Patterns of Adjustment under the Age of Finance: The Case of Turkey as a Peripheral Agent of Neoliberal Globalization*

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Turkey experienced a severe economic and political crisis in November 2000 and again in February 2001. The IMF has been involved with the macro management of the Turkish economy both prior and after the crisis, and provided financial assistance of $20.4 billions, net, between 1999 and 2003. Following the crisis, Turkey has implemented an orthodox strategy of raising interest rates and maintaining an overvalued exchange rate. The government was forced to follow a contractionary fiscal policy towards attaining a primary surplus to the 6.5% of the GNP, and promised to satisfy the customary IMF demands: reduce subsidies to agriculture, privatize, and reduce public sector in economic activity.

Contrary to the traditional stabilization packages that aim to increase interest rates to constrain domestic demand, the new orthodoxy aimed at maintaining high interest rates to attract speculative foreign capital. The end result in Turkey was shrinkage of the public sector; deteriorating education and health infrastructure; and failure to provide basic social services to the middle class and the poor.

Furthermore, as the domestic industry intensified its import dependence, it was forced to adapt increasingly capital-intensive, foreign technologies with adverse consequences on domestic employment. In the meantime the transnational companies and the international finance institutions have become the real governors of the country, with implicit veto power over any economic and or political decision that is likely to act against the interests of global capital.

Turkey experienced a severe economic and political crisis in November 2000 and again in February 2001. The crisis erupted when Turkey was following an *exchange-rate based disinflation programme* led and engineered by the IMF.[1] Over 2001 the GDP contracted by 7.4% in real terms, whole sale price inflation soared to 61.6%, and the currency lost 51% of its value against the major foreign monies. The burden of adjustment fell disproportionately on the

[1] The underlying elements of the disinflation program and the succeeding crisis are discussed in detail in Akyuz and Boratav (2004); Ertugrul and Yeldan (2003), Yeldan, (2002), Boratav and Yeldan (2006), Alper (2001). See also the GPN Report on Turkey, 2005 and the web site of the *Independent Social Scientists Alliance* (www.bagimsizsosyalbilimciler.org) for further documentation of the crisis conditions.

laboring classes as the rate of unemployment rose steadily by 2 percentage points in 2001 and then another 3 percentage points in 2002. Real wages fall abruptly by 20% upon impact in 2001 and could not recover since then as of the time of writing this report.

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The post-crisis economic and political adjustments were overseen by the newly founded *Justice and Development Party* (AKP) which came to power enjoying absolute majority in the parliament in the November 2002 elections. Though maintaining the pro-Islamic political agenda, the AKP nevertheless distanced itself from the previous "national View" orthodoxy of the traditional Turkish Islamic movement. The AKP refurbished itself with a more friendly view towards the West, ready to do business with the global finance capital and willing to auctioning off the strategic public assets to the trans-nationals. On the political arena, the AKP had given unequivocal support to the US interests in the Middle East including the then approaching war in Iraq.[2]

With a new *stand-by* on which the existing AKP government reached consensus with the IMF in 2004, the international financial institutions (IFIs) and the Turkish businesses were assured that the "reform" process would continue up to 2008 along the course set by the IMF's *structural adjustment* programme since 1998. The programme was officially declared as a bundle of policies aimed at checking increases in both domestic and external debt and channeling the country again to the path of "stable" growth. However, it is widely known that, beyond what has been declared officially, the programme envisages much more radical arrangements in restructuring the political and social life as a whole. It is also common knowledge that the primary and the most important target of these arrangements is to *eradicate* public services and related achievements in the fields of social security, education and health, and to *commodify* these services through privatizations. A critical point to be underlined here is that all of the governments of the recent period, including the AKP, have displayed their "*most determined*" political stand (and in turn were hailed as "*credible*" and "*reputable*") together with their full neglect to reactions coming from the people and the working classes. Taken from this angle, it will be safe to assert that Turkey constitutes one of the best examples of those societies where only formal aspects of political democracy are observed and nothing more (ISSA, 2006).

In fact, shortly after it has taken office, the AKP abandoned the discourse manipulating anti-IMF and anti-liberal reactions in the country immediately after taking office and showed no hesitation in fully adopting neo-liberal policies entrusting national resources and economic future of the country directly to foreign capital and the non-fettered workings of the market. The distinguishing feature of the AKP government in this respect was that it has undertaken the

[2] In fact, many analysts draw parallels with the declaration, in the summer months of 2002, of the three-party coalition government granting no support for the US plans to invade Iraq and the decision to hold early elections later in the same year.

mission of executing the neo-liberal project under the discourse of a "strong government" without confronting any strong popular opposition (ISSA, 2006; Cizre and Yeldan, 2005). The AKP had acted faster and more boldly than any preceding government in implementing the above neoliberal agenda in attempt to respond to the requests of international capital on the one hand, and to settle its problem of adaptation to the State and administrative traditions of the country, on the other.

It is the purpose of this paper to portray the post-2001 crisis adjustments and the warranted transformations in the Turkish political and economic arena under the auspices of the *Bretton Woods Institutions* (The IMF and the World Bank). The exclusive focus is on the macroeconomics of the AKP period, rather than the evolution of the 2001 crisis per se. The paper is organized under 4 sections. In the next section an overview of the Turkish macroeconomic adjustments is summarized with the relevant economic evidence. The section focuses on the *speculative* nature of growth with a detailed assessment of the modes of balance of payments financing under the AKP era. Section II in turn, takes on the *joblessness* growth patterns and document data on the labor markets. The deterioration of the position of wage labor along with its role in generating the necessary economic surplus under the post-crisis adjustments is documented in Section III. Section IV concludes with a discussion on the political inferences of the neoliberal reforms of the post-crisis era.

I. Post-Crisis Characteristics of Growth

The current IMF program in Turkey relies mainly on two pillars: (1) fiscal austerity that targets a 6.5 percent surplus for the public sector in its primary budget[3] as a ratio to the gross domestic product; and (2) a contractionary monetary policy (through an *independent* central bank) that exclusively aims at price stability (via inflation targeting). Thus, in a nutshell, the Turkish government is charged to maintain *dual* targets: a *primary surplus* target in fiscal balances (at 6.5% to the GDP); and an *inflation-targeting* central bank[4] whose sole mandate is to maintain price stability and is divorced from all other concerns of macroeconomic aggregates.

According to the logic of the program, successful achievement of the fiscal and monetary targets would enhance "credibility" of the Turkish government ensuring reduction in the country risk perception. This would enable reductions in the rate of interest that would then stimulate private consumption and fixed investments, paving the way to sustained growth. Thus, it is alleged that what is being implemented is actually an *expansionary* program of *fiscal contraction.*

The post-2001 growth had indeed been high. Annual rate of growth of real GNP averaged 7.8% over 2002-2006Q2. Growth, while rapid, had very unique characteristics. *Firstly*, it was mainly driven by a massive inflow of foreign finance capital which in turn was lured by significantly high rates of return offered domestically; hence, it was *speculative-led* in nature (*a la* Grabel, 1995). The main mechanism has been that the high rates of interest prevailing in the Turkish asset markets attracted short term finance capital, and in return, the relative abundance of foreign

[3] *i.,e.,* balance on non-interest expenditures and aggergate public revenues. The primary surplus target of the *central government budget* was set 5% to the GNP.
[4] The target was set at 5% on consumer price inflation for 2006, and 4% for 2007 and 2008.

exchange led to overvaluation of the *Lira*. Cheapened foreign exchange costs led to an import boom both in consumption and investment goods. Clearly, achievement of the fiscal contraction under severe entrenchment of public non-interest expenditures was a welcome event boosting the hungry expectations of the financial arbitrageurs. (See Table 1). The *second* characteristic of the post-2001 era was its *jobless-growth* pattern. Rapid rates of growth were accompanied by high rates of unemployment and low participation rates. The rate of unemployment rose to above 10% after the 2001 crisis, and despite rapid growth, has not come down to its pre-crisis levels (of 6.5% in 2000). Furthermore, together with persistent *open* unemployment, *disguised* unemployment has also risen. According to TURKSTAT data, "persons not looking for a job, but ready for employment if offered a job" has increased from 1,060 thousand workers in 2001, to 1,936 thousands by 2006, bringing the *total* (open + disguised) unemployment ratio to 15.5% (see Table 6 in section II below).

