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Introduction

MOST COUNTRIES AROUND THE WORLD have experienced significant increases in per capita income and improvements in human development during the last two centuries. Turkey's performance in economic growth and human development has been a little above but close to developing-country and world averages. This book aims to establish that record in a global comparative framework for the first time and explore why Turkey's economic performance has remained close to the averages.

The economics and economic history literature has been emphasizing in recent decades that the proximate causes of economic growth, namely the economic variables such as the increases in inputs, land, labor, and capital, and the productivity increases brought on by investments in physical and human capital as well as advances in technology, can provide only a partial explanation. We also need to address the deeper causes for economic growth, particularly the social, political, as well as the historical causes that influence the rate at which inputs and productivity grow. In recent decades, a still developing literature has renewed the argument that for deeper causes, we need to study the institutions defined as written and unwritten rules of a society and their enforcement that affect the incentives to invest and innovate.

Two of Turkey's special features as a developing country are that it has not been subject to colonial rule and that it has experienced waves of top-down institutional changes brought about by its own modernizing elites during the last two centuries. The Ottoman government launched a detailed reform program in 1839. The new nation-state established after World War I continued the secular modernizing reforms in law, administration, education, and elsewhere. Turkey's political system was opened to greater participation and competition after World War II with the transition to a multiparty system which gave greater voice and power to average citizens. Turkey's formal economic institutions and economic policies also experienced a great deal of change during the last two centuries. In each of the four periods I will define herein, governments adopted economic institutions and economic policies that were consistent with the most commonly adopted institutions and policies in the developing countries around the world.

Not all of these changes in formal institutions have supported or enhanced economic growth and development. In fact, some were designed more to support the interests of certain groups than to bring prosperity to all. Nonetheless, many of these institutional changes were designed to and did lead to increases in per capita income and improvements in human development. How did these changes in formal political and economic institutions bring about average rates and why did they not bring about higher rates of economic growth and human development? The answer is not simple and the state of our knowledge is not sufficient for a precise answer. Nonetheless, I will explore the causes in a global comparative framework.

This chapter provides an overview of the book. I will begin by summarizing Turkey's record in economic growth and human development both in absolute and comparative terms. I will then discuss the proximate causes by focusing on investment, accumulation of inputs, technology, and productivity. The deeper causes of Turkey's record in economic development relate to the broader environment, including the social and political environments as well as institutions. I will offer an overview of the recent literature in the role of institutions in long-term economic development and then summarize my argument about the role of institutions and how and in what respects they mattered in the case of Turkey.

Economic Growth and Human Development since 1820

For thousands of years, per capita production and income levels around the world had remained close to subsistence. Even if a society managed to raise per capita incomes, the increases could not be sustained for long. This pattern has changed dramatically in the last two centuries, however. Technological progress began to accelerate in the aftermath of the Industrial Revolution and a higher share of incomes began to be set aside for investments in physical and human capital. Economic growth, defined as lasting increases in per capita production and income, became the fundamental process that determined the wealth or poverty of nations.

Today, most countries in the world have average incomes that are much higher than their levels in 1820. In Britain, the first country to experience the Industrial Revolution, for example, per capita income in 2010 was approximately twelve times that of 1820. Countries or regions did not all grow at the same rate during the past two centuries, however. Countries in Western Europe and North America, which began industrializing early, grew at a faster pace until the middle of the twentieth century. In contrast, the majority of the countries currently referred to as developing experienced limited or no increases in per capita incomes until after World War II, when they began their process of industrialization. Since the end of World War II, a limited number of countries, including Italy, Japan, and South Korea, began to close the gap with high-income countries, thanks to high rates of economic growth. In addition, the pace of economic growth has picked up in the past thirty years in the world's two most populated countries, China and India, and more generally in East and South Asia. Nonetheless, the gap between the early industrializers and developing countries is not smaller today than it was in 1950. In other words, the disparities between the countries, which began industrializing in the nineteenth century and are now developed, and those that started their industrialization later and are currently developing, are much larger today than they were two centuries ago.

Economic growth or increases in per capita income cannot be the only goals or the only measures used to evaluate economic performance. Economists and social scientists argue that in any assessment of long-term economic performance, quality of life, income distribution, health, education, and changing environmental conditions need to be taken into account, as well as production and income. Aside from income or GDP per capita, the measure most widely used to evaluate the development of economies in recent years has been the human development index, which gives equal weight to health and education, in addition to GDP per capita.

The pattern of improvements in health around the world during the last two centuries has also been uneven and followed broadly the pattern of GDP per capita. Life expectancy at birth, the most basic measure of health, first began to rise in Western Europe and the Western offshoots during the nineteenth century while it rose very slowly if at all in the rest of the world. Since the end of World War II, however, along with GDP per capita, life expectancy began to increase rapidly in the developing countries. In fact, a global convergence in life expectancy has emerged since 1950, with life expectancy in most parts of the developing world approaching those of the developed countries.

It is more difficult to develop simple measures of education, the other component of the human development index, but there is a broad correlation between the pattern of GDP per capita and years of schooling of the adult population around the world during the last two centuries. Years of schooling of the adult population rose much more rapidly in Western Europe and North America until World War II, and, as in GDP per capita but unlike life expectancy at birth, there has not been any catch-up, at least in terms of years of schooling, between the early industrializers and the developing countries since.

