



Hacettepe University Graduate School of Social Sciences

Department of Economics

Master of Economics

**“A COMPARATIVE ANALYSIS OF IMPORT SUBSTITUTION
INDUSTRIALIZATION IN EGYPT AND TURKEY ”**

Deena Saleh Hashad

Master Thesis

Ankara, 2016

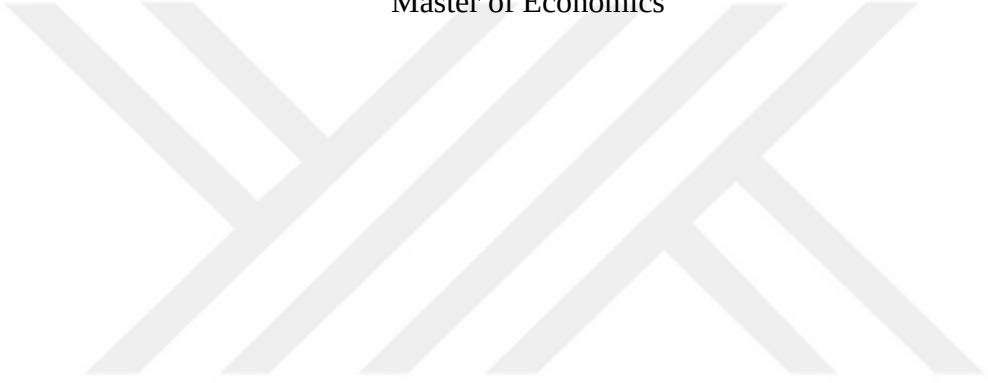
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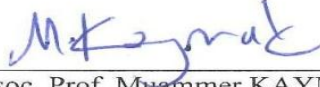
ACCEPTANCE AND APPROVAL

ACCEPTANCE AND APPROVAL

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ABSTRACT

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This thesis tried to shed light on ISI in Egypt and Turkey. Both have been regarded promising economies by International Financial Institutions (IFIs). Nevertheless, similar signs of political instability, social changes, and economic hardships have taken place in both. In this regard, we believe those signs are better understood by having a retrospective view into their economic and political history. Both had similarities in economic and political challenges since the first decade of the 21st century. This defines a similar development path based on adopted import-substitution industrialization (ISI), then by liberal economic policy and structural adjustment programs (SAPs). A central theme of this literature is the success of ISI in terms of increased industrial output. However, Turkey was better on economic and political scales more than Egypt, which was drowning in many wars, after it got over British Colony. We attempt to analyze political and economic institutions, and their role in political economy of each country. Political, international, economic, and institutional context, however, differed in many aspects. This explains the divergence in Turkey's economic performance. It is argued that some factors such as institutional framework, political and economic ideology, social coalitions, and international financial institutions affected implementation and success of ISI in each country, differently.

Key Words

Import Substitution Industrialization, Less Developed Countries, Egypt, Turkey, Middle East, Etatism, Infitah, Export Led Growth.

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List of Acronyms

ASU	Arab Socialist Union
CHP	Republican Peoples Party (RPP)
DCs	Developed Countries
DP	Democrat Party
ELG	Export-Led Growth
EGP	Egyptian Pound
GNI	Gross National Income
ISI	Import-Substitution Industrialization
IFIs	International Financial Institutions
IMF	International Monetary Fund
LDCs	Less Developed Countries
MENA	Middle East and North Africa
NATO	North Atlantic Treaty Organization
OECD	Organization for Economic Cooperation and Development
SAPs	Structural Adjustment Programs
SEEs	State Economic Enterprises
SCF	Free/ Liberal Republican Party
SPO	State Planning Organization (Devlet Planlama Teşkilatı)
USD	United States Dollar
WWI	World War I
WWII	World War II

INTRODUCTION

World economy has been shaped through ages from 18th, 19th, and 20th century. Changes in the world system have affected less developed countries (LDCs), in terms of prices, terms of trade, and institutional laws. First World War (WWI), the Great Depression (1929-1931), and Second World War (WWII) were milestones in international development and trade (Cohn, 2000: 21).

Capitalism in Europe created a world market based on industry's need for raw materials. Pre-capitalist countries were transformed into commodity producers based on need for raw materials. By WWI, world economy focused on exporting capital instead of commodities trade. Industrial capital flowed to backward areas in return for raw materials and markets (Clawson, 1978: 18-19). European Capitalism revived the LDCs awareness of modern economic development (Akamatsu, 1962: 3). Low manufactures of consumer goods was due to focus on war equipment. Therefore, prices increased and LDCs aspired at less reliance on imports. The idea of continuous decline in prices of primary commodity was due to the Prebisch-Singer Thesis¹ (Adewale, 2012:294).