Together with rapid growth, dis-inflation has been hailed as another area of "success" for the AKP government. The Central Bank has started to follow an open inflation targeting framework since January 2006. The Bank's current mandate is to set a "point" target of 5 percent inflation of the consumer prices. Inflation rate, both in consumer and producer prices, has, in fact, been brought under control by 2004. Producer price inflation receded to less than 3% in late 2005. After the brief turbulence in the asset markets in May-July 2006, inflation again accelerated to above 10% and could only be brought under control gradually to 9.6% towards the end of 2006.

Despite the positive achievements on the dis-inflation front, rates of interest remained slow to adjust. The real rate of interest on the government debt instruments (GDIs) for instance remained above 10% over most of the post-crisis period and generated heavy pressures against the fiscal authority in meeting its debt obligations. (See figure 1). The persistence of the real interest rates, on the other hand, had also been conducive in attracting heavy flows of short term speculative finance capital over 2003 and 2005. This pattern continued into 2006 at an even stronger rate.

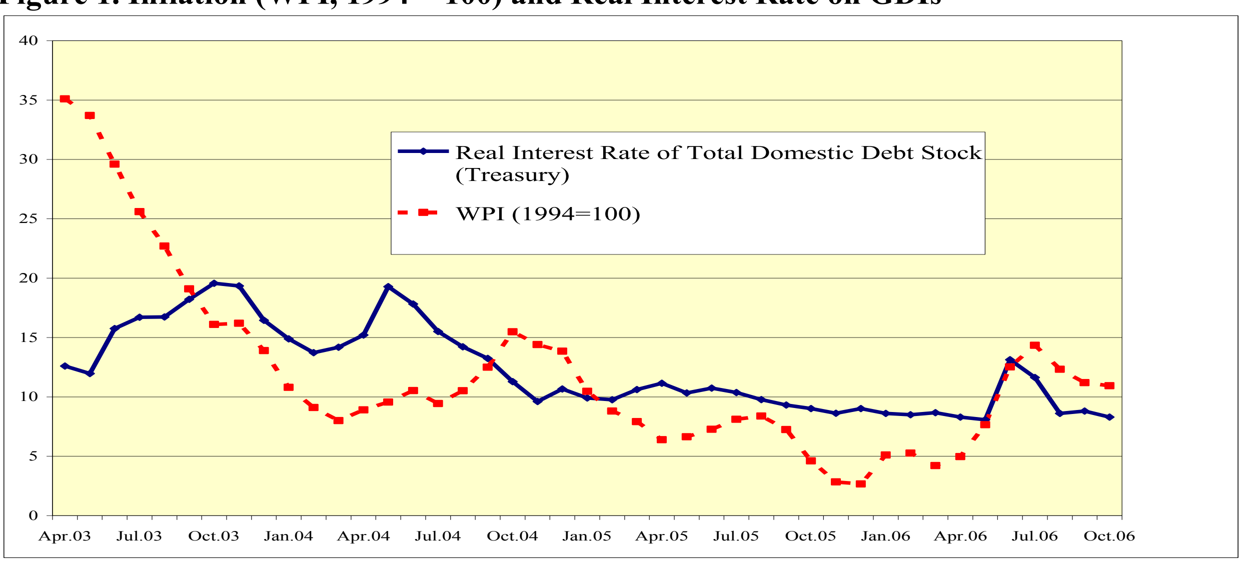
Table 1. Key Macroeconomic Indicators, Turkey							
			IMF-Led Post-Crisis Adjustments				
	IMF-Led Dis-inflation Programme	Crisis	Under 3-party Coalition Government	Under Pragmatic and Western-friendly Islamism of the AKP			
	2000	2001	2002	2003	2004	2005	2006.Q3
GNP Growth Rate	6.3	-9.5	7.9	5.9	9.9	7.6	7.8
Inflation (CPI, 12 months averages)	54.9	54.4	44.9	25.3	10.6	8.2	9.6[1]
Real Wage Growth (%)[2]	2.1	-20.1	1.1	5.1	3.9	-0.1	1.3
Unemployment Rate (%)	6.5	8.4	10.3	10.5	10.2	10.2	8.8
Budget balance / GNP (%)	-10.9	-16.2	-14.3	-11.2	-7.1	-2.0	-0.6[2]
Non-Interest Primary Budget Balance / GNP (%)	5.7	6.8	4.3	5.2	6.1	7.4	6.3
Central Adm. Domestic Debt (Billions $)	58.0	84.9	91.7	139.3	167.3	182.4	173.1
Central Adm. Domestic Debt / GNP (%)	29.0	69.2	54.5	54.5	52.3	50.3	45.7[2]
Total External Debt Stock (Billions $)	118.5	113.6	130.1	144.9	162.2	171.1	198.3
External Debt / GNP (%)	59.3	78.0	71.9	60.6	54.2	47.4	52.4[2]
Foreign Trade Balance (Billions $)	-23.8	-7.1	-11.4	-18.2	-30.6	-39.8	-32.0
Exports (fob, billions $)	30.7	34.3	40.1	51.1	66.9	76.7	63.9
Imports (cif, billions $)	54.5	41.4	51.5	69.3	97.5	116.5	95.9
Current Account Balance (Billions $)	-9.8	3.4	-1.5	-8.1	-15.6	-23.1	-25.3
Current Account Balance / GNP (%)	-4.9	2.3	-0.8	-2.8	-5.3	-6.4	-6.7[2]

Source: TR Central Bank (www.tcmb.gov.tr); Undersecretariat of Treasury (www.treasury.gov.tr)

1. As of end of 2006.
2. As a ratio of last four quarters.

Inertia of the real rate of interest is enigmatic from the successful macro economic performance achieved thus far on the fiscal front. Even though one traces a decline in the general plateau of the real interest rates, the Turkish interest charges are observed to remain significantly higher than those prevailing in most emerging market economies. The credit interest rate, in particular, has been stagnant at the rate 16% despite the deceleration of price inflation until the May-July turbulence. Since then the credit interest rates accelerated to 23.5% (Turkstat, 2006).