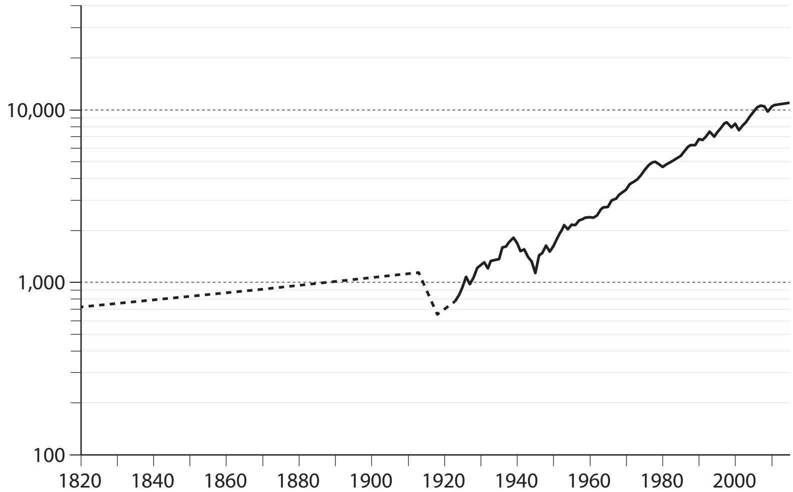

FIGURE 1.1. GDP per Capita in Turkey, 1820–2015 (PPP adjusted and in 1990 US dollars). Sources: Pamuk 2006 for Turkey until 1950; Maddison 2007, pp. 375–86; Bolt and Van Zanden 2014; also see the discussion and sources cited in chapter 2.

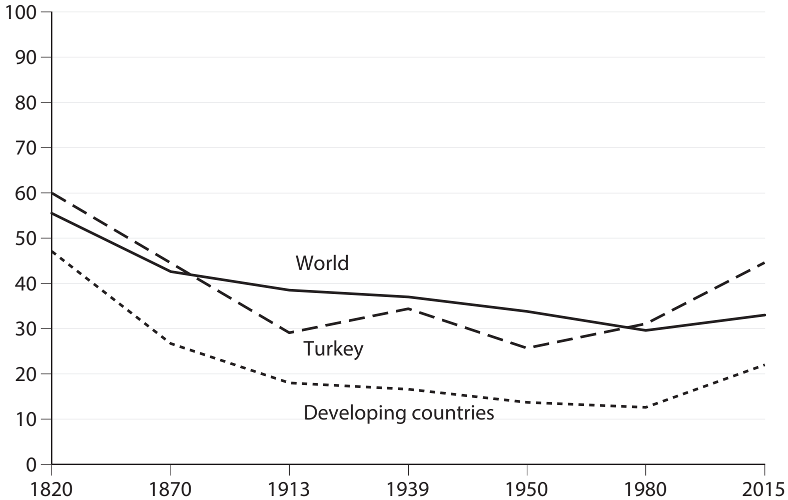

FIGURE 1.2. GDP per Capita in Turkey and the World, 1820–2015 (PPP adjusted and as percentage of Western Europe and the United States). Sources: Pamuk 2006 for Turkey until 1950; Maddison 2007, pp. 375–86; Bolt and Van Zanden 2014; also see the discussion and sources cited in chapter 2.

This book presents for the first time a GDP per capita series for Turkey since the year 1820. This will be an important part of the evidence for evaluating Turkey's absolute and relative economic performance. As I will discuss in greater detail in the next chapter and in the rest of the book, GDP per capita in the area within Turkey's current borders has increased approximately fifteenfold, and Turkey's rates of economic growth have been close to world averages during the last two centuries. Economic growth in Turkey began in the nineteenth century and per capita incomes more than doubled until 1950. However, long-term rates of increase of per capita income remained below 1 percent per year during this period (figure 1.1). Even though Turkey did better than the averages for the developing countries from 1820 until 1950, the gap with developed countries continued to widen. The most basic reason for this pattern was the relatively rapid industrialization in Western Europe and North America while Turkey as well as other developing countries stayed mostly with agriculture. In the case of Turkey, there was a spurt of industrialization and high rates of growth during the 1930s, but those gains were reversed during and after World War II. Per capita incomes in the area within Turkey's current borders declined from 60 percent of average per capita income in Western Europe and the United States in 1820 to 26 percent in 1950 (figure 1.2).

As is the case for most developing countries, long-term growth rates have been significantly higher since the end of World War II. As urbanization and industrialization picked up, annual rate of increase of per capita income rose above 3 percent, and per capita income increased more than sixfold between 1950 and 2015. As a result, per capita incomes in Turkey rose from 26 percent of the per capita income in Western Europe and the United States in 1950 to 31 percent in 1980 and 43 percent in 2015. Between 1950 and 1980, per capita incomes in Turkey have increased at rates slightly higher than the population-weighted averages for the developing countries of Asia, South America, and Africa. Turkey's growth rates continued to be higher than the averages for South America and Africa since 1980. However, the two large developing countries, China and India, and more generally East, Southeast, and most recently South Asia have experienced significantly higher rates of growth than Turkey in recent decades.

