

**POLITICS WITHIN THE STATE:  
INSTITUTIONS AND DILEMMAS OF TURKISH PRIVATIZATION  
IN COMPARATIVE PERSPECTIVE**

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*Based on a critical examination of Turkey's privatization experience during the 1990s from a comparative perspective, the study attempts to confront the larger question of why some countries have been quite successful in undertaking large-scale privatization, while others have not. Three central and interrelated influences are highlighted in this context, namely the strength and coherence of the executive authority, the depth of the economic and political crises experienced prior to the implementation of the privatization program and the nature of the external environment. Special attention is directed towards a key new institution, the Turkish Privatization Administration, the underlying logic of which is very much along the lines of similar highly centralized institutions designed in Latin American countries dominated by presidential styles of decision making. The Turkish experience testifies, however, that such institutions are unable to perform successfully in political environments, characterized by fragmented party systems and weak executive authority, at least in the absence of a major fiscal crisis of the state and resultant pressures from the international community in the direction of large-scale privatization and reform.*

Privatization has emerged as a key element of the Turkish neoliberal experiment in the 1980s designed to accomplish successful integration into the world economy. The privatization component of the brought neo-liberal strategy focused on increasing efficiency, reducing the burden of the state economic enterprises (SEEs) on the government budget and widening property ownership. In retrospect, however, we observe a paradox. Although the privatization process in Turkey had started earlier than in most developing countries, its achievements to date, at least measured in terms of the size of divestiture, have been limited compared with the principal Latin American and Eastern European cases. Between the starting point of the program in 1986 and August 2000 total proceeds of the Turkish privatization program have amounted to US \$7.1 billion 2.5 billion of which has been generated in the year 2000. This figure represents a considerably lower magnitude in comparison with the two major Latin American experiments involving hyperprivatization, namely the Mexican experience under Salinas and the Argentinean experience during the presidency of Carlos Menem (1).

Obviously, in measuring the performance of a privatization program, the size of divestiture does not constitute the sole criterion of judgement. In fact, a case of hyperprivatization, involving a massive sale of public assets to the private sector over a short period of time may not necessarily be welfare enhancing privatization. Mass privatization or hyperprivatization may fail to increase social welfare if public enterprises are disposed of at significantly less than their true market values or if public monopolies are transferred to the private sector in the absence of adequate regulation. With these reservations in mind, we hypothesize that the Turkish experience to date is characterized, with certain notable exceptional cases, by limited achievement, in terms of both the scale of the program implemented and the degree of realization of the basic efficiency objective. The Turkish privatization program has mainly involved the divestiture of relatively small and medium-scale public enterprises until the realization of a large privatization in 2000. A focal point of the program has been the privatization of public enterprises in tradeable goods sectors, notably the cement industry. One may discern the importance of the privatization of cement factories by examining the overall revenues generated via the sale of the enterprises concerned. Privatization of twenty-nine factories has been accomplished with sales revenues amounting to almost US \$ 1 billion, a figure that corresponds to around 13.5 percent of the total privatization proceeds as of August 2000. Although the privatization of large-scale public enterprises has been continuously on the agenda, it has not been possible to translate the rhetoric into actual or effective implementation until the year 2000. Indeed, there have been cases where, in the context of large enterprises, only minority shares of the company have been transferred to the private sector. These sales may be important in terms of magnitude, but do not provide a sufficient basis for a radical restructuring of managerial incentives needed to improve corporate efficiency.

The objective of the paper is to explain the puzzle of why the Turkish privatization experiment has been so protracted and limited in scope, at least until very recently, compared with both the relative achievements of the neoliberal program in Turkey in several other respects, notably in the fields of trade and capital account liberalization and the privatization records of other "emerging markets"(2). The paper also attempts to account for the recent resurgence of privatization in Turkey from a comparative perspective, the Turkish case is interesting in identifying the type of variables which may facilitate or hinder privatization processes on a large scale. The Turkish experiment is also illuminating in terms of highlighting the importance of the broad environmental factors which heavily condition the success of a privatization program. The Turkish example demonstrates the difficulties of implementing privatization in a relatively open yet fragmented political system with a significant legacy of state interventionism. Our central thesis is that the political, legal and institutional context and their mutual interaction are crucial in explaining the pace or success of implementing a privatization program. In the Turkish setting, a fragmented political system, characterized by a succession of weak coalition governments, has been instrumental in the delays and setbacks experienced by the privatization program. It is also the case that within a fragmented polity, newly established agencies responsible for the implementation of neoliberal reforms, such as the Privatization Administration (PA), fail to achieve *the degree of autonomy* needed to facilitate the rapid and effective implementation of the program. In this type of environment, intra-bureaucratic conflicts between established layers of the state (e.g. the Constitutional Court) or the bureaucracy (e.g. the Treasury or the Ministry of Finance) and the newly formed bureaucratic units emerge as a striking obstacle to the smooth implementation of the reform process. The Turkish experience also raises broader questions concerning

the process of state restructuring that we observe in many late-industrializing countries undergoing reform experiences and *also the problem of institution building and democratic accountability* as central elements in carrying out welfare-augmenting privatization programs.

## **SLOW VERSUS HYPERPRIVATIZATION: THEORETICAL AND EMPIRICAL PERSPECTIVES**

Three broad and interrelated hypotheses may be advanced to account for the ability of certain countries to undertake large-scale privatization. First, the presence of a strong executive authority with a deep sense of commitment to the implementation of the program constitutes a crucial influence. A strong executive is central to the implementation of the broad macroeconomic, structural and legal-infrastructure reforms which are instrumental to the successful implementation of the privatization program itself. The presence of a powerful executive is also crucial in terms of breaking down opposition to the privatization program and allowing such key institutions as the privatization agencies, a substantial degree of autonomy from interest groups both within and outside of the state. Arguably, presidential system of government offer significant advantages compared to their parliamentary counterparts in this context. The second crucial influence concerns the depth of the economic and political crises experienced by a given country prior to the implementation of the program. It becomes much easier to implement a privatization program in a country which finds itself in the midst of a deep financial crisis. In such an environment, the power of external actors or constituencies for reform, such as the IMF or transnational business, increase considerably. Furthermore, in such an environment the executive authority enjoys greater autonomy and legitimacy for its

underlying reform agenda. Thirdly, a favorable external context or the presence of a powerful external anchor provides an additional space for the state elites in which to maneuver and provide an extra impetus for the rapid implementation of the program. State elites or policy makers are able to legitimize the process and to undermine opposition to reform when they are faced with a supportive international environment.

The relevance of these broad set of influences may be illustrated and highlighted with reference to key Latin American countries, Chile, Mexico and Argentina. These are the countries which have managed to undertake comprehensive privatization programs over a short space of time (3). The Chilean case, the first major example of a radical move in the direction of neoliberal reforms in the Southern Cone, is comparatively straightforward to explain. A highly authoritarian regime under Pinochet with a single-minded ideological commitment to the “free market” has been instrumental in overriding political opposition and implementing a drastic privatization program. In the two larger Latin American economies, Argentina and Mexico, the hyperprivatization experiences of the late 1980s and early 1990s are somewhat paradoxical. Mass privatization has been accompanied by a process of democratization in Argentina and by some degree of political liberalization in the one party dominant, semi-authoritarian political system of Mexico.