Figure 1. Inflation (WPI, 1994 = 100) and Real Interest Rate on GDIs

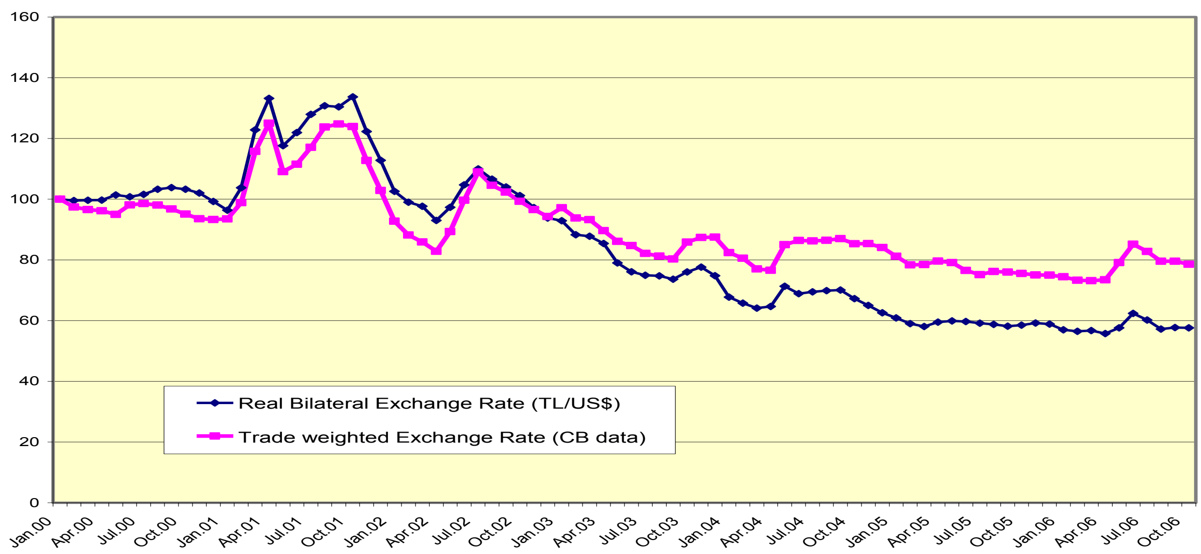


Source: TURKSTAT, www.die.gov.tr

High rates of interest were conducive in generating a high inflow of hot money finance to the Turkish financial markets. The most direct effect of the surge in foreign finance capital over this period was felt in the foreign exchange market. The over-abundance of foreign exchange supplied by the foreign financial arbitrageurs seeking positive yields led significant pressures for the Turkish Lira to appreciate. As the Turkish Central Bank has restricted its monetary policies only to the control of price inflation, and left the value of the domestic currency to the speculative decisions of the market forces, the *Lira* appreciated by as much as 40% in real terms against the US$ and by 25% against Euro (in producer price parity conditions).

Figure 2 portrays the paths of the *bilateral* (vis-à-vis the US$) and the *trade-weighted* real exchange rate (in PPP terms, with producer prices as the deflator) over 2000-2006. The currency crises of November 2000 through February 2001 are clearly visible in the figure. The recent blip in May-July 2006, on the other hand, has had a minimal effect on the *real* value of the real exchange rate and did not suffice to change the direction of the course of ongoing real appreciation.

Figure 2. Indexes of the Bilateral and Trade-Weighted Real Exchange Rate



Source: TR Central Bank and TURKSTAT.

I-1. Components of Balance of Payments and External Debt

The structural overvaluation of the TL, not surprisingly, manifests itself in ever-expanding deficits on the commodity trade and current account balances. As traditional Turkish exports lose their competitiveness, new export lines emerge. Yet, these proved to be mostly import-dependent, assembly-line industries, such as automotive parts and consumer durables. They use the advantage of cheap import materials, get assembled in Turkey at low value added and then are re-directed for export. Thus, being mostly import-dependent, they have a low capacity to generate value added and employment. As traditional exports dwindle, the newly emerging export industries had not been vigorous enough to close the trade gap.

Consequently, starting in 2003 Turkey has witnessed expanding current account deficits, with the figure in the third quarter of 2006 reaching a record-breaking magnitude of $25.3 billion, or 6.7% as a ratio to the aggregate GNP. In appreciation of this figure, it has to be noted that Turkey traditionally has never been a current account deficit-prone economy. Over the last two decades (80s and 90s) the average of the current account balance hovered around plus and minus 1.5-2.0%, with deficits exceeding 3% signaling for significant currency adjustments as had been in 1994 and 2001. In fact, the mechanics behind the culminating current account deficit of the post-2001 period can only be understood in the context of the speculative transactions embedded in the *Finance account* of the BOP. Table 2 summarizes the relevant data.

Table 2. Selected Indicators on Balance of Payments and Foreign Debt (Millions US$)

	2001	2002	2003	2004	2005	2006Q3	Total over 2006Q3-2003
Exports (fob)	34,373	40,124	51,206	67,047	76,595	63,916	258,764
Imports (fob)	-38,106	-47,407	-65,216	-90,925	-109,171	-95,922	-361,234
Trade Balance	-3,733	-7,283	-14,010	-23,878	-32,576	-32,006	-102,470
Current Account Balance	3,392	-1,524	-8,037	-15,604	-22,852	-25,334	**-71,827**
Finance Account Balance	-14,643	1,161	7,098	17,679	44,069	34,462	**103,308**
Foreign Direct Investment by Residents Abroad	-497	-175	-499	-859	-1,047	-361	-2,766
Foreign Direct Investment by Non-Residents	3,352	1,137	1,752	2,847	9,650	12,804	27,053
Non-Residents' Portfolio Investments in Turkey	-3,727	1,503	3,851	9,411	14,670	4,849	32,781
Residents' Portfolio Investments Abroad	-788	-2,096	-1,386	-1,388	-961	-1,284	-5,019
Other Investment, Net	-12,983	792	3,380	7,668	21,757	18,454	51,259
Net Errors and Emissions	-1,759	118	4,941	2,267	1,983	-659	**8,532**
Change in Reserves (-: Increase)	12,924	212	-4,097	-4,342	-23,200	-8,469	**-40,108**
Foreign Debt Stock	113,592	130,093	144,915	162,202	171,078	198,261	68,168
Short Term Foreign Debt Stock	16,403	16,424	23,013	32,569	38,247	43,322	26,898
Ratio of Short Term Foreign Debt Stock to Central Bank Reserves	0.87	0.61	0.68	0.90	0.76	0.74	..

Source: TR Central Bank (www.tcmb.gov.tr)

Data in Table 2 indicate that the finance account has depicted a net surplus of 103.3 billion over the "AKP period", 2003 through 2006 (September). About half of this sum ($151.2 billion) was due to credit financing of the banking sector and the non-bank enterprises, while a third ($32.8 billion) originated from *non-residents' portfolio investments* in Turkey. *Residents* have exported financial capital at the magnitude of $5.4 billion, and if one interprets the *net errors and omissions* term of the BOP accounts as an indicator of *domestic hot money flows* (see e.g. 6and Akyuz, 2004; Boratav and Yeldan, 2005), the total sum of *net speculative finance capital inflows* is calculated to reach $36.2 billion over the three years of the post-crisis adjustments.

The *foreign direct investment* (FDI) is taken as an important source of financing the current account deficit especially after 2005. It is true that the BOP data reveal a sudden increase in the flow of FDI monies totaling $22.4 billion in the last two years. However, looking at the FDI more closely, it would be revealed that the bulk of the aforementioned flow had been due to privatization receipts plus real estate and land purchases by foreigners. Neither of these items are sustainable sources of foreign exchange, and they were driven by speculative arbitrage opportunities rather than enhancing the real physical capital stock of the domestic economy. In fact as reported by the ANKA researchers, the *stock* of "hot money" has reached to $52.3 billion as of August 2006. This stock is fed upon three sources: (i) foreigners' holdings of government debt instruments (£17.9 billion) and (ii) of securities at the Istanbul Stock Exchange Market ($30.6 billion); and (iii) foreign exchange deposits at the banking sector ($3.7 billion). The aggregate stock of hot money reaches to two-thirds of the cumulative current account deficit over the post-2001 crisis period.

A significant detrimental nature of hot money led balance of payments financing is its foreign debt intensity. As reported in Table 2, the stock of external debt has increased by a total of $63.5 billion over the end of 2002 to the second quarter of 2006 (the most recent data available at the time of writing). This indicates a cumulative increase at a rate of 48.8% in US dollar terms over a period of 3.5 years. Despite this rapid increase, the *burden* of external debt as a ratio to the GNP has fallen from 71.9% (2002) to 47.4% (2005). This fall is due to both the rapid expansion of the GNP and the unprecedented appreciation of the Lira over the period. The appreciation of TL disguises much of the fragility associated with both the level and the external debt induced financing of the current account deficits. A simple purchasing power parity "correction" of the real exchange rate, for instance, would increase the burden of external debt to 76.8% as a ratio to the GNP in 2005.[5] This would bring the debt burden ratio to the 2001 pre-crisis level. Under conditions of the floating foreign exchange regime, this observation reveals a persistent fragility for the Turkish external markets, as a possible depreciation of the Lira in the days to come may severely worsen the current account financing possibilities. This persistent external fragility is actually one of the main reasons why Turkey had been hit the hardest among the emerging market economies in the May-June 2006 turbulence (IMF, 2006).