Comparisons with four countries with similar populations in southern Europe and the Middle East will provide additional insights into Turkey's long-term trajectory. Early in the nineteenth century Italy and Spain had higher levels of GDP per capita in comparison to Turkey. They began their industrialization during the nineteenth century and achieved higher rates of growth than Turkey during the nineteenth century and the Interwar period primarily because the rates of industrialization were lower in Italy and Spain than in the developed countries. Italy and Spain experienced very high rates of economic growth and were able to converge more significantly than Turkey to the level of the developed countries since the end of World War II. Compared to Turkey, Egypt and Iran had slightly lower levels of GDP per capita early in the nineteenth century and they experienced lower rates of economic growth during the nineteenth century. The GDP per capita levels remained unchanged in Egypt during the Interwar period and the gap with the developed countries widened further until 1950. In contrast, Iran was able to raise its GDP per capita to Turkey's levels in 1950 thanks to large revenues from oil. From the end of World War II until 2015, the GDP per capita gap with Turkey continued to widen. With the support of oil revenues, Iran's GDP per capita remained above that of Turkey until 1980 but has fallen behind since.

A small number of countries in southern Europe like Italy and Spain, and others in East Asia such as Japan and South Korea, as well as Hong Kong and Taiwan, have produced "economic miracles" and were able to significantly close the gap with developed countries since the end of World War II. During each of these catch-up or convergence episodes, annual rates of increase in per capita incomes in these countries remained higher than 5 percent for a period of at least 20–30 years. Turkey's economic growth performance did not come close to the catch-up performances exhibited by these more successful examples. In Turkey, increases in GDP per capita never reached 5 percent during any subperiod in the last two centuries. After falling significantly behind the developed countries during the nineteenth century and until 1950, Turkey's catch-up has been rather limited since. In short, Turkey's long-term growth performance has been close to but slightly higher than the averages for developing countries and close to the averages for the world during the last two centuries.

The pattern of improvements in health and education in Turkey since 1820 is correlated with but not identical to that in GDP per capita. Improvements in health and education in Turkey were also slow in the nineteenth century but they have picked up pace after World War I and especially World War II. Life expectancy at birth in the area within present-day borders increased slowly from about 26–27 years in 1820 to 44 years in 1950. While life expectancy at birth in Turkey remained slightly higher than the averages for the developing countries as a whole, the gap in life expectancy at birth between Turkey and the developed countries increased significantly during the nineteenth century and until 1950. Together with higher rates of economic growth, life expectancy at birth began to increase rapidly after the end of World War II, by almost one year in every two years or by more than 30 years between 1950 and 2015. As a result, the gap with the developed countries in life expectancy at birth closed significantly since the end of World War II for Turkey and for developing countries as a whole.

Turkey's experience with education shows a broadly similar pattern of slow improvement during the nineteenth century and more rapid improvement during the twentieth century, especially since the end of World War II. Despite the education reforms in the nineteenth century, schools and schooling did not spread to rural areas where the great majority of the population lived because of fiscal constraints and because the new schools were not easily accepted by the Muslim population. Literacy rates for the adult population increased slowly during the century and were only slightly above 10 percent on the eve of World War I. In the Interwar period, the overall literacy rate rose faster but educational efforts remained limited mostly to the urban areas and did not reach the rural areas where a majority of the population lived. The overall literacy rate stood at 33 percent in 1950 but rose to 68 percent in 1980 and 95 percent in 2015. Progress was even slower among women.

Since literacy rates from the early periods are not easily available for most developing countries, for international comparisons we need to turn to another basic indicator. Average years of schooling for the adult population over age 15 remained well below 1 year during the nineteenth century and edged up to 1.5 years by 1950. It has since risen to more than 7 years. Data from other regions indicate that in this basic education indicator, Turkey has lagged behind not only the world averages but also the averages for the developing countries as well as the countries with similar levels of GDP per capita for most if not all of the last two centuries. One important cause of this poor performance is the existence of large and persistent gender inequalities. Turkey's low rankings in health and education are also a result of the large regional inequalities and low levels of health and education as well as per capita income in the southeast region, where the majority of the Kurdish population live.

Proximate Causes and Deeper Determinants

For a long time, economists have focused on the proximate causes of economic growth, namely the increases in productivity brought on by investments in physical and human capital as well as advances in technology and organizational efficiency. In recent decades, however, the focus has been shifting from the proximate causes toward the deeper determinants. The latter refer to aspects of the social, political, and economic environments that support and bring about these investments and at the same time determine the extent to which they are productive. The growing recognition that rates of investment and rates of productivity growth are not exogenous but are determined by a variety of factors, both economic and non-economic, has supported the search for deeper determinants. Evidence has been building up in recent years that some part of the international variation in per capita income is explained by the fact that long-term causes such as resource endowments and geography, culture, education, and institutions that interact with each other impact economic growth as a result of deeply interlinked historical processes. Consequently, it has been very difficult to disentangle them and treat the impact of each of these causes separately.

In recent decades a diverse and still developing literature has renewed the argument that institutions, defined as written and unwritten rules of a society and their enforcement, play key roles in promoting economic development. According to this literature, more complex and advanced forms and innovations that lead to increases in productivity can only emerge if institutions or rules and their enforcement in a society encourage and support activities to that effect. Laws supporting production and investment and their enforcement, equality before law, and opening the economy to broader sections will encourage the formation of new partnerships and they will encourage individuals from different sections of society to develop their talents and engage in economic activity.