Following the Great Depression, international belief was in weak performance of market economies. The economics of intervention by Keynes spread around the globe, with demand policies authorizing governments to plan the economy to avoid unemployment and inflation. The Great Depression affected LDCs due to four reasons: low international demand for exports, deteriorating terms of trade due to low price elasticity of demand (PED) for primary products, and lack of manufactures supply by industrial countries. Moreover, decline of international funds inflows, and finally debt to the West (Owen and Pamuk, 1998: 6; Naş, 2008: 15; Silva, 2007:67).

¹ A thesis associated with Raul Prebisch and Hans Singer examining how technical influenced welfare in developed and developing countries progress. In Developed countries, technical progress is retained in form of high incomes. In LDCs, it is sent abroad in terms of lower prices (Maneschi, 1983:104).

Less developed countries had to choose an economic strategy to develop. Two promoted alternatives were Import Substitution Industrialization (ISI) in Latin America, and export-oriented industrialization (EOI) or Export-Led Growth (ELG) in East Asia (Gibson and Ward, 1992:331). ISI goes back to 19th century, when Britain was world's greatest industrial power. Later on, European countries such as Germany followed infant industry protection and closed economy principles. Many Western countries had state intervention, through tariffs and licenses. Governments adopted financial measures such as foreign exchange selective rates, rationing, and credit allocation (Brooks and Kurts, 2012: 103).

ISI reflected attitudes favoring industrialization to cure economic crises. Industrialization was a phenomenon in former countries whose economies grew gradually through expanded exports and domestic market (Hirschman, 1968:4). In 1930s, the deteriorated terms of trade of primary exports re-initiated ISI (Waterbury, 1993: 24), as a deliberate policy for economic growth (Baer, 1972:97). WWII increased global shortage of manufactures, and export markets for primary goods collapsed. There was domestic will to overcome dependency on foreign supply sources and diversify production structure (Adly, 2013:14; Ahmad, 1978:21-22).

In 1950s, ISI was the main growth strategy, aiming to divert resources and investments into import replacing sectors. It was expected that capital, skills, and technology transfer would initiate spillovers in whole economy. Instruments followed were tariffs, overvalued exchange rates, quotas, and controls. Tariffs on final goods were higher than tariffs on intermediate goods, to discourage imports of consumer goods and favor capital imports. Capital accumulation was a necessity to improve development outcomes (Adly, 2013:14; Ahmad, 1978:21-22).

Middle East is an important area and a main party in world events. It includes heterogeneous countries such as, Israel, Turkey, Egypt, Yemen, and Saudi Arabia (Kamrava, 2012:96). Middle East can be narrowed down to three countries: Egypt, Turkey, and Israel, because they had a growth path different from countries such as Gulf area, which depended on oil as main source of wealth (Owen and Pamuk, 1998: xvi).

The World Bank defined Middle East to include Middle East and North Africa (MENA) region, Arab League, and Iran. Members are all middle-income except Kuwait and Qatar, which are oil rich; and Yemen, a low-income country (Yousef, 2004: 92). Middle East is an important part of developing world, an area with major population. It is a geo-politically significant region. Egypt and Turkey are the biggest two countries in the area. Both countries had economic interests, in terms of their relative economic size to their neighbors and rivals, economic interdependence in the region, their capacity to undertake giant projects, and military expenditures. Both assumed leadership role in many conflicts that affected world's politics (Kuntay, 2014:8; Owen and Pamuk, 1998:3; Atasoy, 2011:86).

Egypt lies in North Africa. Egypt, for 25 centuries was ruled by foreigners: starting by Persian conquest in 525 B.C., passing by Byzantines, Fatimid, Mamluks, and Turkish conquest in 1516. In 1882, it fell under colony of Britain. Egypt always had a subsistence economy. Between 1920 and 1952, monarchy followed free market system. After 1952, military government moved the economy to state-led growth. During 1970s, the country adopted *Open Door* Policy and signed agreements with IMF, but it did not achieve impressive success (Marsot, 2007:153; Issawi, 1963:5).

Republic of Turkey was established in 1923², after the Ottoman Empire fell. The economy suffered by debts' settlement and low levels of custom duties. In 1923, Lausanne Treaty was signed with an expected expiry in 1929, preventing the country from setting fiscal and protective foreign trade policies (Harrison *et al*, 1993:191; Owen and Pamuk, 1998:13). In 1924, Turkish population was around 13 million, a number reflecting the declining population because of wars. ISI was adopted in Turkey through etatism since 1930s. In 1980s, Turkey adopted much liberalized free economy based on export led Growth. It was considered a successful model by international financial institutions (Harrison *et al*, 1993:191; Owen and Pamuk, 1998:13).