Both the Mexican and the Argentinean cases illustrate the importance of the domestic political institutions, notably the role of presidential systems, in facilitating a drastic reform or privatization process. The patterns observed in Argentina and Mexico are strikingly similar. In both cases, a strong President (Carlos Salinas in Mexico and Carlos Menem in Argentina), with unequivocal commitment to reform, has provided an unusual degree of autonomous space to a narrow group of technocrats. The so-called "technicos" associated with the centralized privatization agencies could implement an

ambitious program at an extraordinary pace (4). Consequently, the type of intra-bureaucratic or intra-state struggles, characteristic of the Turkish case have largely been eliminated in both the Mexican and Argentinean settings. The Menem experiment in Argentina is particularly striking from a comparative perspective given that a "populist" politician, in the standard Peronist tradition with the strong backing of labor unions, has been converted into a neoliberal reformer. He has subsequently displayed, in radical contrast to his initial electoral platform, an unusual degree of commitment to the success of the privatization program. His personal popularity as well as the popular base of his political support have proved to be critical in helping to build consensus around the reform project in the Argentine environment.

In retrospect, it is clear that the type of presidential regimes in Latin America that we have drawn close attention to resembles the type of presidential or quasi-presidential regime that Turgut Özal had tried to establish but could not institutionalize in Turkey, given the country's strong traditions of parliamentary government, an issue which will be discussed more explicitly at a later context. The link which is hypothesized to exist between a presidential system, on the one hand, and the scale and pace of the neoliberal program on the other hand highlights the presence of a serious dilemma. At least, during a lengthy transition phase, a serious conflict seems to emerge between the two central objectives of establishing a "durable or high quality democracy" and a "truly free" market economy (5). In more concrete terms, the Latin American style of presidential politics, so dear to Özal during his final days, is quite different from the American presidential or the French semi-presidential regimes. In such systems, strong institutions and checks and balances exist, thus limiting the arbitrary exercise of power by the president himself. In Latin American systems, however, where institutional checks and balances are largely absent, the individual who

occupies the presidential office embodies an unusual degree of authority and an unusually wide domain to exercise personal power. The unique scope of authority bestowed upon the President performs a catalyst role in initiating and sustaining a large-scale reform process. It is clear, however, that the system is not "democratic" by Western standards of liberal democracy. Furthermore, in the absence of appropriate checks and balances, and the presence of high degree of concentration of presidential power, a paradoxical situation arises in the sense that a conducive environment is created for hyperprivatization, but at the same time the system is open to abuses and vulnerable to possible instances of corruption. Hence, serious doubts may be raised concerning the degree of political accountability associated with regimes of this nature in the context of emerging democracies (6).

At a different level of analysis, one ought to reiterate the point made earlier that hyperprivatization may not necessarily imply "successful" or welfare enhancing privatization. In fact, serious criticisms have been leveled concerning the quality of hyperprivatization experienced in Argentina. The tendency to relegate fundamental issues pertaining to regulation and competition into the background, resulting in excessive concentration of economic power and the low quality of the subsequent services provided have been frequently emphasized by a number of commentators investigating the Argentina experiment. This has been particularly evident in the context of telecommunications (7).

Turning to our second broad explanatory category, the economic and political crises experienced by Southern Cone countries have been much deeper crises compared with the crises experienced in the Turkish case. Mexico for example, experienced virtually zero growth throughout the 1980s whereas Turkey recovered within two or three years from the major balance of payments crisis of the late 1970s,

signifying the major crisis of import-substitution in Turkey. Furthermore, the duration of the authoritarian regimes characterizing the post-import substitution phase of development and the subsequent crises have been significantly longer in Southern Cone countries such as Argentina and Brazil. Judged by the intensity and duration of economic and political crises, therefore, the Turkish case may be characterized as a relatively stable case or an example of "stable instability". "The depth of crises" argument is important considering that Turkey has not experienced, at least well into the late 1990s, the type of crises, which would provide the kind of "big push" needed to dramatically accelerate the pace of the privatization program. One has to remember the 1980s leaders in Argentina and Mexico were paralyzed and unable to respond effectively to national problems. It took hyperinflation and a very serious economic crisis before the Argentine Congress passed laws giving sweeping powers to President Menem to privatize state enterprises. The depth of the crises and the failures of the previous authoritarian regimes in the economic realm have proved to be vitally important in Latin America in terms of securing legitimacy for and generating consensus around the reform and privatization program. For neoliberal reformers, it has been comparatively easy to override opposition in this type of environment.

As a third broad category, the "external anchor or discipline argument" is also directly relevant in the Latin American context, notably in the case of Mexico. Economic crisis seems to have played a large, but less significant role in Mexico, where other considerations, such as President Salinas` desire to sign NAFTA, also spurred privatization. Mexico's special relationship with the United States of America and the requirements of NAFTA membership have acted as a source of external stimulus or discipline. This has been instrumental in accelerating the pace of the reform program in all areas including trade and capital account liberalization, macroeconomic stabilization

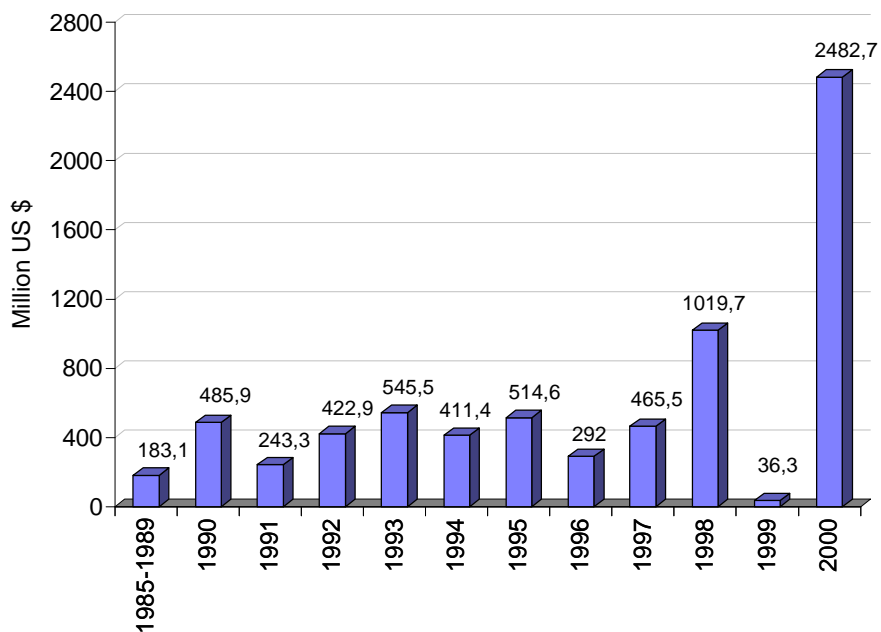
and divestiture of state-owned enterprises. Stated somewhat differently, membership of NAFTA helped to augment the degree of autonomy of the domestic policy making elite with respect to its own electorate. The rationalization of the reform process and the overriding of political opposition have been relatively smooth processes in the presence of such a powerful external anchor.