While research on institutions is still in its early stages, institutions are increasingly seen as more fundamental determinants of economic development and of long-term differences in per capita GDP between countries than rates of physical and human capital accumulation or research and development themselves. Recent studies also suggest not only that rates of physical and human capital accumulation are higher and new technologies are developed in countries with better institutions but also that the existing physical and human capital stock are used more efficiently and the productivity of the existing physical and human capital stock is higher in those countries with better institutions. In other words, differences in the quality of institutions are also seen as the main cause behind the intercountry differences in human capital formation and total factor productivity.

Included among institutions are the written or formal rules or laws legislated from the top down that facilitate economic exchanges by enforcing contracts, protecting property rights, and monitoring all parties to ensure that they adhere to their commitments. Formal institutions did not all originate with states, however. Family, kinship and ethnic ties, religious networks, patronage networks, coalitions, business partnerships, guilds, and foundations are all examples of informal arrangements that began as small-scale, bottom-up efforts in order to regulate and reduce uncertainty in economic life and to develop cooperation between different individuals and groups. Over time, many of these institutions began to be enforced at least partly by the state. The developing literature emphasizes the key role played by political institutions.

The distribution of political power and interests as well as the formation of alliances and coalitions among the elite will influence the choice of political and economic institutions.

Institutions are not limited to formal rules enforced by the state. Large numbers of informal institutions are self-enforced or enforced by non-state actors. These privately organized arrangements, typically built from the bottom up within communities and rooted in social networks, usually do not work by themselves but interact or work together with constellations of other informal and formal institutions. In fact, informal institutions are often necessary for formal arrangements to work properly. In order to understand the role of institutions, it is necessary to understand how the formal and informal institutions interact and create pressures for institutional configurations that may contribute to or prevent growth. In the longer term, for the emergence of economic transactions, cooperation, and partnerships involving larger numbers of people and more complex organizations, some but not necessarily all of the private order or informal institutions need to be replaced by more universalistic and formal arrangements.

External forces have also played important roles in shaping the institutions of a given society. The cases of colonies or formal colonies in which an outside power shapes formal institutions are examples of recent and direct external influence. Equally important during the last two centuries has been the influence of international or global rules such as free trade, the gold standard, and the Bretton Woods system of rules and organizations that were shaped after World War II. More recently, the Washington Consensus principles such as reliance on markets, trade liberalization, and privatization which are often enforced either by the leading global powers or international agencies have influenced formal economic institutions including policies.

There is growing consensus in the literature that the role of the state in economic development is not limited to providing external and internal security, protecting property rights, and enforcing contracts. The state also plays a key role in the formation and enforcement of institutions as well as their development and evolution over time. Historically, the relations between competing elites and their relations to the state have been critical in the formation of the state and state policies. Reaching an understanding if not consensus between elites and harnessing the different powers and capacities of the various elites was a key aspect of state formation and state policies. When the distribution of benefits from an existing institution or a new institution was not consistent with the existing distribution of power in society, the various elites could mobilize, bargain, and put pressure on others as well as the state to try to bring formal and informal institutions back into line. In other words, the extent to which formal institutions could be enforced or to which rule of law prevails often depended on the relations and the degree of understanding between the various groups as well as their elites and the state.

The experience of Britain and the later industrializers in Europe both during the early modern era and the nineteenth century shows that states played key roles in economic development not only by providing security and enforcing laws and contracts, but also by supporting markets and long-distance trade, and in most cases protecting domestic production against foreign competition. States in today's developing world had limited capacity and played limited roles in economic development during the nineteenth century. Since the 1930s and especially after World War II, state interventionism in the economy spread rapidly and states in some developing countries, most notably in East Asia, played key roles in industrialization. The existence of such examples does not mean, however, that state interventionism will always produce results that favor economic development and industrialization. As the results of attempts to replicate the East Asian experience with industrialization confirm, even if the same formal institutions and the same economic policies are adopted, the outcomes can be very different because new institutions interact with other existing institutions as well as the existing social structure and distribution of power.

While the new and growing literature has provided both a theoretical framework and empirical evidence that institutions matter for long-term economic development, it also has some significant limitations. For one thing, how economic institutions are shaped and why they vary across countries is not well understood. The literature has so far not examined in detail the mechanisms through which they shape economic and political outcomes. Similarly, the recent literature has not addressed adequately how institutions may change in the longer term. Here, more attention needs to be paid to the role of agency, the role of different groups in bringing about institutional change. In other words, while evidence is growing that institutions matter, we need to learn more about how they are shaped, how they work, how they persist, and how they change.

At its broadest, the new literature is an attempt to shed light on how economic behavior and outcomes are mediated by the institutional setting in which they take place. The interaction between institutions and economic change, technology, politics, social structure, distribution of power, beliefs, ideologies, and expectations also work both ways. Institutions influence the others but are also influenced by them. Similarly, institutions shape behavior and relations among the various actors and, in turn, are shaped by them. Institutions thus influence behavior, but they are not the sole cause of outcomes. While it may be easier to isolate the effect of institutions on economic development if we believe that institutions evolve independently of the path of economic development, it will not be easy to do so if the other variables also influence the evolution of institutions. The analysis of the role of institutions is more complicated and the case for attributing economic growth to institutions alone is weaker if institutions are endogenous and are influenced by economic change as well as the other variables. Nonetheless, to acknowledge that institutions are influenced by the other variables does not imply that institutions do not matter or that they have only limited impact on economic performance.