Another facet of the external fragility of the Turkish balance of payments regards the *composition* of debt. As far as the post-2001 era is concerned, two critical features of external debt driven current account financing have been that, (i) the foreign debt accumulation was

[5] Measured in 2002 producer prices. If the PPP-correction is calculated in 2000 prices, the revised debt to GNP ratio reaches to 82.3%.

mostly of short term duration; and (ii) it was mostly driven by the *non-financial private sector*, rather than the public sector. I document the relevant data in Table 3.

Table 3. Composition of External Debt Stock (Millions US$)

	2000Q4	2001Q4	2002Q4	2003Q4	2004Q4	2005Q4	2006Q3	2006Q3 - 2002Q4 Increase
External Debt Stock (1 + 2)	118,504	113,592	130,093	144,915	162,202	171,078	198,261	68,168
(1) Short Term Foreign Debt	28,301	16,403	16,424	23,013	32,569	38,247	43,322	26,898
Banks	16,900	7,997	6,344	9,692	14,529	17,740	19,828	13,484
Other Sectors	9,748	7,654	8,425	10,461	14,753	17,744	20,897	12,472
TR Central Bank	653	752	1,655	2,860	3,287	2,763	2,774	1,119
(2) Medium-Long Term Debt	90,203	97,189	113,669	121,902	129,633	132,831	154,939	41,270
(2.1) Public Sector	47,621	46,110	63,618	69,503	73,825	68,114	68,660	5,042
(2.2) TR Central Bank	13,429	23,591	20,340	21,504	18,114	12,654	12,921	-7,419
(2.3) Private Sector	29,153	27,488	29,711	30,895	37,694	52,063	73,358	43,647
(2.3.1) Financial Enterprises	7,581	4,789	4,637	5,060	8,284	15,316	21,264	16,627
Banks	4,550	3,211	3,026	3,140	5,750	12,231	17,310	14,284
Non-Bank Financial	3,032	1,578	1,611	1,920	2,534	3,085	3,954	2,343
(2.3.2) Non-Financial Enterprises	21,571	22,699	25,074	25,835	29,410	36,747	52,094	27,020

Source: Undersecreteriat of Treasury (www.hazine.gov.tr)

As Table 3 attests, of the accumulated foreign debt of $68.2 billion over the AKP era, 43% was short term in maturity. Turkey's external short term debt stock, which had reached to $28.3 billion just before the eruption of the February 2001 crisis, was reduced to as low as $13.7 billion in the first quarter of 2002. The stock of short term debt has increased rapidly, especially after 2003, to reach $43.3 billion as of the third quarter of 2006. A critical account of this episode pertain the ratio of short term debt to central bank's international reserves. This ratio is regarded as one of the crucial leading indicators of external fragility (see, *e.g.*, Kaminsky *et.al.*, 1999), and has been interpreted as the "most robust predictor of a currency crisis" in Rodrik and Velasco (1999). The path of this indicator over the post-2001 period is summarized in the last row of Table 3.

As the ratio of short term external debt to CB international reserves rise, it signals a "fall" in the capability of the CB to meet the external liabilities of the domestic economy, and is interpreted as *worsening* of external fragility. This ratio stood at 0.87 by the end of 2001[6], and after receding to 0.61 in early 2002, rose up to 0.92 by the third quarter of 2005. It is brought back to 0.74 by the third quarter of 2006, thanks mainly to very rapid build-up of foreign exchange reserves by the Turkish Central bank in the past year. By way of comparison, the aforementioned "fragility ratio" was 0.60 in Malaysia, 0.91 in the Philippines, and 1.50 in Thailand just before the break down of the 1997 Asian crisis. Thus, it can be argued that 0.60 is

[6] The ratio of short term foreign debt to CB international reserves was 1.47 just before the eruption of the February 2001 crisis.

regarded as a critical threshold from an international speculation point of view (see, *e.g.*, Kaminsky *et.al*, 1999).[7]

The preceding discussion indicates that despite the brief deceleration of the turbulence of May-June, Turkish economy continued to increase its intensity of external debt accumulation in 2006. Available data of the first nine months of 2006 is a manifest of this as summarized in Table 4 below.

Table 4. Main Components of the Balance of Payments in 2006 (Millions US$)

	Jan - Sept 2005	Jan - Sept 2006	Difference
Current Account Balance	-15,870	-25,334	-9,464
Capital Originating from Foreign Sources	25,821	38,108	12,287
Capital Originating from Domestic Sources	-4,052	-7,188	-3,136
Change in Reserves ("-" indicates increase)	-8,561	-4,927	n.a.
Net Errors and Omissions	2,662	-659	-3,321
Net Capital Inflow	24,431	30,261	5,830
Foreign Debt Inducing Capital Inflows	17,291	23,705	6,414
Net Hot Money Flows	11,959	-1,869	-13,828
Sources: Boratav, 2006; TR Central Bank.			

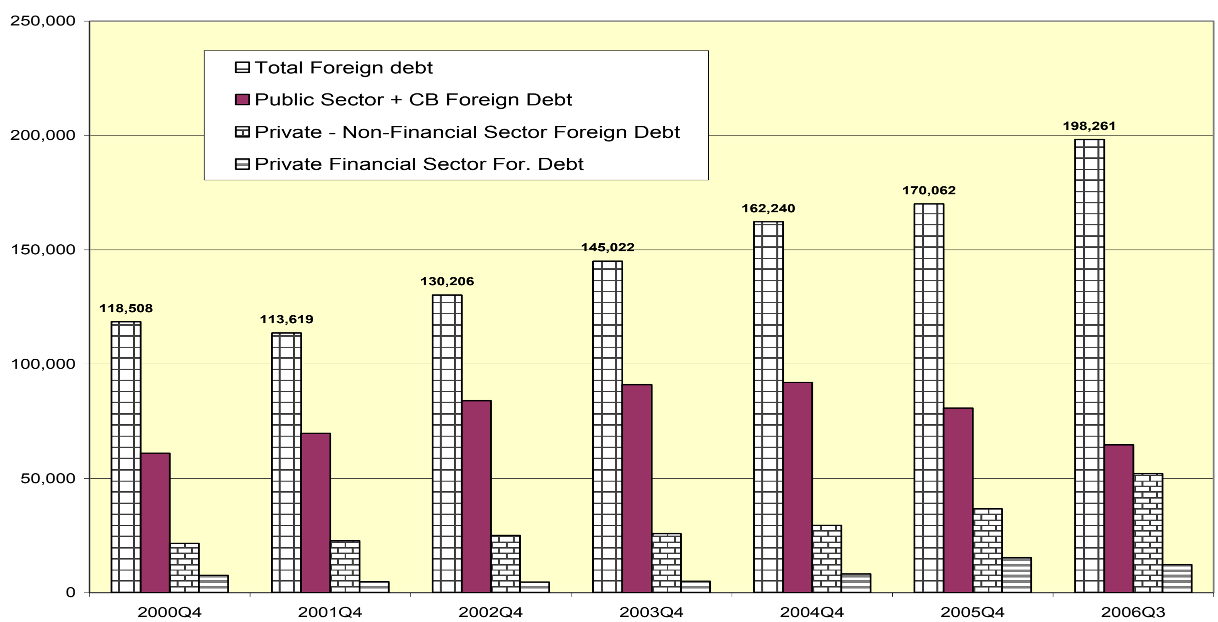
In table 4 we distinguish the BOP data of January-September 2006 over two axes: first is the decomposition of the in/out-flows of foreign capital into two sources: by the foreign non-residents *versus* domestic residents. Capital inflows originating from the *foreign* sources are observed to increase by 48% over the comparable period of 2005, and reached to $38.1 billion. The *domestic* source, on the other hand, displayed an *out*-flowing tendency and had been on the order of $-7.2 billion. This figure comprises outflows due to operations of the banking sector and the enterprises, as well as the domestic rentiers' decisions. Taking account of the net errors and omissions figure of $-0.7 billion, the overall *net foreign capital inflow* into Turkey reached to $30.3 billion, a 24% increase over the same period of 2005.