### **THE DOMINANT CHARACTERISTICS OF TURKISH PRIVATIZATION DURING THE 1990s.**

An examination of the pattern of privatization in Turkey, as portrayed in Figure 1, suggests a comparatively stable pattern of low privatization revenues well into the late 1990s. It is striking that the maximum revenues generated in a single year has never exceeded the US \$600 million mark in a single year right up to 1998 (8). A casual inspection of the Figure 1 seems to point towards a major jump in privatization revenues in 1998, with sales proceeds exceeding the US \$1 billion mark per annum for the first time. However, a major qualification is called for, in evaluating the sudden jump of 1998 because the sale of minority shares in Ýþbank, a privately owned major banking institution, has accounted for over sixty percent of the privatization revenues generated during that particular year. In retrospect, 1998 might have represented a major landmark in the history of Turkish privatization if the privatization of one major public enterprise, namely POA<sup>a</sup> (engaged in the distribution of oil) could have materialized, an issue which will be examined further in the subsequent section. The year 2000 represents a major landmark in the history of privatization program in Turkey. Almost US \$ 2.5 billion worth of privatization was concluded as of August 2000. This has been the highest privatization realization ever reached in a single year by the privatization agency of Turkey. It compensates partially for the worst record

experienced in 1999 amounting to a dismal figure of US \$ 36.3 million, an outcome which may be explained by the fact that 1999 constituted an election year and the absence of effective external pressure.

**Figure 1**  
**Privatization Implementation on an Annual Basis.**  
**(1985-2000)**



**Source:** DPT (State Planning Organization), 1998 and Periodic Bulletin of the ÖYB (The Privatization Administration of Turkey), August 2000.

There is an underlying consensus in the literature on the need to design an institutional framework for effective regulation as a critical precondition for welfare-enhancing privatization. In fact, many investigators have drawn attention to the importance of creating a competitive environment as being more significant than the transfer of ownership per se (9). In spite of this apparent consensus in the theoretical literature on privatization, the regulation element, at least until very recently has

constituted a neglected dimension of the Turkish experiment **(10)**. Although the privatization program effectively started in 1986, the legal framework for regulation in Turkey could only be established in October 1994 (**check**), largely to meet the obligations imposed by Turkey's entry into the Customs Union with the European Union. The Competition Board, the key institution responsible for regulation is creation of this Law. However, this institution could initiate its operations only with significant time lag. The newly created institution has been quite vocal and active during the recent episodes of Turkish privatization. The institution itself has generated a novel set of challenges. A striking example of these challenges became evident in the context of the proposed sale of POA<sup>a</sup> during late 1998 and early months of 1999. A conflict arose between the PA and the Competition Board on the grounds that the latter institution had not been consulted for approval during the initial phase of the privatization process. Subsequently, the Competition Board has effectively blocked the divestiture of POA<sup>a</sup> through its actions. The consortium of bidders initially interested in buying the enterprise have later declared they were no longer interested allegedly because of the new constraints imposed by the Competition Board that did not exist during the bidding process itself. The POA<sup>a</sup> affair clearly highlights the dilemmas experienced in Turkey in terms of privatizing large-scale enterprises, on the one hand, and the problems encountered in terms of effective regulation and imposing rules of fair competition on the other. Following this incident, however, we observe much closer cooperation between these two key institutions, with the Competition Board from that point onwards being actively and formally involved in the privatization process **(11)**.

Admittedly, to argue that regulation has been totally ignored, at least until very recently, would represent an overstatement in the sense that during the early years of

the program, the "golden share" rule has been frequently practiced (12). The "golden share" implies that the government retains a very small share of the company's ownership in order to retain control over corporate governance and hence, indirectly performing a regulatory role in the post-privatization era. However, in the absence of an institution specifically designed to implement the golden share formula, the desired outcome from a social welfare point of view could not materialize. In fact, there exist well-documented cases where the company has abused its monopoly power in the post-privatization context because of the failure of the government to effectively implement the golden share practice (13).

A multitude of objectives have been identified in the context of the Turkish privatization program. However, given the presence of large budget deficits and the underlying fiscal crisis of the state, the emphasis has been unambiguously placed on the goal of revenue maximization (14). The emphasis on fiscal gains has also been implicit in the most recent case involving the sale of public stake in Ýþbank in 1998 and partial sale of Tüpra° in 2000 while the overt objective had been announced as widening of share ownership in the spirit of popular capitalism. Indeed, it is fair to say, in retrospect, that the fundamental objective that one normally associates with a privatization program, namely an improvement in efficiency and the creation of a more competitive environment have largely been downplayed or deemphasized in the Turkish context.

## **THE SEARCH FOR STRONG EXECUTIVE AUTHORITY: POLITICS WITHIN THE STATE AS BARRIERS TO EFFECTIVE PRIVATIZATION**

The architect of the Turkish privatization program, Turgut Özal realized the need to create a powerful bureaucratic institution which would be directly tied to the office of

the Prime Minister while being largely independent from other key bureaucratic organizations responsible for economic policy making (15). The design of this powerful new institution proceeded in the following manner. First, the Law No. 2983 set out the legal foundation that allowed the establishment of the Housing Development and Public Participation Administration (HDPPA) in 1984. The overt objective was to create a new institution vested with the authority to finance mass housing and major infrastructure projects as well as to implement privatization. However, an implicit objective was to create a new managerial bureaucracy as a means of by-passing the possible constraints on the implementation of the program by the principal layers of the "classical bureaucracy", that arguably form the "pro-public enterprise coalition". Such groups who benefit from the existence of public enterprises in terms of power, prestige and employment are likely to lose their privileges in the aftermath of privatization. It is also striking that the HDPPA, as a newly empowered institution, governing the largest extra-budgetary fund, has not been subjected to normal budgetary discipline and parliamentary control. The very fact that it became directly responsible to the office of the Prime Minister is rather reminiscent of Latin American styles of decision making, with a corresponding absence of checks and balances that would normally be associated with a parliamentary form of governance. What was clearly intended is the creation of a highly centralized and autonomous institution.

