayı (1981): 117–32.
The growth rate of total output (value added) $\frac{\dot{Q}}{Q}$ can be written as

$$\frac{\dot{Q}}{Q} = \frac{A}{A} + \epsilon K K + \epsilon L L,$$

where $\frac{A}{A}$ denotes the rate of technological change, $\frac{K}{K}$ and $\frac{L}{L}$ are the rates of increase in capital and labor inputs, respectively; $\epsilon K$ and $\epsilon L$ are the share of capital and labor in total output. Using the aggregate data for the 1963–75 period, the following results (%) are obtained: $\frac{\dot{Q}}{Q} = 6.4, \frac{K}{K} = 6.82, \frac{L}{L} = 1.02, \epsilon K = 55, \epsilon L = 45, \frac{A}{A} = 2.23$. See H. D. Chenery, S. Robinson, and M. Syrquin, Industrialization and Growth (London: Oxford University Press, 1986), 22.

These percentages do not add up to 100.0 because the mining and energy sectors are left out; see various publications of the State Institute of Statistics and the State Planning Organization.


World Bank, Turkey: Policies and Prospects, 129.

Given the nature of our discussion, we cannot go into a detailed analysis of these intricate issues here. For a more in-depth discussion, see A. A. Çeçen, A. A. Doğruel, and F. Doğruel, Türkiye de Ekonomik Büyüme, Yapısal Değişim ve Kriz (İstanbul: Egemen Y., 1990); L. Rittenberg, “Financial Liberalization and Savings in Turkey,” in Liberalization in the Turkish Economy, ed. T. Nas and M. Odekon (New York: Greenwood Press, 1988), 115–27.


World Bank, Turkey: Policies and Prospects.

For a detailed discussion of the incentive structure and protectionist measures in Turkish manufacturing, see F. Yaşıcı, Protection and Incentives in Turkish Manufacturing (Washington, D.C.: World Bank Staff Working Paper, 1984). Krueger, on the other hand, argues that excess capacity in manufacturing could be the result of firms' deliberate overexpansion; Foreign Trade Regimes, 230.


For a more detailed discussion of these financial reforms, see G. Kopits, Structural Reform, Stabilization and Growth in Turkey (Washington, D.C.: IMF, 1987).

Wage determinations by the council were mandatory for the public sector and were used as guidelines in the private sector. However, in the face of growing labor unrest, the role of the council declined and collective bargaining was liberalized somewhat after 1987.

For a detailed discussion of the determinants of exports during this period, see D. Rodrik, “External Debt and Economic Performance in Turkey,” in Liberalization in the Turkish Economy, 161–85, esp. 175–80. For an analysis and description of export-incentive programs, see B. Milanovic, Export Incentives and Turkish Manufactured Exports, 1980–84 (Washington, D.C.: World Bank Staff Working Paper, 1986); according to Milanovic, the efficiency of the export-incentive policy, measured by its deviation from the optimal structure, did not show any significant improvement in the period 1980–84, but exchange-rate adjustment was correct.
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23Ibid.; Anand et al. go on to suggest that “[these results] show that stabilization programs relying on reductions of public sector investment will have high and permanent negative output effects . . .”. They also emphasize the fact that the key factor in this growth performance was the substantial excess capacity inherited from heavy investments made in the 1970s, which is very much in line with our discussion of the historic nature of excess capacity.


25These equations are part of the 45-equation macroeconometric model estimated for the Turkish economy for the 1963–85 period, using three-stage least-square estimation techniques. For a more complete discussion of the determinants of inflation and the underlying structural rigidities, see Çeçen et al., Türkiye'de Ekonomik Büyüme, section 5.


29Kopits, Structural Reform, Table 2.


ing that keep bank stockholders in the black. One might argue (or even believe) that this is essential to maintain order in the international financial system, but that raises the question of in whose interest the system works. For many who are paying the bill now, there have been few benefits before and there are no obvious ones down the road” (533).

36We are not claiming here that this is indeed the actual state of affairs in Turkey. This question should be empirically analyzed beyond theoretical possibility and anecdotal evidence.