[7] See also Goldstein (2005) for a recent evaluation of the external fragility accross emerging market economies, where Turkey is reprotedly found to display above average fragility indexes among comparable economies. See also the IMF's 2006 report on Turkey for further discussion.

Data reveal that a significant deceleration of the *hot money* component of this transfer ($-1.9 billion), as the domestic outflows of hot money had outpaced the speculative inflows of non-residents. Consequently, the role of hot money financing of the balance of payments is reduced in the first nine months of 2006. The period further reveals, however, a 37.7% increase in net foreign indebtedness, to reach $23.7 billion. Given that the public sector is currently following a strict austerity programme, and has generated a sizable primary surplus, this increase in foreign debt has originated mainly from the private sector —and mainly by the non-banking, private enterprise sector (see Table 3). The external debt obligations of the private sector ($73.4 billion) now exceeds aggregate public foreign debt ($68.6 billion) as of third quarter of 2006.

Within the private sector, non-financial enterprises explain 60% of the aggregate increase of private external debt over the post-2002 AKP period and accounts for 70.9% of the total stock of private debt by 2006Q3. (See Figure 3).

Figure 3. External Debt By Sectors



Source: TR Central Bank, **www.tcmb.gov.tr**

I-2. The "IMF Program"

The rapid increase of private sector debt —both by the financial and non-financial sectors alike, reveals the true essence of the IMF-engineered adjustment mechanisms following the currency and banking crises of February 2001. The underlying characteristics of the Turkish post-crisis adjustments ultimately relied on maintaining high real rates of interest in anticipation of increased foreign capital inflow into the domestic economy. Coupled with an overall contractionary fiscal policy, the programme found the main source of expansion in speculative inflows of foreign finance. Persistent offerings of high rates of interest against the back-drop of lower inflation and fiscal primary surplus targets were the main attributes of the IMF programme as implemented both by the three-party coalition government under Mr. Bulent Ecevit (until November, 2002) and by the AKP government (post-November, 2002).

The aforementioned elements of this adjustment path were clearly stated, in fact, in the Turkey Country Report prepared by the IMF staff in late 2001. Table 5 below makes a reference to that 2001 report which had laid out the macroeconomic targets of the post-crisis adjustment path as envisaged by the IMF. It is very illuminating to note that the targets of the 2001 IMF Report encompassing 2002 through 2006 have eventually become the official targets of both governments over that period. The targeted rate of real GNP growth, for instance, was persistently set at 5% for each coming year, despite the observed rapid expansion of the economy in rates often exceeding 7% in the preceding year! This choice was clearly no coincidence. Likewise, the inflation targets of the "independent" central bank each year followed the path envisaged in the 2001 IMF Report, beginning with 20% of 2003 to 5% in 2006. (Note that the Turkish CB has declared the onset of its official inflation targeting monetary regime in January 1, 2006).

Finally, the very sanctimonious primary surplus target of the public sector at 6.5% as a ratio to the GNP clearly finds its origins in the aforementioned report.

Table 5. Macroeconomic Targets of the Current IMF Programme

	2002	2003	2004	2005	2006
GNP Real Growth Rate	3.0	5.0	5.0	5.0	5.0
Non-Interest Budget balance / GNP (%)	6.5	6.5	6.5	6.5	6.3
Inflation Rate	35.0	20.0	12.0	8.0	5.0
Nominal Rate of Interest on Domestic Debt	69.6	46.0	32.4	27.4	23.9
REAL Rate of Interest on Domestic Debt	25.6	21.7	18.2	18.0	18.0

Source: IMF, 2001 Turkey Country Report (*www.imf.org*)

That being said, what remains noteworthy is the IMF's choice of a very high and persistent *real* interest rate targeted at 18% throughout the programming horizon. The real interest rate target is persistently kept at its very high level despite the falling trajectory of the inflation rate. In comparison of the Figure 1 above where the realized rates of inflation and real interest were disclosed, the persistence of the high level of real interest rate against falling inflation rates seem to find a resonance in the adjustment path assumed by the IMF staff in the immediate post-2001 crisis. It is clear that the main adjustment mechanism of the post-crisis IMF programme was embedded in maintaining a significantly high rate of real interest. The high interest rates attracted short term finance capital; and the relative abundance of foreign exchange led to overvaluation of the *Lira*. Cheapened foreign exchange costs led to an import boom both in consumption and investment goods. Achievement of the fiscal contraction under severe entrenchment of public non-interest expenditures, in turn, was a welcome event further boosting the hungry expectations of the financial arbiters.

In sum, contrary to the traditional stabilization packages that aimed at increasing interest rates *to constrain the domestic demand*, the new orthodoxy aimed at maintaining high interest rates for the purpose of *attracting speculative foreign capital* from the international financial markets. The end results in the Turkish context were the shrinkage of the public sector in a *speculative-led growth* environment; deteriorating education and health infrastructure which necessitate increased public funds urgently; and the consequent failure to provide basic social services to the middle classes and the poor. Furthermore, as the domestic industry intensified its import dependence, it was forced toward adaptation of increasingly capital-intensive, foreign technologies with adverse consequences on domestic employment. It is to this issue now I turn.

II. Persistent Unemployment and Jobless Growth

Another key characteristic of the post-2001 Turkish growth path has been its "jobless" nature. The rate of open unemployment was 6.5% in 2000; increased to 10.3% in 2002, and remained at that plateau despite the rapid surges in GDP and exports. Open unemployment is a severe problem, in particular, among the young urban labor force reaching 26%. Table 6 tabulates pertinent data on the Turkish labor market.

Table 6. Developments in the Turkish Labor Market (1,000 persons)

	2000	2001	2002	2003	2004	2005	2006Q3
15+ Age Population	46,209	47,158	48,041	48,912	49,906	50,991	51,770
Civilian Labor Force	23,078	23,491	23,818	23,640	24,289	24,989	25,622
Civilian Employment	21,581	21,524	21,354	21,147	21,791	22,566	23,279
Unemployed (Open)	1,497	1,958	2,473	2,497	2,479	2,509	2,343
Open Unemployment Ratio (%)	6.5	8.4	10.4	10.5	10.3	10.2	9.1
Disguised Unemployment[a]	1,139	1,060	1,020	945	1,223	1,714	1,936
Total Unemployment Ratio[b] (%)	10.9	12.3	14.1	14.0	14.5	15.8	15.5
Civilian Employment by Sectors							
Agriculture	7,103	8,089	7,458	7,385	7,400	6,661	6,809
Industry	3,738	3,774	3,954	3,821	3,988	4,360	4,429
Services	9,738	9,661	9,942	10,080	10,403	11,545	12,041

Source: Turkish Statistical Institute (TURKSTAT), Household Labor Force Surveys.

a. Persons not looking for a job yet ready to work if offered a job: (i) Seeking employment and ready to work within 15 days, and yet did not use any of the job search channels in the last 3 months; plus (ii) discouraged workers.