The most striking aspect of the legal framework established in the 1980s concerns the transfer of ownership and all the legal authority over the company on the privatization agenda to the HDPPA itself. The institutional model developed rested on a division of labor between the executive (i.e., the Prime Minister) and the Privatization Administration, as the technical-bureaucratic unit with a minimum direct

role in the decision-making process. In such a setting, rapid privatization becomes possible only if the political authority is committed to this objective and possesses the political power to implement privatization. If these preconditions are satisfied, the PA would, indeed, emerge as a very powerful organization because the ownership of the company to be privatized is passed on fully to the orbit of this institution itself. In other words, the PA, by assuming the sole control or authority over the enterprise to be privatized, effectively cuts the link between the enterprise and the Minister previously empowered with its ownership and control. This division of labor may work very effectively when a dominant party (or a president in the Latin American context) is in power and strongly committed to the success of the privatization program. This two-tier structure may facilitate a speedy decision-making process, limiting interference from other layers within the state. However, when a coalition government emerges with weak commitment to privatization and reform, the apparent "autonomy" of the institution with respect to other layers of the state largely disappears. In the context of a fragmented state, the ability of this newly created institution to engineer a process of rapid privatization fails to materialize because, by definition, the decision-making powers are vested solely with the executive itself. This pattern is clearly observed in Turkey as the Turkish political scene during the 1990s has been characterized by a highly fragmented party system and successive coalition governments with serious ramifications concerning the fortunes of the privatization program. The formation of a new government involving the right-of-center True Path Party (DYP) and the left-of-center Social Democratic Populist Party (SHP) in 1991 marked the starting point of coalition politics in Turkey in the 1990s. These two political parties, in spite of their ideological differences, have shared an identical mistrust of the privatization process. In fact, both parties while in opposition, had played an important role in reversing early

block sale of public assets to the private sector **(16)**. Once the commitment of the executive or the political authority vanishes, then inevitably the privatization process becomes lengthy and politicized, with new sale of public assets abandoned or earlier sales reversed as a natural outcome of this politicized environment **(17)**. The lack of governance and commitment has been an obvious reason not only in the slow implementation of the privatization program, but also in the areas of tax reform, social security reform, and implementation of an overall disinflation program **(18)**. One could argue that the legacy of étatism generated a widespread suspicion of privatization. This étatist mind-set rendered even the proponents of privatization insecure about their own positions and often put them on the defensive. Discussions frequently centered around the protection of the public owned goods against potential political abuses. Efficiency arguments were rarely emphasized. The nature of Turkish politics and more specifically the party system are also critical in understanding the fortunes of the privatization program. One needs to recognize that Turkish politics is characterized by patronage politics **(19)**. Parties are typically clientelistic networks whose major function is to channel public resources to create their own bases of political support. What is important in the Turkish context is that even strongly pro-private enterprise political parties did not push for privatization in practice because it would take away significant patronage opportunities from them. Lip service was paid to the need for privatization but achievements were limited. In fact, limited privatization that occurred appeared to be tied in with patronage **(20)**. One could go even further and argue that rent-seeking behavior and outright corruption have been central to an explanation of limited privatization in Turkey. Such corruption through insider trading, false information, lack of transparency and illegitimate business ethics has become one of the critical aspects of the Turkish economy as witnessed throughout the 1990s. This, in turn, has

exercised a rather adverse impact on the overall progress of privatization in Turkey (21).

The link between the political environment and the legal framework became critical to the fortunes of the privatization program in two critical respects. First, opponents of privatization, who also form part of the pro-public enterprise coalition, including some members of the political elite, certain layers of the bureaucracy, labor unions and intellectuals committed to a statist ideology, have effectively exploited the absence of a Privatization Law until the enactment of a comprehensive privatization law in 1994. The privatization process has been marred by major and costly legal setbacks. The dominant logic underlying the decision-making style instituted by Özal favored decrees with the force of law in order to accelerate the pace of the privatization and the overall reform process by overriding political or bureaucratic opposition. However, opponents of privatization have utilized the weaknesses of the legal infrastructure as a way to bloc the progress of the privatization program in Turkey. "Politics within the state" is critical to this argument since the Constitutional Court, a key institution of the legal arm of the established state apparatus, has emerged as a critical institutional vehicle in translating the explicit and formal demands of the opposition into a concrete blockage of the privatization program.

A crucial dichotomy underlying the political economy of Turkey during the late 1980s and the early 1990s has been that politicians who oppose privatization while in opposition changed their positions drastically or at least became partial supporters of privatization in when they came into government. This apparent contradiction may be explained primarily by a domestic factor, namely the fact that parties in office perceive privatization as a source of revenue for overcoming the underlying fiscal crisis of the state. Perhaps, to a lesser extent, the changing global context more favorable to

privatization, in the course of the 1990s has also been instrumental in accounting for the U-turn in the approach of the parties in opposition when they actually came into office. However, even if a Turkish government, in principle, feels forced to proceed in the direction of privatization, the absence of an adequate legal framework and the presence of well-organized opposition lobbies who capitalize on this very absence, create a serious set of barriers to the progress of privatization. This problem could be solved, in principle in the Turkish context, via an amendment in the Constitution itself. Yet, this is a rather complex process in the Turkish setting because it requires a two-thirds majority in the Parliament, the achievement of which in the 1990s has been an almost insurmountable task. The second best solution would be to introduce a Privatization Law, which conforms to the basic spirit of the Constitution. However, the enactment of such a law has not been possible until 1994. Consequently, governments in power had to resort to a piecemeal and ad hoc approach, trying to make individual designs for particular cases of privatization resulting in costly delays.

The year 1994 represented a critical point in the evolution of the Turkish experiment. After a significant delay, the Privatization Law has finally been introduced. To some extent, this has managed to overcome the deficiencies of the legal framework encountered during the initial years of program implementation. The new law provided greater flexibility in the choice of privatization techniques and emphasized transparency in all transactions. Another key innovation involved the explicit recognition of labor adjustment issues and redundancy payments for displaced workers. As part of the new legal framework, the proceeds of privatization could now be utilized for meeting the costs of divestiture, compensation of displaced labor and financial restructuring of enterprises in the PA portfolio **(21)**.

A critical implication of the new Law involved the inevitable weakening in the power of opposition lobbies to reverse privatization decisions through the Constitutional Court. However, opposition lobbies continued to be an active and vocal source of blockage for the privatization program as testified in the case of the telecommunications privatization process in the case of what the general privatization law proved to be inadequate. Strong opposition to telecom privatization manifested itself, on this occasion, as an opposition to the Telecommunication Laws of 1994 and 1995 themselves. In particular, it has been alleged that these laws have not conformed to the basic principles of the Constitution. This criticism, in turn, has been effective in the annulment of these laws. Lack of institutionalized bidding procedures, especially in valuation techniques and the formation of valuation committees have been singled out as the critical missing elements underlying the decision to abandon the telecommunications laws. A new Telecommunication Law was passed in 1996 with no reversals to date **(22)**. The Constitutional Court's rulings on valuation techniques led to the annulment of the related clauses of the Privatization Law of 1994. An amendment to deal with this problem was accomplished in 1997. More recently in 1999, the concept of privatization has, at last, been incorporated into the Turkish Constitution as a by-product of accepting the rules of international arbitration **(23)**. The acceptance of the rules of international arbitration heavily demanded by foreign investors for a long time illustrates the importance of the influence exercised by international actors, notably the transnational corporations, in gradually weakening of the étatist coalition.

From a broader perspective, an interesting question arises from the Turkish experience concerning the position of the Constitutional Court, as a key component of the state, in influencing the implementation of the privatization program. Hitherto, the

emphasis has been on the negative role whereby opponents of privatization have utilized this institution to bloc the very momentum of the privatization process itself. It would be extremely misleading, however, to view the Constitutional Court on a totally negative light. One also needs to acknowledge the positive aspect of having a strong and independent institution like the Constitutional Court in terms of avoiding possible abuses of the privatization process involving severe undervaluation of public assets for example. This concurs with our earlier observation that hyperprivatization, achieved over a very short period of time, may not be welfare enhancing. If anybody is to be criticized for the slow phase of privatization in Turkey, it is not the Constitutional Court, but the politicians for their failure to institute a sound and constitutionally compatible legal framework in a timely fashion.