Turkey's performance in economic growth and human development has been close to developing-country and world averages. I will argue in the rest of the book that this pattern cannot be satisfactorily explained with reference only to the proximate causes such as rates of investment in physical and human capital and productivity growth. In order to better understand this record, it is also necessary to analyze the deeper causes, most important among them Turkey's institutions, including policies and their evolution. I will argue that while institutions are not the only thing that matters, it is essential to understand their role in order to evaluate Turkey's economic growth and human development performance during the last two centuries. In the following overview I aim to illustrate this distinction regarding the causes of economic growth in the case of Turkey.

Proximate Causes for Turkey since 1820

The basic proximate cause of the growing gap between Western Europe and much of the rest of the world during the nineteenth century was the very different rates of adoption of the new technologies. The steam-powered engines of the Industrial Revolution and other new technologies that followed were introduced first in Western Europe and North America. As investments in these technologies spread, productivity increased sharply in industry, transport, and to a lesser extent in agriculture. Conversely, in Turkey and in most developing countries, industrialization remained limited and the adoption of the steam engine and other new technologies occurred slowly and mostly in transport during the nineteenth century.

Population of the area within Turkey's current borders increased from about 10 million in 1820 to 17 million in 1914. Close to half of this increase was due to immigration. A large part of the slow increases in per capita GDP and incomes in Turkey during the same period were achieved by the expansion of agricultural production for domestic and export markets owing to the improvements in maritime shipping and the construction of railroads. These changes enabled rural households to specialize more in agriculture by increasing their labor time and cultivating more land to produce more cash crops for markets. Technological change in agriculture was slow, however. Mechanization in agriculture remained limited to small pockets of export-oriented production. Rates of aggregate investment were not higher than 5–6 percent of GDP for most of the century and rose to as much as 8 percent during the decades before World War I. As much as one-third of the investments in fixed capital after 1880 were undertaken by European companies that concentrated in railroad construction, infrastructure for foreign trade, and urban utilities. Low rates of investment, slow spread of the new technologies, and slow increases in productivity in agriculture and to a lesser extent in trade are the leading proximate causes of the low but positive rates of economic growth before World War I. Rising but low levels of state expenditures as well as the slow diffusion of new technologies also led to slow improvements in health and education (figure 1.3).

Turkey's population decreased by 20 percent during and after World War I. The large declines in the numbers of Greeks and Armenians, as well as Muslims, had long-term economic as well as political and social consequences. After the disintegration of the Ottoman Empire and the emergence of a new nation-state following World War I, Turkey gained the right to establish its own tariffs beginning in 1929. In response to the Great Depression and the collapse of agricultural prices, an important shift took place in economic strategy. Industrialization was embraced as the new engine of economic growth and protectionism was adopted as the key economic policy for this purpose. Rates of investment mostly in manufacturing and more generally in the urban economy, financed almost entirely with domestic savings, averaged 10 percent of GDP during the 1930s (figure 1.3). The new technologies began to spread in the urban economy. However, agriculture, which continued to employ close to 80 percent of the population, turned inward and remained mostly insulated until after World War II.

Turkey's population increased from 21 million in 1950 to 44 million in 1980 and 79 million in 2015. Urbanization was slow during the nineteenth century and the shift of labor from agriculture to the urban sector accelerated only after World War II. As some of those previously engaged in agriculture began migrating to urban areas to work in industry and services which, on the whole, used more advanced technologies, average labor productivity began to grow more rapidly. Estimates indicate that more than a third of all the increases in labor productivity and per capita income achieved in Turkey since 1950 have been due to the shift of labor from the low-productivity agricultural sector to the more productive urban economy. Share of agriculture in total employment declined from 75–80 percent in 1950 to 50 percent in 1980 to less than 20 percent in 2015, while share of the urban economy in employment increased

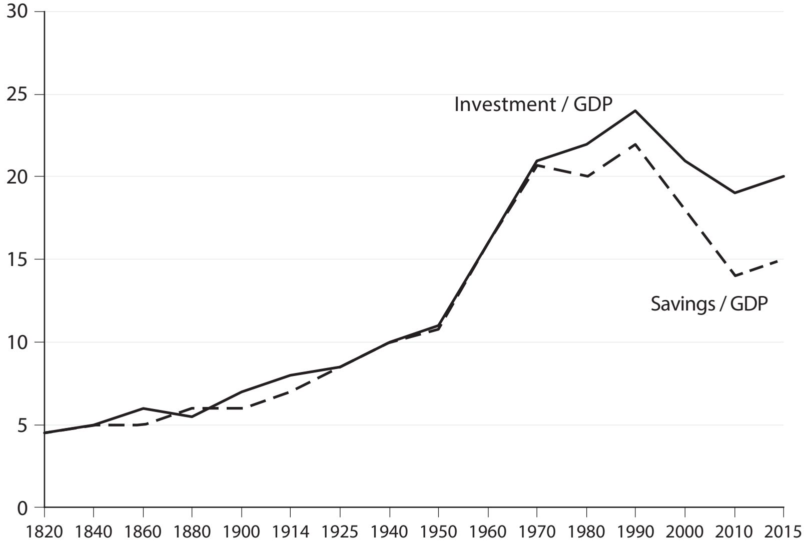

FIGURE 1.3. Savings and Investment Rates in Turkey, 1820–2015 (as percentage of GDP). Sources: Author's estimates until 1913 and official series from Turkey, Turkish Statistical Institute 2014 and Turkey, Ministry of Development 2017 for the period since 1923.