² During the 20th century, the Ottomans had control over some provinces in Europe, Arab lands in Syria and Libya. They imposed their administrative and political power. Young Turk revolution in 1908 was done by officers aiming to reform institutions and enlightens sense of nationalism (Owen, 1992:6).

The rationale of this paper is to examine Import Substitution Industrialization in Egypt and Turkey. Specification of both countries was based on certain considerations. First, both have had common characteristics in terms of natural resources, economic, and political policies. Second, they suffered from external debt, and were similar in terms of internal shortcomings. Both regained their independence in 1923 (Hansen, 1991: 437-459).

In terms of trade policy, Turkey followed the state-led growth through ISI in industries such as textiles and tobacco, in 1930s to increase diversity and develop labor skills. Egypt adopted ISI before 1952, but on limited scale since 1930s. ISI in textile sector was expected to create backward linkages for weaving industries. During ISI, protective states focused on local market that depended on raw materials and agricultural exports (Adly, 2013:15; Richards and Waterbury, 1990: 25). In terms of discussed aspects above, the current study aims at answering these questions: How did state and government affect economic policy and decision making in both countries? What were internal and external factors that created such diverse industrialization and development plans? Were they domestic factors related to capital accumulation, political organization, institutions, trade policy, or external factors related to International Financial Institutions (IFIs) and global events?

The current study starts with an introduction. The first chapter discusses rise of development economics, trade policy, emergence of ISI and its implementation, and export-led growth that some countries adopted after ISI. The second chapter provides an overview on ISI in Egypt. It discusses economic and political incidents that affected economic policies in Egypt. Third chapter explains ISI in Turkey. It discusses the Turkish economy after the Republic was declared in 1923, and passing by Ataturk's reforms, Democrat Party in 1950s, military Coups in 1960s, 1970s, and shift to free market in 1980s. Afterwards, fourth chapter offers a comparative analysis on two countries. The conclusion is followed by the references and appendix.

1. DEVELOPMENT ECONOMICS AND IMPORT SUBSTITUTION INDUSTRIALIZATION

This chapter discusses development economics. It mainly discusses emergence of import substitution industrialization (ISI), its principles, rationales, implementation, and failure. Export-led growth (ELG) is also discussed.

1.1. THE RISE OF DEVELOPMENT ECONOMICS

Underdevelopment and poverty could be attributed to production structures that focused on agriculture and mining (Bruton, 1998: 904), high corruption, and excess power. Economic problems could be lack of foreign exchange, preventing the country from maintaining minimum level of imports or paying for international debt. Social problems could be poor human capital (Richards and Waterbury, 1990:13-17), low educational attainment, and high illiteracy (Hosseini, 1999:26).

Although heterogenic, less developed countries specialized in exporting primary commodities and importing manufactures. This phenomenon resulted from replacing handmade goods with mechanized ones. LDCs are countries with low, lower-middle and upper-middle income, as classified by World Bank. LDCs are diverse in their structure, size, colonial background, resource endowment, ethnic and religious composition, size of public and private sectors, dependence on external political and economic factors, and institutions (Panza, 2014:146; Todaro and Smith, 2006: 10-41).

After Great Depression, the world was divided into developed First World and underdeveloped Third World (Hosseini, 1999:19). Third World describes Latin America, Asia, and African countries that were not First world (Europe and North America), or Second World (Communist-socialist) countries (Smelser and Reed, 2012:231). After WWII, USA became the world hegemony owing to its military and economic power. It had a GDP three times larger than Soviet Union (Alexander, 1967:296; Bruton, 1998: 906; Cohn, 2000:9).

Welfare systems in postwar Europe provided a model for LDCs (Yousef, 2004: 94). It was believed poverty traps could be escaped by government intervention (Rodrik, 2004:1), and that free markets were created to make poor remain poor and rich remain rich (Bruton, 1998:905). Miracle of industrialization in Soviet Union helped embracing greater role of the state in planning all economic activities, aggregate demand, market regulations, resource allocation, and intensive capital industrialization (Alexander, 1967: 296; Cohn, 2000: 9; Krueger, 1997: 2).

After WWII, former colonies gained UN membership. The question was how they would be modern entities. Growth and development studies appeared in form of multidisciplinary endeavor, considering economics, sociology, political science, anthropology, and demography, all factors that matter for governments and financial organizations (Smelser and Reed, 2012:230). The term development economics emerged in 1940s to help policy makers solve problems of backwardness. It was a practical term, field, and subject, sought to consider underdevelopment. It rested on the idea that LDCs suffer from market failure, which necessitated state intervention. Since 1929, Keynesian³ economics saved Western Europe (Hosseini, 1990:19; Krueger, 1997:3; Todaro and Smith, 2006: 104). Central control was to achieve full employment through larger role of governmental fiscal policies, investments in public projects, and less emphasis on international trade and specialization (Cohn, 2000:81; Bruton, 1998: 906).