#### **POLITICAL CONSTRAINTS, ABSENCE OF INSTITUTIONAL AUTONOMY AND PERVERSE INCENTIVES: THE TURKISH PRIVATIZATION ADMINISTRATION IN CRITICAL PERSPECTIVE**

So far, our analysis has focused on the broad political and legal framework within which the key institution responsible for the implementation of the privatization program, the PA, is situated. The performance of the PA has heavily depended on the underlying commitment of a strong and autonomous political authority. Moreover, the institution has been characterized by a number of internal organizational deficiencies, reflecting possible failures of institutional design in the first place. The current organizational structure of the PA is clearly not commensurate with the existing complex and heavy workload imposed on the institution. The organization is characterized by a top-down internal decision-making process with excessive workload concentrated at the center with the top management, with limited avenues for

delegation and decentralized decision making. The operational effectiveness of the agency is significantly diminished by the unusually wide scope of the privatization program with a disproportionate share of the public enterprise sector on the privatization agenda at any given time. In fact, the PA is currently responsible, as of August 2000, for the divestiture of forty seven companies ranging from relatively small and medium-scale enterprises to such major operations as oil refineries, petrochemical concerns, iron and steel companies and national airlines. It also plays a pivotal role in the ongoing telecommunications privatization process.

A vicious circle emerges as slow privatization increases the workload on the agency with additional public enterprises being placed on the privatization agenda on top of the lengthy list of the public enterprises waiting to be privatized. The absence of a delegated decision-making system manifests itself at two different levels. Neither lower level management within the agency itself nor the managers of the enterprises to be privatized can make a significant contribution to the decision-making process. As a consequence of this design deficiency, top managers within the agency became responsible for a disproportionate share of the decisions regardless of their significance for the overall program itself.

Another unintended outcome of this process is that top managers within the agency are not able to focus explicitly on certain key strategic issues. Perhaps the most obvious manifestation of the excessive workload phenomenon concerns the unusually long waiting periods between the time that an enterprise is placed on the privatization agenda (i.e., the preparatory stage) and the date of the final sale itself. As of August 2000, companies have been under the privatization portfolio for an average of 50.4 months. The preparatory stage is even lengthier for larger and more "visible" companies whose shares are traded on the stock market. For example, the oil refining

company (TÜPRA<sup>a</sup>) and the national airline company (THY) had been incorporated into the privatization program in 1990 with limited success to date. Similarly, the integrated steel mill and producer of flat steel (ERDEMÝR) and the petrochemical complex (PETKÝM) have been integral parts of the program almost right from the beginning since 1987 (24). The average waiting period for such large companies has reached almost twelve years (Table 1).

**Table 1**  
**Waiting Periods in the Case of**  
**Large Enterprises on the Privatization Program**

| Name of the Company                                   | Industry Type      | PA Share (%) | Date of Incorporation (months/years) | Waiting Periods (years. months) (As of August 2000) |
|---|--------------------|--------------|--------------------------------------|---|
| THY   | Airline            | 98.17        | 08/90                                | 10.00   |
| TÜPRA <sup>a</sup>                                    | Petroleum Refining | 96.42        | 07/90                                | 10.01   |
| PETKÝM  | Petrochemicals     | 95.86        | 09/87                                | 12.11   |
| ERDEMÝR   | Iron and Steel     | 51.66        | 04/87                                | 13.04   |
| <b>Average Waiting Period (Years. months) : 11.07</b> |                    |              |                                      |   |

**Note:** Only small portions of these companies have been privatized.

**Source:** Periodic Report of ÖÝB (The Privatization Administration of Turkey), August 2000

The lengthy privatization process and lack of direction in the program have resulted in a deterioration of the financial strengths of the enterprises to be privatized and hindering their vital expansion plans and marketing strategies. For example, up until recently, the petrochemical complexes of PETKÝM have not been allowed to undertake large-scale investment projects which are desperately needed to keep up with changing technologies and satisfying growing consumer demand. As a consequence of inadequate technological adaptation and slow expansion, the company's performance has arguably failed to reflect its true potential.

Rather paradoxically, some of the in-built strengths of traditional bureaucratic agencies have been strikingly absent in the PA. Indeed, one of the key problems confronted by the agency has been its inability to institute well-defined and objective recruitment procedures. The current recruitment system is based on political and personal connections. Ad hoc and arbitrary selection criteria have rendered the agency increasingly vulnerable to political pressures and external intervention. Heavy political involvement in the recruitment process is also reflected in the high turnover of top management. The PA has undergone major changes too frequently at the top management level (Table 2). Between 1993 and 1997, (acting) presidents have been able to serve only for 5.25 months on average. It is rather striking that the PA has had more than three presidents and ten vice-presidents, on average, for each year in the past three years (25). Since 1998, stability has been finally restored, with no change being observed in the top management

**Table 2**  
**Top Management Turnover**  
**in the Privatization Administration**

|                                  | <b>1986-1993</b> | <b>1994</b> | <b>1995</b> | <b>1996</b> | <b>1997</b> | <b>1998**</b> |
|----------------------------------|------------------|-------------|-------------|-------------|-------------|---------------|
| <b>Number of Presidents*</b>     | <b>6</b>         | <b>2</b>    | <b>3</b>    | <b>4</b>    | <b>3</b>    | <b>1</b>      |
| <b>Number of Vice-Presidents</b> | <b>18</b>        | <b>3</b>    | <b>9</b>    | <b>10</b>   | <b>11</b>   | <b>7</b>      |

**Note:** If any president/vice president serves in different calendar years, he/she is counted in all corresponding calendar years.

\*Between 1993 and 1997, the average tenure of presidents has been 5.25 months.

\*\*Since 1998, the PA enjoys a very stable pattern of top management

Source: The Privatization Administration of Turkey, Prime Ministry of Turkey

High turnover of top management clearly disrupts continuity and the accumulation of expertise. Rather ironically, stability of top management is more adequately secured in classical bureaucratic agencies that the PA was intended to bypass in the first place. For example, even the removal or the appointment of a middle

manager (i.e., head of department) at the Treasury requires a decree signed by the President, the Prime Minister and the relevant Minister responsible for the institution. At an institution such as the Capital Markets Board (SPK), the Chairman is appointed for a fixed term of three years, making it very difficult to remove him before the end of his term. On the other hand, in the context of the PA, both the president and the vice-presidents are vulnerable to the fast changing political climate (26). The removal of the vice-president is even easier. Their fate is left to the president of the PA and the Minister in charge of privatization. The fragile nature of the appointment in the agency leads to frequent turnover of top personnel, leading to inertia and myopic bias.