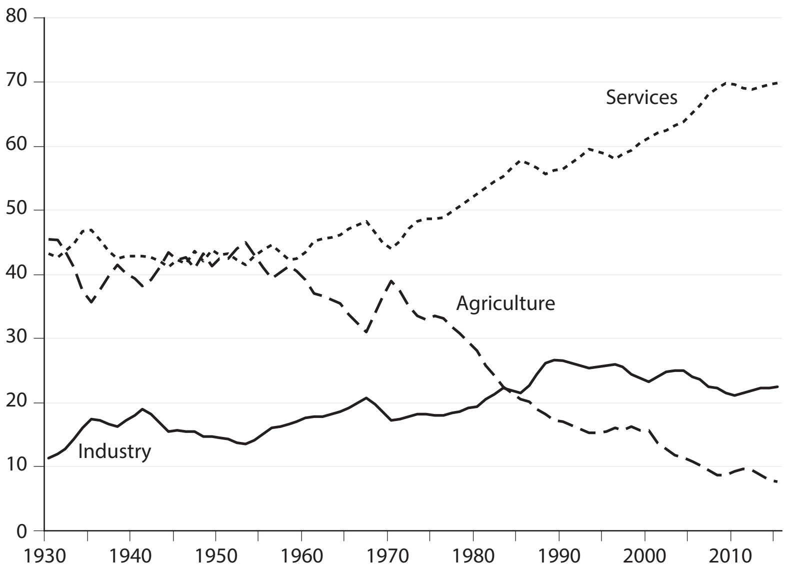

FIGURE 1.4. Changing Sectoral Shares in Turkey, 1930–2015 (three-year moving averages as percentage of GDP). Source: Based on the national income accounts in Turkey, Turkish Statistical Institute 2014.

from 20–25 percent in 1950 to more than 80 percent in 2015. The share of the urban economy in GDP also increased from about 58 percent in 1950 to 75 percent in 1980 and to 92 percent in 2015. Rates of growth of manufacturing industry averaged more than 8 percent per year and the share of manufacturing in total labor force edged upward between 1950 and 1980. However, rates of growth of manufacturing industry slowed to about 5 percent per year and its share in total employment stagnated since 1980 while the share of services in both employment and GDP continued to rise (figure 1.4).

Higher incomes allowed for higher savings rates and higher rates of investment in the more productive technologies. Investment rates rose from 11 percent of GDP in the early 1950s to 22 percent of GDP in the 1970s (figure 1.3). Most of these investments were financed with domestic savings. In contrast to the period before World War I, foreign direct investment remained limited during the Interwar period and also during the decades after World War II. In the more recent period since 1980, the aggregate investment rate did not rise any further and averaged 21 percent of GDP. As the savings rate began to decline after 1998, an increasing share of investments was financed with foreign capital inflows, mostly short and medium term. The resulting current account deficits and stop-go cycles associated with foreign capital inflows have emerged as a serious source of instability for the economy. While there were medium-term fluctuations in average growth rates due to domestic politics and their impact on macroeconomic stability, the average rate increases in GDP per capita have been similar in the two periods, 1950–1980 and 1980–2015, at approximately 3 percent per year.

Another potential source for the increases in productivity in both agriculture and the urban economy was the more efficient use of existing resources, in other words, increases in total factor productivity. As was the case in most developing countries during this period, however, total factor productivity increases remained limited in Turkey since World War II, at around 1 percent annually. Moreover, a large part of this increase was due to urbanization and the shift of labor from agriculture to the urban economy mentioned earlier. In other words, only a small fraction of the increases in total GDP were obtained through more efficient use of the inputs. The rest were due to the accumulation of more inputs, especially physical and to a lesser extent human capital. In fact, while rates of physical capital formation in Turkey since World War II have been close to the averages of other countries with similar levels of per capita income, rates of human capital formation have lagged behind. Levels of education and skills obtained by women, Kurds, and rural population have lagged even further behind.

Broadly speaking, then, with the exception of a spurt in the 1930s, rates of investment remained low and rates of increase of GDP per capita remained below 1 percent from 1820 to 1950. Rates of investment increased and rates of increase of GDP per capita averaged above 3 percent per year since 1950. Higher growth rates since 1950 were also due to the shift of labor and other resources from agriculture to manufacturing and services. Turkey's rates of investment and growth have been close to long-term averages for the developing countries and the world as a whole. These proximate causes provide insights into the rise in productivity and the pattern of economic growth in Turkey in both absolute and relative terms. They do not tell us, however, why rates of investment in physical and human capital were not higher, why investment in technological innovation lagged behind, and why rates of growth in total factor productivity have remained low in Turkey since 1950. For answers to these questions, we must turn to the deeper determinants of economic growth and development.

Deeper Causes for Turkey since 1820

Although research on institutions and their role in long-term economic development in Turkey is in its early stages, a good deal of evidence does exist and this book will emphasize that in each period new institutions have facilitated some economic growth and at the same time created obstacles in the way of further growth and development. To understand the role of institutions in economic development in Turkey, it is necessary to understand how formal and informal institutions interacted and created pressures for institutional configurations that contributed to or prevented economic development. It is also necessary to examine how formal and informal institutions have interacted with economic development and social structure.