The basis of the development strategy, which will be implemented in underdeveloped world, and general architecture of postwar world economy were shaped in Bretton Woods Conference in 1944. Three international economic organizations were established to redefine international economic system. The International Monetary Fund (IMF), the International Bank for Reconstruction and Development (IBRD or World Bank), and the General Agreement on Tariffs and Trade (GATT)⁴ (Cohn, 2000:23-81).

³John Maynard Keynes (1883-1946) attributed the Great Depression to overestimation of convergence degree between self-interest and public interest by orthodox liberals. Another economist Karl Polanyi believed self-regulating market was the reason for economic Depression and that societies should shift into protection against unregulated market activities (Cohn, 2000: 81; Bruton, 1998: 906).

⁴In July 1944, the Bretton Woods Conference designed a framework for economic cooperation. IMF and World Bank were part of this institutional framework. There were 27 LDCs, among which 19 were Latin American, but their role

Bretton Woods's institutions stated that underdevelopment was caused by inadequate macroeconomic policies. International financial institutions (IFIs) offered conditional loans (Yousef, 2004:94), recommended industrialization based on expected gains in terms of increased per capita income and productivity (Adewale, 2012: 289-295), and reconstructed the world capitalism (Silva, 2007:70).

Development planning was universally accepted after WWII as means for economic growth, and development plans were made. National planning drew the organizational and institutional mechanism to achieve growth. An economic plan includes quantifiable economic targets to be achieved in certain duration, and strategies to achieve them. Planning is a process through which government decides on social goals and sets targets and implementation frame for its development plan (Todaro and Smith, 2006: 518-519).

In 1950s, UN published seminal reports defining central goals of development, characteristics of LDCs, obstacles to growth, and strategies to achieve self-sustaining growth. Some reports highlighted the role of trade issues in development, balanced growth, and capital accumulation. In 1961, the First Development Decade Plan was published by UN. It was a blueprint for global socio-economic targets and policies of development, focusing on LDCs (Ghai, 2008:768-769). Goals of development were higher national income and productivity (Smelser and Reed, 2012:236).

However, economic performance in absolute terms should not be the only way to judge performance. Other factors should be considered such as life quality, reduced unemployment, and poverty. During second half of 20th century, rapid increases in life standards occurred in many countries. For example, Turkey, between 1920s and 1980s increased per capita income that was above averages in other LDCs. However, it was not an economic miracle, in terms of economic production, human development records (Pamuk, 2008:266). In the 1960s, economic development focused on GNI, and relationship between growth and balance of payments. Employment was another objective beside GNI growth (Thorbecke, 2006:9).

was marginal. There were trials to establish international trade organization, which is as powerful as IMF and World Bank (Cohn, 2000: 23).

In 1960s, planning was viewed as experimental, but gained acceptance in 1970s. It was viewed as techniques for systemic economic analysis done by government. However, the focus was not purely on economic growth, it was general focus on social objectives, improving income distribution and employment (Naş, 2008:5-6).

In the 1970s, development problems did not end. The development process was re-examined. Factors such as under-employment, unequal income distribution, poverty, rural-urban migration, urban congestion, and balance of payment deficits, were considered during development process. Development thinking shifted in favor of distributing growth benefits equally (Ghai, 2008:768-769; Thorbecke, 2006:10-11; Todaro and Smith, 2006: 37).

The concept of economic development refers to change in values and institutions, along with growth in national per capita income. It aims to close gap between rich and poor countries and increase social welfare (Hosseini, 1990:21). It is about improvements in life quality and standards of living, reflecting quality of education represented by human capital (Richards and Waterbury, 1990:12). It refers to promotion of human rights, participation in decision-making, gender equality, social justice, and environmental sustainability (Ghai, 2008:767).

Adly (2013:4) believed economic development was a changing mode of how LDCs insert their economies into global economy, through transformation process into high value-added products in global division of labor. The insertion mode depends on how these countries use social and institutional factors to build a comparative advantage. It was concerned with LDCs sharing different cultures and ideologies, yet, had similar economic problems. It studied institutional, economic, and social mechanisms, which improved people's lives (Todaro and Smith, 2006: 8-9; Adly, 2013:4). Economic development was a transformation of LDCs to a developed status, in terms of economic structure (Ghose, 2010:41).

Development strategies are governmental policies defining and mediating the relationship between country and global economy. A development strategy influences allocation of domestic resources among social groups and industries. Governments set national priorities relative to equity and growth (Gereffi, 1989: 93).