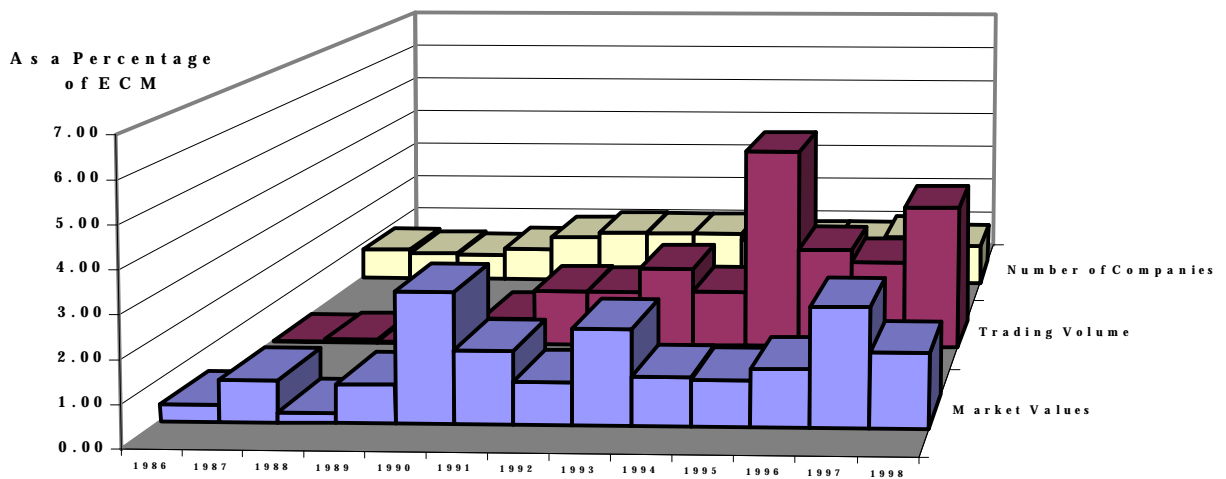
One should also point out that the agency has inherited some in-built weaknesses of the existing bureaucratic order. Given civil service rules, no clear link could be established between performance and incentives. At present, an incentive system that allows a sharp differentiation between high and low performers is non-existent. This poses a real obstacle in terms of attracting highly-motivated and qualified people to the agency. In other words, the agency faces the same problem of lack of accountability that is a characteristic of the existing bureaucratic structure as a whole. Clearly, attempts to improve performance are severely undermined in the absence of sufficient accountability in the system. All in all, high turnover of top management coupled with lack of accountability result in perverse incentives.

### **THE VICIOUS CIRCLE OF MACROECONOMIC INSTABILITY AND SLOW PRIVATIZATION IN TURKEY**

It has been argued that the most significant achievement of Turkish privatization to date has been its contribution to the development of capital markets in Turkey (Ertuna, 1997). Empirical evidence for this assertion is provided by a study which covers the period from 1989 to 1993. During the period concerned, 14 public offerings of

companies on the privatization agenda appear to have represented 15.7 percent of the total number and 42 percent in value terms of the initial public offerings in Turkish capital markets. Moreover, it was found that these offerings, in the long run provided better rates of return compared to private sector issues (Özer, 1995). While it is true that privatization in Turkey provided a major initial boost to capital market development, this did not prove to be a sustainable process during the 1990s. Furthermore, when we consider the pace or depth of capital market development in comparison with other "emerging markets" we fail to observe a dramatic increase in the relative position of the Turkish capital markets among emerging capital markets (ECM). In the overall total judged by various indicators including market capitalization, trading volume and the number of trading companies involved, the share of the Turkish market still remains low. In fact, the comparative evidence suggests that the Turkish capital markets, in spite of sporadic developments, have failed to accomplish a major jump in the hierarchy of emerging markets (Figure 2). Arguably, if a major breakthrough had been established with respect to the implementation of the privatization program, the intensity and depth of capital market development in Turkey could have been significantly more pronounced.

**Figure 2**  
**The Relative Significance of the Istanbul Stock Exchange**  
**In the Emerging Capital Markets (ECM)**  
**(1986-1998)**



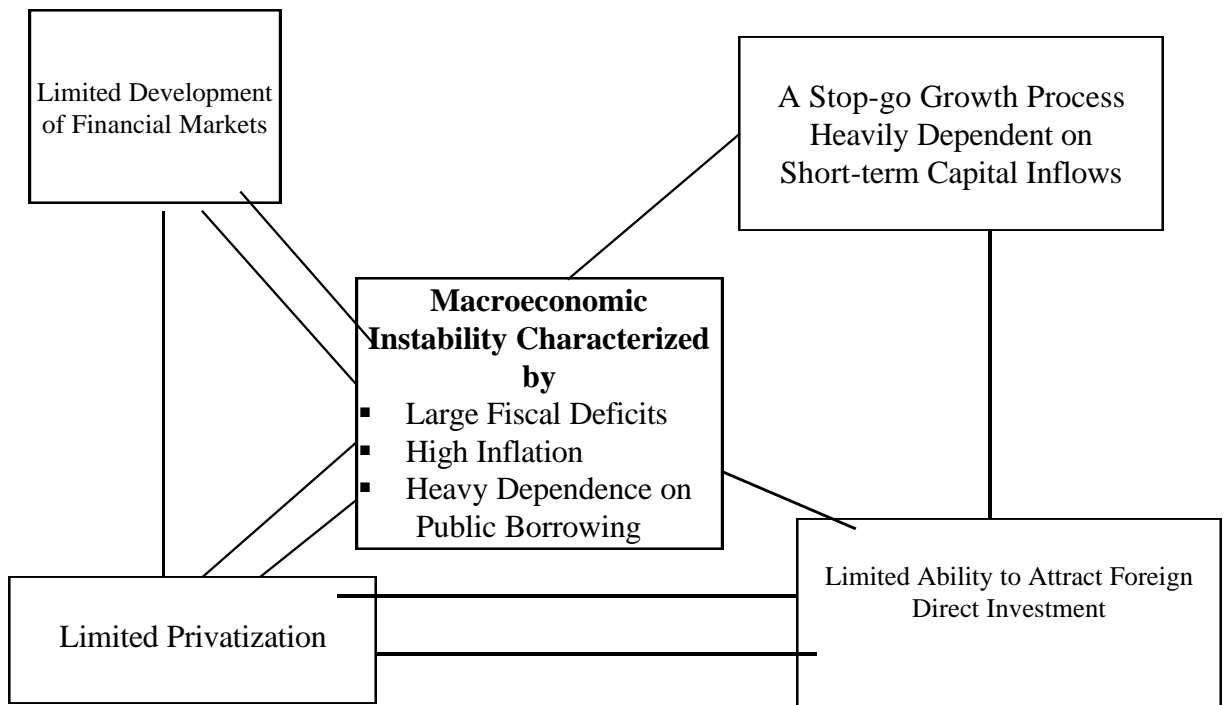
**Source:** IMKB Dergisi, Istanbul Stock Exchange, Vol. 3, No. 10, pp. 55-58.