There was some popular support and also some support among the elites, but much of the formal institutional changes Turkey experienced during the last two centuries, especially those in the earlier period, have been top-down. In the Ottoman Empire before the nineteenth century, the economic elites, landowners, merchants, manufacturers, and money changers had enjoyed a good deal of local power and autonomy, but they were not represented in central government. Similarly, the nineteenth-century reform program called *Tanzimat*, literally re-ordering, enjoyed some support among the elites including the provincial notables, but it was designed and launched by the Ottoman central government. The reforms promised all Ottoman subjects, Muslim and non-Muslim, the same basic rights and equality before the law. The Tanzimat also promised to strengthen property rights and end the centuries-old practice of confiscating the wealth of government officials who had lost their positions. During the nineteenth century, the Ottoman government attempted to create a modern bureaucracy and a new educational system as well as reform the legal system and the tax collection system. There were also some changes in political institutions. The first constitution and a parliament with elected as well as appointed members that opened in 1876 could last only one year, but they both returned after the Young Turk Revolution of 1908.

Top-down institutional changes were continued after the end of the Ottoman Empire and the emergence of Turkey as a new nation-state following World War I. The radical modernizing reforms of the new republic built upon the secularization of state, law, and education begun one century earlier. With the adoption of the Swiss civil code and the Italian penal code in 1926, the linkages to Islamic law were abolished entirely. The public education system was completely separated from religion and the religious schools were closed in 1924. The public schools and some areas in civil service and the professions were opened in greater numbers to urban, middle-class women who embraced the new secularism of the republic. Following a few years with a pluralist parliament, however, the new regime in Ankara turned more authoritarian after 1925, eliminating the opposition in parliament and creating a one-party political system.

The political system was opened to greater participation with the transition to a multiparty system and regular elections after World War II. As urbanization began to gain momentum, the transition to a more open and competitive political system gave greater voice and power to the ordinary people, both rural and urban. At the same time, however, a series of military coups until the end of the century ensured that the military closely controlled the political system, guarding secularism and restricting political freedoms including the rights of the Kurdish minority.

Turkey's formal economic institutions and economic policies underwent extensive changes during the last two centuries. In each of the four periods I will define, the formal economic institutions as well as economic policies adopted by the governments have been influenced by the international or global rules such as free trade, the Bretton Woods system, and Washington Consensus principles which were enforced either by the leading global powers or more recently by international agencies. In fact, I will show that in each of these four periods, governments in Turkey adopted economic institutions and economic policies that were consistent with the most commonly adopted institutions and policies in the developing countries around the world at the time.

During the nineteenth century, in exchange for the support of the European states for the reforms, the Ottoman government agreed to pursue laissez-faire policies and keep the economy open to foreign trade and foreign investment. The economic institutions of this period were shaped to a large extent by the bargaining between the central government and the European states.

The open economy model of the nineteenth century ended during and after World War I. Interventionism, protectionism, and greater emphasis on national economies emerged as new principles guiding economic policy. With new political institutions and new leadership, the new nation-state strived to create a national economy within the new borders during the Interwar era. In response to the Great Depression, the government adopted protectionism and pursued a state-led industrialization strategy.

Protectionist and inward-looking policies continued after World War II. Along with the shift to multiparty politics, however, the private sector increasingly took control of the economy in the post–World War II decades. After 1980, economic policies and institutions of the inward-looking industrialization era were abandoned in favor of Washington Consensus principles, most important, greater emphasis on markets, trade, and financial liberalization and privatization. The customs union agreement signed with the European Union in 1994 helped foster the growth of exports of manufactures.

These extensive changes in formal political and economic institutions played important roles in bringing about significant increases in per capita income as well as major improvements in health and education since 1820. Changes in formal institutions have been only part of the story, however. In order to understand the role of institutions, this book will also explore how the formal and informal institutions interacted and how they interacted with economic change, social structure, the distribution of power and expectations, and whether the new institutional configurations that emerged were growth-enhancing or growth-inhibiting.

The diffusion of the new formal institutions was slow during the nineteenth century and the first half of the twentieth century. The privately organized arrangements built from within communities and rooted in informal social networks continued to coexist with and often substituted for formal institutions in both urban and rural areas. With urbanization and economic growth as well as improvements in health and education after World War II, the fiscal, administrative, and legal capacities of the state also increased. These broad developments did not mean the disappearance of informal institutions, however. On the contrary, with rapid rural to urban migration, patronage, regional solidarity, and religious networks developed further and flourished in the urban areas since 1950, interacting with formal institutions and creating new institutions.

I will argue that there were a number of important reasons why formal institutions did not crowd out informal institutions but continued to coexist with informal institutions since the nineteenth century. First, many of the reforms were rather costly and required effective implementation and enforcement. In contrast, the fiscal, administrative, and legal capacities of the state were limited, especially in the earlier periods. The rural areas remained especially insulated from the top-down, secularizing reforms of the government. Second, the new formal institutions were not modular constructions but often interacted with other institutions. Other formal as well as informal arrangements were often necessary for the workings of the new formal institutions. At least some of these institutions were shaped by values, beliefs, and social norms as well as interests and distribution of power. While political institutions and laws could change very quickly, sometimes literally overnight, values, beliefs, social norms, and related institutions changed more slowly. Third, the design and implementation of the formal institutions remained top-down and they were not fully embraced by the public at large. In many situations, powerful groups tried to prevent changes because they believed that the new institutions would damage their own interests. In the earlier periods, opposition to the reforms also came from those who had controlled and benefited from some of the Islamic-Ottoman institutions. The opposition used both formal and informal institutions as strategic resources in the conflicts over distributional benefits and tried to undermine the new institutions.