Development policy depends on structure and interdependence among primary, secondary, and tertiary industrial sectors. Primary sectors are fishing and agriculture; secondary are manufactures; tertiary are finance, commerce, and services (Todaro and Smith, 2006: 48). Industrial sector describes manufacturing and industrial activities, of which 50 percent is formed of manufactures (Gemmell, 1985:55).

A question posed by Great Depression and crystallized by WWII was how LDCs could develop and gain economic independence (Ahmad, 1978: 6). The need for development erected different development strategies (Kaya, 2010:1153). Patterns of development study sequence of change in industrial, economic and institutional structure in LDCs, through which modern sector replaces agriculture (Todaro and Smith, 2006: 113).

There is an overlap between economic development and economic growth. The latter describes changes in GDP per year. It reflects an increase in output and economy's annual productivity (Richards and Waterbury, 1990: 12). Thereby, economic growth occurs in developed world and economic development in developing countries. Development is the capacity of one economy with static initial economic status to create and maintain an increase in GNI. It means altered production structure and employment. Agricultural share shrinks and shares of service and industrial sectors increase (Todaro and Smith, 2006:15).

Both terms could be defined according to their origins whether endogenous or exogenous. If productive capacity of domestic economy increased, it would describe endogenous economic growth. Meanwhile, degree of structural changes involved should be considered. Economic development includes qualitative structural changes, and transformation in social, cultural, political, and economic aspects along with output increases. On the other hand, economic growth describes quantitative changes (Hosseini, 1999:22-24).

1.2. IMPORT SUBSTITUTION INDUSTRIALIZATION IN DEVELOPING COUNTRIES

A development policy describes set of interrelated and consistent policies. It depends on three elements: development objectives that are derived from definition of development process, conceptual state of the art that considers available body of development theories, and data system available to analyze situations and evaluate performance (Thorbecke, 2006:1). ISI was one of development policies adopted by some countries, and it is discussed below:

ISI has older origins since 18th century. The Industrial Revolution distinguished industrialized and non-industrialized countries (Panza, 2014:146). Britain was the earliest industrializer thanks to Industrial Revolution, depending on textile exports to accumulate capital (Cohn, 2000: 21; Alexander, 1967: 298). After 1870, sea transport improved, and British manufactures were transformed among national borders (Waterbury, 1999:325; Ahmad, 1978: 21). In the late 19th century, Britain started to lose its power, due to slower trade and industrial protectionism in Europe. Late industrialized countries in Europe improved agricultural sector to create net transfers of savings towards manufactures. For example, USA built its industrial basis through protecting infant industries and restricting imports. Therefore, it became a large industrial power. Alexander Hamilton believed that manufactures development in new American nation was through imports displacement, tariffs, and protection. After initial industrialization in Europe, ISI did not end. It became a part of growth process in 20th century (Ahmad, 1978: 21; Cohn, 2000:21; Alexander, 1967:298; Baer, 1972:95).

LDCs have developed a sector, linked to world's markets within their traditional self-sufficient economies. Shocks to these countries started during WWI and followed up during the Great Depression. Colonies were economically dependent on European markets' demand for primary exports and global prices. The viable solution was either dependency on local resources or giving up on these imports. After the Great Depression, the decision was to declare reliance on domestic capacity towards industrialization and economic independence (Hirschman, 1968:4; Adly, 2013:114; Tafunell, 2007:299-300).

There were international and domestic conditions that necessitated change in LDCs, especially in Latin American countries. Export-led model was adopted between 1860s and 1920s. New social groups were formed such as merchants, middle class, and urban labor. The urbanization was in finance and trade. When liberal model collapsed, conflicts emerged among these groups. In the 1930s and 1940s, it was inevitable to regain social peace, political stability, and economic growth. This means ISI emerged as set of political and social policies adopted by governments to compromise among interests of middle and lower classes (Silva, 2007:68-69).

ISI was in some sectors and had economies of scale. However, when trade restrictions were imposed, the region stagnated (Todaro and Smith, 2006: 47). Latin American countries had attractive external markets for their exports, and there was little need for economic structural change. Moreover, there was no entrepreneurial class, market size, and infrastructure to cope with European powers (Baer, 1972:96).

Before WWII, social and economic development of developing colonies was not an objective for rulers. This objective would have been in contradiction with labor division and trade patterns among colonial blocks (Thorbecke, 2006:1). ISI was the only way towards economic independence and self-sufficiency (Ahmad, 1978:4-6). It was intensified through protective tariffs, exchange controls; preferential treatment for domestic firms importing capital goods, cheap loans, direct participation of governments in some industries (Baer, 1972:98), protection to domestic manufactures, subsidies, and promotional policies for industry (Cameron and North, 1998:51-52), to build a domestic industry, infrastructure, and manufacturing sector (Silva, 2007:67).