Large fiscal deficits and macroeconomic instability have remained a persistent problem in Turkey throughout the 1990s (27). One may hypothesize that limited privatization and macroeconomic instability constitute a two-way relationship. Macroeconomic instability, in an environment of political uncertainty, has, in turn, restricted the country's ability to attract foreign direct investment on a sufficient scale. The inability to attract foreign direct investment exercised a negative effect on the pace of privatization in Turkey (Figure 3). However, a major qualification is called for, however, in the sense that Turkey, at no stage, could present a fully prepared privatization project sufficiently attractive to foreign investors. Furthermore, restrictions have been placed on the participation of foreign investors in areas considered to be of strategic national interest. The vicious circle involving macroeconomic instability, limited capital market development and limited foreign direct investment has encouraged a pattern of unstable economic growth in Turkey, a

process which has been dependent on the ability to attract large inflows of short term capital in response to high domestic interest rates (28).

It is clear that a major breakthrough in the privatization effort possesses the potential to convert the "vicious circle" into a "virtuous circle". A major boom in privatization activity would be instrumental in reducing the size of the fiscal deficit, accelerating the pace of capital market development and the magnitude of long-term capital inflows which, in turn, may feed onto each other, providing the basis of a cumulative improvement in economic performance (29).

**Figure 3**  
**The Vicious Circle of Macroeconomic Instability**  
**and Limited Privatization in Turkey.**



## **THE RECENT RESURGENCE OF PRIVATIZATION IN TURKEY: A PARADOXICAL DEVELOPMENT?**

It is interesting to observe that privatization has finally gathered momentum during 2000. Two major cases were involved, namely TÜPRA<sup>a</sup> (engaged in petroleum refining) and POA<sup>a</sup> (state oil distribution company). Shares of TÜPRA<sup>a</sup> were sold through domestic and international public offerings. The POA<sup>a</sup> deal, completed after the second attempt, constituted the pioneering case of large-scale privatization in Turkey. It is most likely that the ambitious privatization goals of the government will be fulfilled (30). One possible explanation of this trend involves the strengthening of executive authority. The current coalition government in Turkey, at least for the time being, does no longer seem to be associated with instability or conflict as has previously been the case. A more stable pattern of coalition politics, in turn, resulted in greater stability in the Privatization Administration itself (Table 2). Another favorable sign in this respect is that after significant delay, the legal and institutional infrastructure of privatization has largely been established by the late 1990s, a factor which also helped to undermine the power of the étatist lobby as a major source of opposition to the privatization program.

A closer inspection reveals, however, that there were more fundamental factors at work which helped to accelerate the pace of the privatization program. The combination of the “depth of crises” and “favorable international context” arguments become particularly relevant for Turkey by the end of the 1990s. Endemic fiscal disequilibrium, a perennial problem in Turkey, had almost reached crisis proportions by the end of the decade. Indeed, the current government had to speed up the privatization process not because of profound ideological convictions than the previous governments, but because of deteriorating economic conditions. The mobilization of

support of the international economic agencies could only be feasible through a rigorous implementation of the privatization program as part of a broader economic package. One should add that the announcement of Turkey's candidacy for full EU membership at the Helsinki Summit of December 1999 also represented a favorable push in this context. In retrospect, neither the government nor the bureaucracy had become significantly stronger than before. In a way reminiscent of the pioneering reform program of 24 January 1980, during which a major set of economic actions were taken under strong external pressure, by the weak minority government of the time, the privatization program has started to pick up speed because the government felt obliged to accept recommendations of the international community in order to avoid an impending economic disaster.

An interesting issue for future research concerns a critical assessment of the private sector in the privatization process. Particularly striking in this context are the greater involvement of certain segments of the business community in the privatization process and the changing nature of private sector's relations with the state, questions, which certainly deserve further investigation.

## **CONCLUDING OBSERVATIONS**

Institutions have a significant bearing on countries' ability to implement privatization programs. Institutions, however, do not exist in a vacuum. The effectiveness of bureaucratic institutions depends critically on the domestic political and economic environment as well as the influence of external actors. This suggests that a mere creation of a new institution is not enough to ensure effective privatization implementation. The Turkish privatization program has certainly been negatively affected by the lack of political stability and the associated intra-state or intra-

bureaucratic conflicts aggravated by a fragmented political system. The critical agency responsible for the implementation of the privatization program in Turkey, the Privatization Administration (PA), was largely designed on the assumption that a quasi-Latin American style presidential government could be institutionalized in the Turkish context during the late 1980s. Lack of political stability at the level of the broad macro environment, however, has meant lack of continuity in the direction of the PA itself. Consequently, the 1990s have been characterized by an unusually rapid turnover of top managerial personnel at this critical institution. Delays in privatization, in turn, had undesirable repercussions on the performance of public enterprises placed on the privatization agenda.

The privatization program in Turkey has suffered from the deficiencies of the legal framework, which have subsequently been remedied to a certain extent, but with a major time lag. The weaknesses of the legal framework strengthened the position of those groups who were against privatization in principle. In fact, one of the striking features of the Turkish experience is that a number of privatization cases have been explicitly challenged at the Constitutional Court. This has resulted in the reversal of a series of some key privatization decisions.

The strength of the executive authority in itself is a critical factor in facilitating large-scale privatization. The Turkish case illustrates, however, that the two other fundamental factors, namely the threat of a major economic crisis coupled with pressure from external actors may provide a major impetus for privatization program by strengthening the hand of the executive itself, even in situations where the underlying power of executive authority may not necessarily be greater than before.

## NOTES

1. According to the data provided in Ramamurti (1999, p.141) proceeds from privatization during the period 1988–1998 for Argentina and Mexico have been estimated at US \$18.25 billion and US \$27.32 billion respectively.
2. An overall assessment of the Turkish neoliberal experiment focusing on the depth of the reform process and degree of success achieved is an issue that is beyond the scope of this paper. It is quite clear, however, that much more progress has been achieved with respect to trade and capital account liberalization compared with privatization. For broad evaluations of the Turkish liberalization process during the 1980s and the 1990s, see Arýcanlý and Rodrik (1990), Rodrik (1992), Togan (1993), Öni° (1998) and Boratav et al. (1999).
3. On some of the underlying causes of slow pace of privatization in the developing world, see Ravamurti (1999). For detailed assessments of privatization programs implemented in the Southern Cone, see Aspe (1993), Manzetti (1993), Waterbury (1993), and Teichman (1997). For an important attempt to discuss the relationship between democratization and economic reforms in Latin America from a cross-regional perspective see, Brasser Pereira et. al. (1993)
4. On the importance of the presidential system in terms of allowing the small technocratic elite to undertake drastic economic reform, see Aspe (1993), Manzetti (1993), Centeno (1994), Philip (1997), Teichman (1997) and Weyland (1999).
5. For an interesting discussion of whether the “capitalist revolution” in Latin America will succeed in creating a genuinely “free and competitive market economy”, free from clientelistic ties and based on respect for the rule of law, see Llosa (1998). Many of the points raised by Llosa concerning the limitations of the “capitalist revolution” in Latin America are also applicable to the Turkish case where clientelistic networks also continue to constitute a strong feature of the political system.
6. The issue of insufficient political accountability emerges as a serious problem in many emerging democracies and contains serious ramifications for the effectiveness of a privatization program from a social welfare point of view. Weyland (1999), in particular, emphasizes the important point that Latin American style presidential regimes may be quite effective in terms of initiating a process of radical economic reforms but considerably less successful in terms of consolidating or institutionalizing such reforms.
7. For a penetrating discussion concerning the limitations of the Argentine privatization experiment and especially the problems encountered in the aftermath of telecom privatization, see Manzetti (1993).
8. The Turkish privatization experience to date has been extensively studied. For a small sample, see Öni° (1991), Aktan (1993), Bođaziçi Journal (1993), Karataþ (1993), Celasun and Arslan (1997), Ercan (1997, 2000), Ertuna (1997) and Karata° (1999). For a valuable study of the process of privatization in the cement industry and the problems encountered in the aftermath of privatization, in the form of growing concentration of economic power, see Tallant (1993). For an official assessment of the Turkish privatization experience to date, see DPT (1998).
9. On the importance of competition and regulation for welfare-enhancing privatization, see Vickers and Yarrow (1991).
10. On the objectives of the Turkish privatization program, see the report prepared by the Morgan Guaranty Bank (1986), specially commissioned by the Turkish government.
11. The role of the Competition Board in the privatization process of POA<sup>a</sup>, eventually resulting in the collapse of the proposed sale has been widely documented in the national press. See, among others, “Garanti-Dođuş POAP’tan çekildi” *Radikal*, (National Newspaper) March 3, 1999. The conflict between the PA and the Competition Board was openly admitted by the Chairman of the