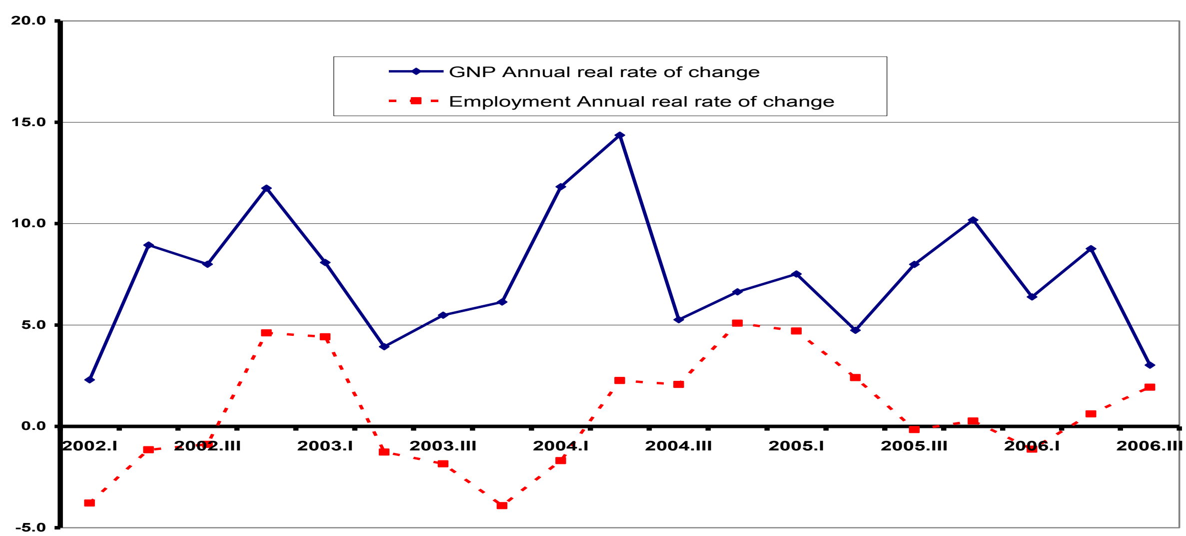
b. Total (open + disguised) unemployment accounting for the persons "not in labor force".

The civilian labor force (ages 15+) is observed to reach 51.8 millions people as of 2006Q3. On the other hand, the participation rate fluctuates around 48% to 50%, due mostly to the seasonal effects. It is known, in general that, the participation rate is less than the EU averages. This low rate is principally due to women choosing to remain outside the labor force, a common feature of Islamic societies, but its recent debacle depends as much on the size of the discouraged workers who had lost their hopes for finding jobs. If we add the TURKSTAT data on the *underemployed* people, the excess labor supply (unemployed + underemployed) is observed to reach 15.5% of the labor force as of the third quarter of 2006.

Yet the most striking observation on the Turkish labor markets over the post-2001 crisis era is the sluggishly slow performance of employment generation capacity of the economy. Despite the very rapid growth performance across industry and services, employment growth has been meager. This observation, which actually is attributed to many developing economies as well,[8] is characterized by the phrase *jobless-growth* in the literature. In Turkey this problem manifests itself in insufficient employment generation despite the very rapid growth conjuncture especially after 2002.

To make this assessment clearer I plot the quarterly growth rates in real gross domestic product in Figure 4, and contrast the *y-o-y* annualized rates of change in labor employment. In order to make comparisons meaningful, the changes in labor employment is calculated relative to the same quarter of the previous year.

Figure 4. Annual Rate of Change in GDP and Aggregate Employment



Source: Turkish Statistical Institute (TURKSTAT), Household Labor Force Surveys.

[8] See, e.g., UNCTAD, *Trade and Development Report*, (2002 and 2003).

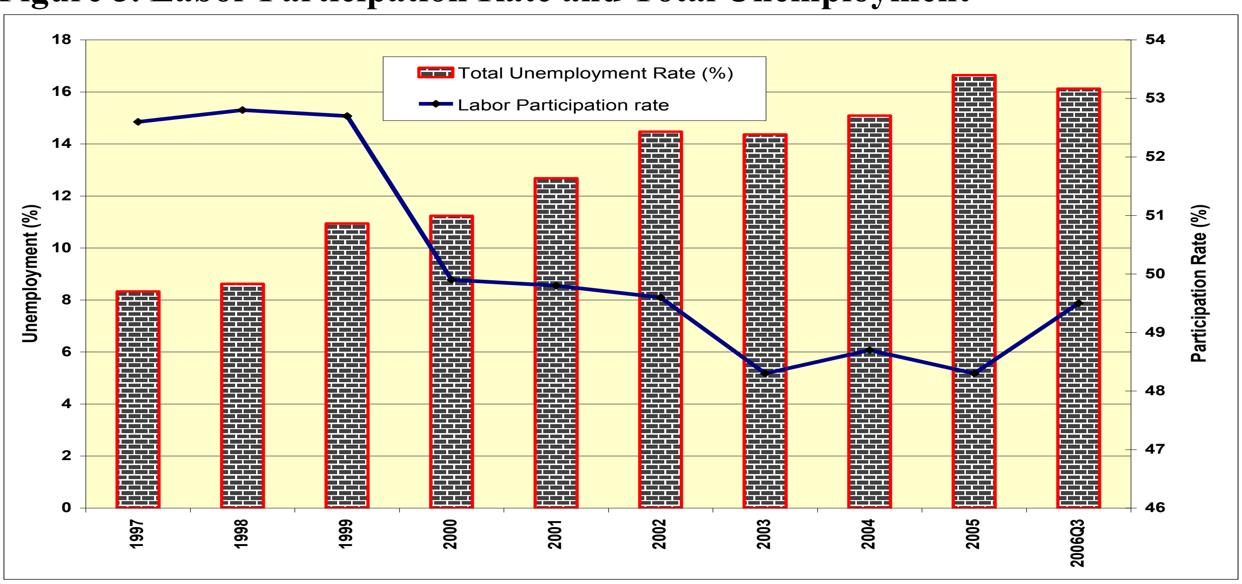
The figure discloses that between 2002.Q1 and 2006.Q3 the average rate of growth in real GDP was 7.5%. In contrast the rate of change of employment averaged *only 0.8%* over the same period. Over the nineteen quarters portrayed in the figure, GDP growth was positive in all periods. Yet, labor employment growth was *negative* in 9 of those 19 quarters.

The sectoral breakdown of the post-crisis employment patterns reveals a massive de-population in the rural economy. Agricultural employment has been reduced by 1,289 thousand workers since 2001. Against this fall, there had been a total increase of employment in the services sectors by 2,380 thousand, and by 655 thousand in industry. Simultaneous to this was the overall expansion of the aggregate labor supply from 47.158 million in 2001 to 51.770 million in 2006, adding to the acuteness of the joblessness problem.

Thus, in conclusion, two important characteristics of the post-crisis adjustment path stand out: first is that the post-2001 expansion is observed to be concomitant with a deteriorating external disequilibrium, which in turn is the end result of excessive inflows of speculative finance capital, and was named *"speculative-led"* in the preceding section. Secondly, the output growth contrasts with persistent unemployment, warranting the term "*jobless growth*".

A further detrimental impact of the speculative-led, jobless growth era had been the overall decline in the labor participation rates. Even though lower than the comparable member countries of the European Union, labor participation rates were nevertheless above 50% during most of the 1990s. The participation rate declined to less than the 50% threshold first during the implementation of the 2000 exchange rate-based dis-inflation programme. It continued its secular decline over the rest of the decade and its trend is depicted in Figure 5.