In the period following Great Depression, free trade was believed as harmful to LDCs due to some assumptions. The slow demand growth for primary products would decrease export prices and income would be transferred to DCs. Moreover, when import restrictions are absent and high-income elasticity of demand for imports, LDCs grow at slow pace to avoid foreign-exchange crises. Free trade impedes industrialization efforts because of comparative advantage in primary goods. Finally, technical skills and capital are accumulated when industrial expansion takes place. However, specialization in producing primary goods prevents factor productivity's growth (Kavoussi, 1985: 380).

Internal integration among economy parts is hindered by large foreign trade sector. The country becomes dependent on external events, upon which it has no control. Therefore, planning is constrained, and many economic actors lose their stake. Dependency upon trade makes a country vulnerable to political pressures, market disruption, and national autonomy could be compromised. High dependency on foreign trade may constraint future growth. Excessive specialization in single export product harms growth. Finally, product of specialization matters; it should not be a primary good (Moon, 1998: 9-13). Many LDCs maintained poverty, despite of their engagement in trade. There were doubts about if trade was engine of growth (Firebaugh and Bullock, 1986:334-336).

ISI was an attempt to industrialize to end traditional reliance on primary goods exports (Salvatore, 1996:22-23). In general, ISI was an answer to the question of why some countries were rich and others were in deep poverty, and a means to eliminate this poverty (Bruton, 1998: 904). It was expected to make it closer for development through changes in labor productivity, learning by doing, and technological diffusion (Cohn, 2000:18; Ahmad, 1978: 4-5).

1.2.1. Principles of Import Substitution Industrialization

There was gap even between rich and poor LDCs in terms of economic, social, and political systems (Todaro and Smith, 2006: 38-41). There were some principles that helped revival of ISI: rejection of market solution, capital formation, and necessity of replicating the North (Bruton, 1998:905).

1.2.1.1. Rejection of Market Solution

In the second half of the 20th century, the state intervened to maintain regulatory operations and control social interactions. Keynesian demand management and state shaped distribution and consumption patterns, savings, and investments (Duvall and Freeman, 1981:99-100). Resource and commodity markets were imperfect, due to lack of information available for consumers and producers, and absence of single equilibrium (Todaro and Smith, 2006:9).

Free markets were viewed as opponents for development. LDCs were unable to gain revenues due to low price of exported goods. This became significant during the Great Depression, when there was shortage of manufactures. This was reinforced by other facts such as wide poverty in developing South, low wages, labor surplus, slow productivity, rivalry among local exporters and deteriorating net barter terms of trade. By contrast, the developed European North had fast growing productivity, powerful labor unions, and rising wages (Bruton, 1998: 905; Naş, 2008:14-15).

1.2.1.2. Capital Formation is a Key Role for Development

The global belief was that capital goods should be imported, as they grow faster than foreign exchange. There was a need to invest in diverse industries, but domestically produced commodities would not compete with foreign counterparts, so industry had to be protected in its initial phases (Krueger, 1997:4). Accumulated factors of production were keys for growth through machinery and capital investments, skill building, organizational efficiency, and productivity (Pamuk, 2008:273-274).

Capital accumulation is one of three components of economic growth: capital accumulation, -both physical equipment and human capital-, labor force growth and population, and finally technological progress. Future output could be augmented through proportions that are saved and invested. Output levels increase when capital stock of a nation increases. Moreover, investments should be in social and economic infrastructure. This means, investments should consider economic structural changes, trade, resource allocation, and socioeconomic factors such as population distribution and urbanization (Todaro and Smith, 2006:97- 113). For example, in Egypt, through ages, the population growth rate was high and it swept away any possible outcomes from economic reforms (Hansen, 1991: 190-195).

Rates of investment could be accelerated by capital, as increased physical capital to labor ratio was a key for growth. In order to reach this capital level, LDCs overvalued exchange rates to accelerate investment and import capital goods. Government used tariffs, customs, and exchange controls on imported durable goods and later on capital goods. Increased capital would generate effective demand due to better allocation of domestic capital (Hout, 1996:605; Schmitz, 1984:1; Bruton, 1998: 907).

That is why a country can maintain its position in international hierarchy based on capital, and if it is invested in technology development, and productive purposes (Borg, 1992:261). For example, some colonized countries such as Egypt have depended on West due to laws of capital accumulation, which reshape status of advanced and under-developed countries (Clawson, 1978:17).

Technical progress creates and widens gap between DCs and LDCs, in terms of real per capita incomes. Differences depend on rates of capital accumulation and population growth (Maneschi, 1983:105). Technological progress refers to newer ways of doing traditional tasks. (Todaro and Smith, 2006: 98-100). The focus of growth was on accumulated physical and human capital, and endogenous technological change (Rodrik *et al*, 2002:2). Therefore, capital-scarce countries were pressured by external forces to attract investments and react to incentives of international liquidity, such as IMF, which required financial openness from countries willing to receive loans (Brooks and Kurts, 2012: 96-100).