I will offer examples throughout this text of how the new formal institutions interacted with informal institutions in various areas, ranging from the spread of education in rural areas and efforts to secure housing and access to local government services by recent migrants in urban areas, to the organization of the private sector to relations between the private sector and the government and more generally the workings of state interventionism in the economy. These examples will illustrate not only that the informal institutions continued to play important roles in the economy but also that the new formal institutions functioned differently as they interacted with the informal institutions as well as with social structure and the distribution of power.

Cleavages

The preceding discussion emphasized the importance of the two-way interaction between formal and informal institutions as well as the two-way interaction between institutions and economic outcomes. It also pointed to the importance of another two-way interaction, that between institutions and social structure. Institutions shape social structure not only through their influence on economic outcomes but also directly through their influence on the behavior of various actors as well as the relations among these actors. For example, formal and informal institutions play key roles in enhancing the ability of different social groups to solve their collective-action problems and pursue their common interests. Formal and informal institutions thus may contribute to and may also impede the cohesion and strength of different social actors. In turn, the social structure made up of many groups with diverging interests, alliances, and cleavages will influence the institutions. Formal and informal institutions shaped by trust and cooperation and other norms or their absence influence how these differences are handled, whether they are resolved or intensified. When the differences are not handled well, the result will often be political and economic instability as well as uncertainty, which will have significant implications on long-term economic development.

In Turkey since the nineteenth century, class cleavages have always mattered although their intensity varied over time in both urban and rural areas. Equally important have been the identity cleavages between the social groups and also between their elites. Some of these cleavages date back to the beginnings of the secular modernization project in the nineteenth century. The rise of Kurdish nationalism in the twentieth century added another dimension to them. In fact, the intensities of the identity cleavages between Muslims and non-Muslims, between seculars and conservative Muslims, Sunnis and other Muslims, between Kurds and Turks have at times been more important than those of class cleavages. While the identity cleavages often appeared to be based on culture, they often overlapped with competing economic interests between the different groups and between their elites. Rulers, politicians, and other elites often used Islam and exaggerated the existing cleavages to gain support among the population.

The configurations between the state and the elites and the various other groups, their alliances, coalitions, and cleavages varied considerably during the last two centuries. In each period, the relations, coalitions, and cleavages were also influenced by the global institutions and the economic models and policies allowed by the global economic system. The identity cleavages have made it more difficult for alliances and coalitions to emerge between the different elites. The cleavages also had negative consequences for state capacity and the ability of the state to enforce the formal institutions. Reaching an understanding if not consensus between the elites including the state elites and harnessing their different powers and capacities, as well as dealing with various collective-action problems, have been critical for the successful enforcement of the new institutions not only at the macro level but also at the micro level. If the distribution of benefits from an existing institution or a new institution was not consistent with the existing distribution of power in society, the various elites could mobilize, bargain, and exert pressure on others as well as the state to try to bring formal and informal institutions back into line. In these conflicts the competing elites often made use of informal institutions, including identity-based networks and patron-client relations.

The cleavages between the various competing elites, between the Muslims and the non-Muslims, the private elites and the state elites, between the secular and conservative elites, and between Turks and Kurds not only undermined state capacity, but they have often made it difficult to maintain political stability. Political order, which depends on the degree of understanding and consensus between different groups in society regarding basic rights, how to resolve conflicts, and the behavior of the state about the rules and their enforcement, is a necessary condition for political and economic development. By changing expectations and beliefs, increasing political uncertainty and instability can cause political and economic actors to behave very differently. The frequent military coups that occurred during the decades after World War II and the recent slide to authoritarianism indicate that Turkey's political system has not been able to manage these cleavages well.

The recurring periods of political instability have had adverse consequences for economic development both in the short and the longer term. In the multiparty era since the end of World War II, periods of political instability have typically resulted in growing macroeconomic problems and lower rates of economic growth. Even more important, the persistence of cleavages between elites, the use of informal networks as well as the mixed outcomes associated with state interventionism made it more difficult to bring together the resources and skills of people from different backgrounds. Many individuals and firms thus found it more expedient to use their resources to stay close to and seek favors from the government rather than invest in education, skills, and technology and pursue long-term gains in value added and productivity.

Outline

The following two chapters will extend this introduction. Chapter 2 will establish in greater detail Turkey's record in economic growth and human development since 1820, and chapter 3 will examine the role of institutions in economic development and the evolution of Ottoman institutions before the nineteenth century. In the rest of the book I will examine Turkey's experience with economic growth and human development since the Industrial Revolution in four historical periods. In each of these periods, governments in Turkey adopted the dominant economic model for the developing countries.

1. Growing specialization in agriculture under open economy conditions during the Ottoman nineteenth century
2. Transition from empire to the nation-state and an inward-looking economy during a difficult period that included two world wars and the Great Depression

3. Post–World War II decades when the import-substituting industrialization was led by the private sector
4. The recent period since 1980 when Washington Consensus principles were embraced and the economy opened up once again to international trade and investment

I will devote three chapters to the nineteenth century and two chapters to each of the following periods. For each period, I will examine the evolution of economic policies as well as the political developments and institutional changes. I will then establish and evaluate Turkey's record in economic growth and human development both in absolute and relative terms. I will also evaluate both the proximate and deeper causes of economic growth and human development.