Figure 5. Labor Participation Rate and Total Unemployment

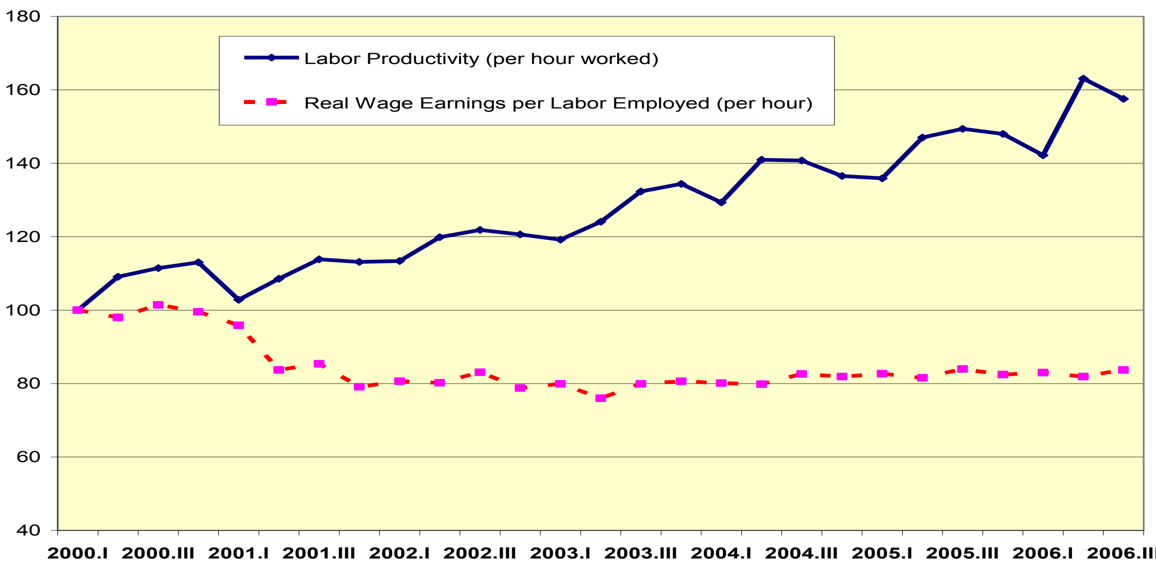


Source: Turkish Statistical Institute (TURKSTAT), Household Labor Force Surveys.

III. Wage-Labor as the Absorber of the Burden of Adjustments

Such a transfer of the financial surplus through very high real interest rates offered to the financial system would, no doubt, call for repercussions on the primary categories of income distribution. It is clear that creation of such a financial surplus would directly necessitate a squeeze of the wage fund and a transfer of the surplus away from wage-labor towards capital incomes, in general. It is possible to find evidence to the extend of this surplus transfer from the path of the manufacturing real wages. I portray the dynamics of the manufacturing real wages in Figure 6, and offer contrasts against productivity of labor.

Figure 6. Real Wages and Labor Productivity in Turkish Manufacturing Industry



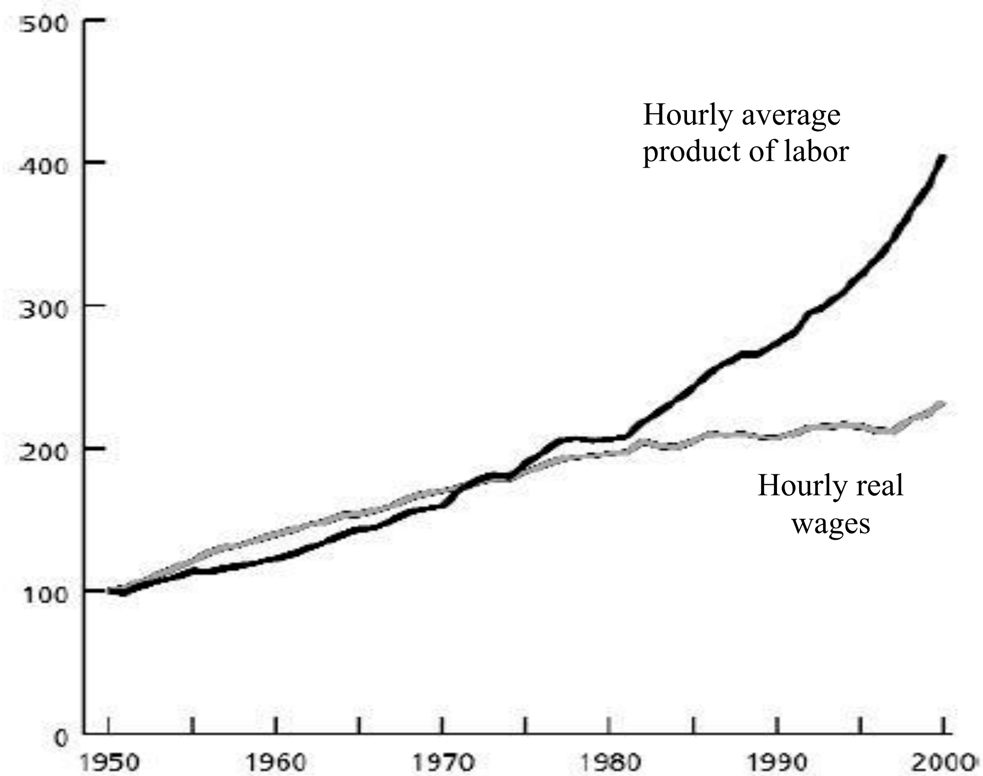
Source: Turkish Statistical Institute (TURKSTAT)

The index of labor productivity, measured in real output per hours, shows a rapid increase with its level reaching to 158 index points (1997=100) by 2006Q3. Over the same period, wage remunerations, on the other, *declined* by a cumulative 23.8% in real terms. This exercise shows very clearly, how in the Turkish economy speculative financial gains were financed through squeezing of real wages. Each rapid rise in the financial returns has been closely associated with a downward movement of real wages and involved a direct transfer from labor incomes towards capital, both domestic and foreign[9]. The real wages contracted severely after the 2001 February crisis and this downward trend was maintained throughout 2002 and 2003.

[9] See also Yeldan (2006) for a more detailed assessment of the labor's position under the post-crisis adjustments of the Turkish economy.

A case can further be made here that the ongoing process of surplus transfer from wage-labor to the financial-industrial conglomerates is nothing new, and not unique to Turkey, either. Capital's assault on labor has, in fact, continued with new forms of industrial organization at the onset of neo-liberal globalization in mid-70s. With intensified policy changes towards flexibility and privatization, position of wage-labor eroded everywhere. This process was most visible in the US, the hegemonic center of global capitalism. In order to depict this phenomenon, I will adhere to the path of real wages and real labor productivity in US manufacturing in the second half of the 20th century. (See Figure 7). As clearly visible, the *Fordist* period under the Keynesian policies had been associated with real wages following to a large extend the movements in labor productivity up until 1970s. The late 1970s, however, reveal the extend of capital's gains against labor. As the real wage rate stagnated, its path remained significantly below the real average product of labor, the gap yielding the increased exploitation of wage labor in the last quarter of the century.[10]

FIGURE 7. Labor Productivity and Hourly Real wages in US Manufacturing (1950 = 100)