- Competition Board at the time. See “6 metrekarelik mutluluk” , *Star* (National Newspaper) May 29, 1999.
12. For a good discussion of the “golden share” practice as a means of regulating enterprises in the post-privatization era, see Karata<sup>o</sup> (1993).
  13. Abuses of monopoly power, in the absence of adequate regulation, have been observed both following the sales of USA<sup>a</sup>, an airplane catering company and ÇÝTOSAN, a cement firm. For evidence on this issue, see Karata<sup>o</sup> (1993) and Tallant (1993).
  14. The acute fiscal disequilibrium experienced by Turkey, notably during the 1990s, has been extensively analyzed. Particularly significant among a multitude of studies are the following: Özatay (1996), Atiyas and Sayın (1998) and Boratav et al. (1999). On the emergence of revenue considerations as the primary objective of the privatization program in Turkey, see Kjellstrom (1990) and Aktan (1993).
  15. Turgut Özal was the Prime Minister of Turkey during the 1983-1989 period and the President from 1989 until his death in 1993. Concerning Özal’s objective of instituting a type of strong presidential system, with an unusual concentration of executive power, to overcome the constraints imposed by the “classical bureaucracy” and his intention to undermine the power of the “traditional bureaucratic elite” in Turkey, to restore the balance between elected politicians and life-time bureaucrats, see Barlas (1996). On the broad political economy of Turkey in the post-1980 era, notably on the dominance of the right-of-center Motherland Party (ANAP) during the late 1980s followed by a period of unstable coalition politics in the 1990s, see Waterbury (1992) and Öni<sup>o</sup> (1998).
  16. In the first half of 1989, 90 percent of the state’s equity in the large cement firm ÇÝTOSAN was sold to Société Ciment Français, and 70 percent of USA<sup>a</sup>, an airline catering service, was sold to Scandinavian airlines. Subsequently, the Constitutional Court in response to the formal demands of the two opposition parties DYP and SHP, blocked the sales of ÇÝTOSAN and USA<sup>a</sup> on the grounds that sales of public enterprises to foreigners were unconstitutional.
  17. Some striking examples involving the reversal of privatization decisions are EBK (meat processing), SÜMERBANK (banking institution) and PETLAS (manufacturer of tires). Most of the companies experiencing a reversal decision have subsequently been privatized.
  18. There are renewed ground for optimism concerning Turkey’s ability to implement privatization and overall macroeconomic reform following the formation of a new coalition government after the general elections of April 1999. For a discussion of this renewed optimism see Öni<sup>o</sup> (2000).
  19. For a valuable discussion of patronage politics, clientelism and the nature of party politics in Turkey see Güne<sup>o</sup>-Ayata (1994) and Heper and Keyman (1998).
  20. Allegations concerning corruption in privatization deals have been frequently advanced by the national press. Striking examples of such allegations include sale of minority shares in TOFAS to foreign investors. However the allegations could not be substantiated through a court decision. Frequent allegations of insider trading involving manipulation of stock prices through false announcement and abuse of market-making power have been advanced during the early stages of the privatization program, notably in the context of public offerings. One ought to remember that during the privatization of major bank, TÜRKBANK, the government in power collapsed following revelations involving the government’s alleged behind-the-closed-door dealings with a potential bidder. This case constituted the most striking case of alleged corruption involving privatization deals in Turkey.
  21. For a good discussion of the Privatization Law of 1994 and its implications for the subsequent course of privatization in Turkey, see Celasun and Arslan (1997).
  22. For a critical assessment of the Turkish privatization experience in the field of telecommunications from a comparative perspective with a specific focus on the legal framework, see Ba<sup>o</sup>aran and Özdemir (1998).

23. The constitutional amendment has been finally made by securing the long awaited two-thirds majority needed.
24. The enterprises concerned are currently among the largest manufacturing establishments in Turkey. For example in 1998, according to the largest 500 industrial establishments in Turkey survey, published by the Istanbul Chamber of Industry, TÜPRA<sup>a</sup> is ranked first, ERDEMÝR is seventh and PETKÝM is tenth. One should note that a very small proportion of shares of these enterprises have been sold to the public and these sales have been accomplished in the early stages of the program with little or no progress in the subsequent periods. Yet, the shares sold as a proportion of the total equity of the enterprises concerned remains unusually low. Currently, the highest percentage is recorded in the case of PETKÝM (4.14 percent). The corresponding figures for TÜPRA<sup>b</sup>, THY and ERDEMÝR are 1.64, 1.55 and 2.93 percent respectively. For evidence, see DPT (1998).
25. In 1996 alone four presidents have been in office
26. Between 1996 and 1997, three governments have been formed. During the period concerned, all presidents and almost all vice-presidents of the PA have been removed from the office right after the new government received the vote of confidence from the parliament.
27. For evidence on the persistence of macro-economic instability in Turkey during the 1990s and investigations of the underlying causes of this instability, see Özatay (1996), Atiyas and Sayýn (1998), Öni<sup>c</sup> (1998 and 2000), Boratav et al. (1999), and Yentürk (1999).
28. The stop-go pattern of economic growth which heavily relies on inflows of short-term external capital in response to high domestic interest rates have been analyzed, among others by Öni<sup>c</sup> (1998) and Yentürk (1999).
29. For evidence on a positive relationship between privatization, efficiency and economic growth, see Galal et al. (1994). The authors are careful to emphasize, however, that the context in which privatization is engineered is crucial to subsequent economic performance. Much will depend on how the sale is transacted, the market structured and the firm regulated

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