1.2.1.3. Necessity of Replicating the North and Take- Off

The global economy was characterized by inequality in power and wealth between North and South⁵. The South accounted for 65 percent of world population in 1950. It was advised to learn and replicate the North through manufacturing goods previously imported. The South had low GDP⁶, poor infrastructure, lack of modern technology, low social development, and low sanitary facilities (Bruton, 1998: 904; Cohn, 2000:10).

Some common characteristics shared by LDCs are low income, poor education, low productivity, high population growth, external dependency, lack of perfect markets and information, and vulnerable international relations (Todaro and Smith, 2006: 49-50). In early years when LDCs gained independence, the main goal was to realize better living standards and rapid growth (Krueger, 1997:3).

⁵The South included Latin America, Asia and Oceania, the Caribbean, the Middle East and Africa (Cohn, 2000:10; Bruton, 1998: 904).

⁶ GDP describes total value of goods and services produced in domestic economy annually. GNI records income based on who owns production factors rather than production location. GNI adds the income residents earn from foreign activity to GDP, and then subtracts income earned by foreigners through activities in the country (Cohn, 2000:9).

LDCs have abundant labor, while DCs develop labor- saving techniques, so labor-intensive production technologies are advisable for long-term development. Therefore, when LDCs import capital goods, there must be awareness that they did not match their factor endowments. Large labor force should be viewed as productivity increasing factor. It depends on absorptive capacity of economy, degree of capital accumulation, and available skills (Todaro and Smith, 2006: 98-100; Mabro, 1967:322).

The now independent nations were believed to industrialize, if conditions in emerging industrial countries (EICs) were replicated. It reflected a belief that industrialization was similar among all countries, only when conditions were met, as change path was identical (Kaya, 2010:1154). Rostow's linear growth stages model emerged after Cold War in 1950s and 1960s. It defined five stages through which societies move to their modernity path: the traditional society, the preconditions for takeoff, the takeoff, the drive to maturity, and the age of high mass consumption. He believed LDCs were at various stages on the route of development, and all countries would develop, once they achieved take-off (Ateş *et al*, 2005: 249; Cohn, 2000:93; Todaro and Smith, 2006: 105).

Every society witnesses an interval when growth becomes normal condition. A sharp stimulus signals the start of take-off. The stimulus can be a political revolution, technological innovation, or favorable international environment. There would be more innovations and investments (Zilibotti, 1995: 1570).

Take-off includes rapid growth in limited sectors, and modern industry techniques are used. In Britain, textile was the leading sector of industrialization. Cluster of entrepreneurs and technicians grows, capital sources are institutionalized, and the economy predisposes investment sources (Rostow, 1959:5-7). At the beginning of economic development, prices and demand of agricultural products decrease and demand for manufactured products increases, so employment increases. However, later on, demand decreases for manufacturing and increases for services (Kaya, 2010: 1155). The model was valuable to understand how a society can turn from an investor of 5 percent to 12 percent, including changes in institutions, attitudes, and techniques. This conversion was the takeoff (Tsiang, 1964: 619).

According to Arnold (2003:56-57), the South was able to innovate after imitation stage. For example, Japan became a center for Research and Development (R&D) activities. A classical example for Rostow's theory was East Asian countries (Arnold, 2003: 56-57). On the other hand, Cohn (2000: 94) believed the South could not repeat Western model easily because of globalization and increased competition (Cohn, 2000: 94).

The model was optimistic regarding LDCs, and was not applicable to some. In order to have self-sustaining growth, these countries should reach the takeoff stage. LDCs, which were in first or second stages, face different challenges. It was illogical to assume the Western capitalist model as universal one with one direction. Rostow showed no consideration for modernization, historical, or objective aspects of underdevelopment in Third World, which was affected politically, economically and socio-culturally by capitalist penetration during colonialism (Ateş *et al*, 2005: 249; Cohn, 2000:93; Todaro and Smith, 2006: 105).

1.2.2. Rationales behind ISI

Continuing with ISI emergence and influencing factors, Grabowski (1994:536) defined rationales behind ISI. As discussed below, each of these rationales was influenced by some theoretical assumptions.

1.2.2.1. Price Distortions and Surplus Labor: A Two-Sector Economy

In development theories, assumptions⁷ on labor supply conditions relate to labor transfer and terms of trade (Hout, 1972: 210). There are two kinds of world agrarian systems. There is efficient agriculture in DCs, with higher productive capacity and worker output. LDCs have inefficient agriculture, where agricultural output does not suffice local population (Todaro and Smith, 2006: 427).