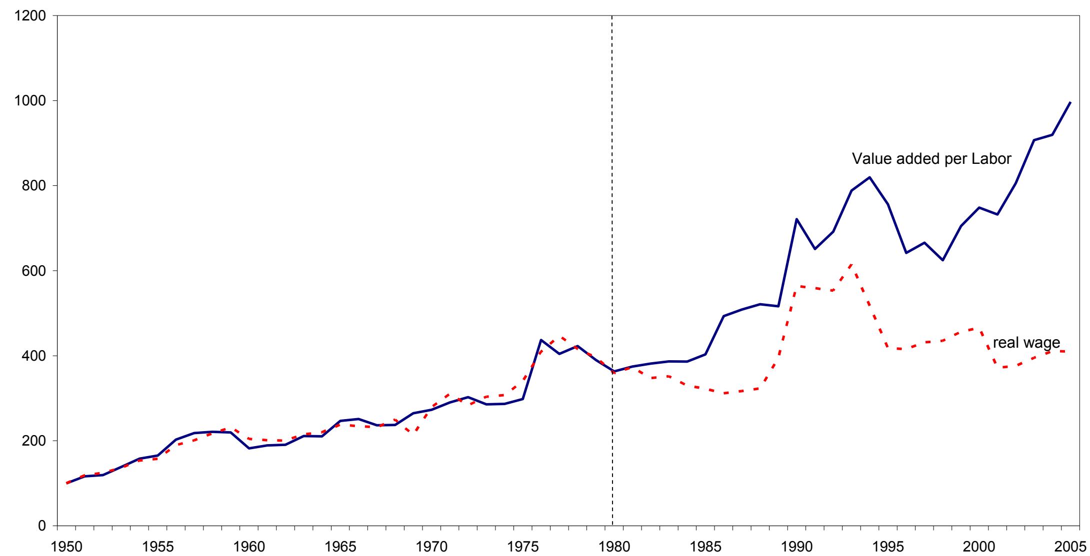


Source: "The New Face of Capitalism: Slow Growth, Excess Capital and A Mountain of Debt" *Monthly Review*, editors, 2002. (*www.monthlyreview.org/0402.editr.htm*)

[10] See, e.g., Moseley (2001) and the series of reports by the *Economic Policy Insititue* on the position of the US labor.

A different facet of this observation was at play across the Atlantic as well. Figure 8 below contrasts the US wage labor's position with that of Turkey. The figure portrays comparable data and the verdict remains exactly the same. Wage rates of the Turkish manufacturing labor follow the average real product until 1980, and under conditions of military dictatorship during the 1980s, a significant wedge is created among the real wage earnings and real labor productivity by way of intensified exploitation of labor.

Figure 8. Labor Productivity and Real Wages in Turkish Manufacturing (1950-2005)



Source: TURKSTAT, Annual Manufacturing Surveys.

Clearly very similar processes had been operational both at the North and South under neoliberal globalization. The end of the Fordist technological organizations led to the demise of the welfare state which enabled a comparatively tolerant attitude towards wage labor. As this delicate balance on mass production for domestic consumption eroded, capital has found a new opportunity in financial returns. Overall this process has led to the demise of the welfare state and an outright hostile attitude against the rights of labor.

As a result, share of labor in national incomes fell everywhere. According to Petras and Veltmeyer (2000) and Diwan's (1999) data, share of wage labor fell from 48% (1970) to 28% (1985) in Chile; from 41% (1970) to 25% (1989) in Argentina; from 37% (1970) to 27% (1989) in Mexico; from 40% (1970) to 17% (1986) in Peru. Similarly, according to calculations of Yeldan (2000, Chapter III) the share of wage labor in manufacturing value added was reduced from 28% in 1976 to 15% by 1987.

This abrupt shift in the distribution of income against labor coincided with the assault against indigenous strategies for economic development and against the fragile democracies of the "South".

IV. Conclusion: From "Fiscal" to "Democracy" Deficit

The detrimental consequences of the neoliberal adjustment path on wage-labor were not limited only to the economic sphere. Labor's position was further curtailed as the developing country governments that are dependent upon foreign capital have been conditioned to adopt or maintain contractionary policies in order to secure "investor confidence" and "international creditworthiness". Such efforts are restricted to a balanced budget, entrenched fiscal expenditures, and a relatively contractionary monetary policy with an ex ante commitment to high real interest rates. All of this signify reduced political autonomy in the developing world in exchange for market access to industrialized North, and itself is a bad bargain as far as development is concerned (Rodrik, 2001).

In this environment portfolio investors become the ultimate arbiters of national macroeconomic policy (Cizre-Sakallioglu and Yeldan, 2000; Grabel, 1996) and any effective public policy is now regarded as synonymous to populism and waste. Democratic institutions are put under siege through endless lists of conditionalities set forth by the IMF and the World Bank, and in the meantime, the transnational companies and the international finance institutions (IFIs) have become the real governors with an implicit veto power over any economic and/or political decision that is likely to act against the interests of global capital. The IFIs report rating scores in aligning the indigenous economies under the strategic realm of finance capital. Even direct political decisions are under scrutiny.

A critical example here is the rejected war motion by the Turkish parliament, disapproving the US troops to utilize the Turkish soil in the early days of the Iraq's invasion. In exchange for a total aid of 24 billion dollars, USA had asked permission from Turkey to use its borders with Iraq. The motion was rejected and a chaos ensued driven by the IFIs and their rating agencies. The following excerpt from *Morgan Stanley Economic Forum on Turkey*, is a typical example: (March 4, 2003).

> "*the latest parliamentary decision to reject the much-debated 'war motion' is such a risk that will no doubt disturb the fragile equilibrium...(Turkey) is unlikely to get the promised $24 billion that would ease pressure on the domestic debt market...*"

The report concludes with the stunning question:

> *"what happens if the parliament does not altogether vote for the economic reforms, arguing that 80% of the Turkish population is against the IMF program?"*

Thus, the report is not only concerned with the loss of 24 billion dollars liquidity for the Turkish financial centers, but is also worried that the people may further exercise their rights over the future of the IMF-led austerity program in Turkey. In the classic words of Diaz-Alejandro (1985), a twist can also be mentioned: *"Good-bye Budget deficits, hello democracy deficit..."*.

In the words of the 2005 Annual Report of the ISSA, two important consequences of these transformations come to the fore as the basic problem of almost all countries including Turkey: Speaking in broad terms, these are related to the *transfer of decisions relating to the public sphere from constitutional institutions of respective countries to "independent" supreme bodies of regulation working under global rules* and further *commercialisation* of the public services and the overall body of public economic activity including decision making and regulation (ISSA, 2006: 4). This process, whose legitimization is presented as "*dissecting politics from economics*" enhances the hegemony of global capital and its domestic extensions on society by keeping large sections of people and working masses afar from political processes. Political leaders in all countries where these reforms are being implemented commonly refer to *clumsily working* "old" state and bureaucratic structures, also lamed by *corruption*; and the new model is championed by reference to its so–called efficient, strong, rule-abiding and accountable features. Any reader with further interest in a more elaborate and advanced analysis of these reforms and the *new State* in agenda as well as the *new public sphere* may refer to any website managed by IMF, WB, OECD or EU.

Reports containing mentioned policy suggestions not only define necessary measures and arrangements to be adopted, but also go as far as advising ways of securing public support in this field. The example below is from an OECD Report (2002) titled *Regulatory Reforms in Turkey: Important Support to Economic Improvement: Governance:*

> "*...It is vital to have open communication channels in order to have continued public support for the reforms. There is a need for dissemination of the targets and the advantages of the regulatory reforms. Another benefit of this approach is to eliminate the widespread public view that the reforms are imposed from abroad. For this reason, the public perception should be treated as an important issue within the communication strategy of the government.*" (page 11, underlined emphasis added).

Assessing the processes which the so-called "emerging market economies" have undergone under the onset of neoliberal globalization, it becomes clearer that what has been pursued is not simply a stride to "stabilize" the economic structures, but goes much beyond it to radically alter the social structures of those nations. The executing actors include political circles who shut their ears to reactions coming from different segments of society, justify their stance by repeating "*it is us who decide on policies to be adopted*" and maintain these policies at any cost whatsoever while keeping themselves content with the slogan "*firm commitment is a virtue"*. These top level bureaucrats, whom we can classify as "global elites", often share the same mode of living and discourse worldwide. Extremely intolerant to any criticism including very innocent ones, these groups may well behave far distant from what can be given as the *sine qua non* of any democracy.

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