⁷ Assumptions on labor supply help to distinguish between neoclassical and classical approach to transformation of two-sector economy (Ho, 1972: 210).

Development was a process of structural transformation, accompanied by gradual disappearance of surplus labor and dualism. LDCs differ structurally from DCs, so different framework was needed to analyze problems of economic development. According to Structural Change Model (Two-sector model⁸) by Lewis, LDCs have dual sector economy with a small capitalist modern sector, and large agricultural primitive sector emerged (Bruton, 1998: 908; Todaro and Smith, 2006: 108).

LDCs have labor surplus, and DCs have full employment. Subsistence sector provides unlimited perfectly elastic labor supply, at fixed wage. Modern sector expands without labor constraints. New investments should be diverted and higher wages should be offered to encourage labor shift to modern sector, as it needs technology, capital, and market mechanisms. That is why the idea of North replication through stop importing and support domestic production emerged (Bruton, 1998:908; Todaro and Smith, 2006: 108; Gollin, 2014:74; Ghose, 2010:41).

Lewis model assigned a passive role to subsistence agriculture that provided unlimited labor. Agricultural output does not decline, when rural labor shifts to industry. Dual economy recognized interdependency between two sectors; agricultural sector has to extract resources, while industrial sector has to absorb them (Thorbecke, 2006:6). Subsistence sector is unproductive. Modern sector uses reproducible capital. There is low level of savings and capital accumulation, not because of poverty, but due to small capitalist sector. Growth depends on enlarging capitalist sector, to increase savings. Therefore, it depends on choice of production techniques: labor saving or labor intensive. Movement of labor should stop when surplus in agriculture ends (Mishra, 1969:879). Surplus labor in agriculture means negative⁹ productivity and low wages. Workers shift towards industrial sector, so productivity does not decline. It could improve if new techniques were introduced (Alexander, 1967:300).

⁸ Two-sector model assumes only two sectors, in which industries supply homogenous consumer and capital goods. Conditions assumed are perfect competition, no physical depreciation of capital goods, lack of technical progress, returns to scale are constant, and full employment of labor and capital (Ozga, 1968:368).

⁹ The excess labor in agriculture sector received wage higher than marginal productivity. This wage was equal to opportunity cost of labor in modern sector. In modern sector, wages were equal to marginal productivity of labor (Grabowski, 1994:536).

To increase labor shift to modern sector, return to capital should increase and labor markets have to absorb high numbers of unemployed. That is why, when economic growth is mentioned, industrial structure, distribution of labor, and GDP should be considered (Johnston, 1970: 370-371; Grabowski, 1994:536; Abdel-Baki, 2013:39). The model was generally adopted in 1960s and 1970s. It focused on labor transfer, output, and employment in industrial sector; recognizing backward sector complementary to modern one. However, there was no dualistic framework defining roles of each sector (Thorbecke, 2006:6). Development in overpopulated¹⁰ countries depends on masses of underemployed labor with negligible marginal productivity; they shift to modern capitalist sector, in which output per worker is high. Growth happens by expansion of capitalist sector. Savings come from this sector, and create jobs (Gollin, 2014:72).

The belief that industry rather than agriculture would absorb surplus labor was one of arguments on industrialization (Hansen, 1991:72). It means value added by labor in industry should be higher than value added by same labor in other sectors. It is a short-term view; economies of scale means the firm can reduce its costs of certain production level, while it can produce at optimum dimensions. During domestic industrial development, several distinct, yet similar, processes occur (Ahmad, 1978: 7; Issawi, 1963:170-171). Industries differ among countries; difference lies in sectors influenced by foreign trade and comparative advantage. Primary products have low-income elasticity of demand because of unlimited substitutes included in consumer goods category (Johnston, 1970: 372).

Lewis Theory, however, was a mono-economics framework. It ignored structural differences between LDCs and DCs, so development and growth were supposed to be the same. Mono-economics means that LDCs are not structurally different; they are all poor with low per capita income. In modern sector, labor and capital are used in production, in traditional sector; labor is used along with simple tools and natural resources. In modern sector, capitalistic entrepreneurs include the government, and hire full-time workers (Ghose, 2010: 41-42).

¹⁰ Lewis Model did not study only "underdeveloped" countries, but "overpopulated" countries as well. Overpopulation means large population in relation to fixed production factors, such as land. It is linked to underemployment of labor (Gollin, 2014: 72).

1.2.2.2. Export Pessimism and Dependency Theory: Core –Periphery

Export pessimism¹¹ was promoted by Prebisch-Singer Thesis. It assumed secular declining volatile prices and terms of trade of primary products, which have inelastic demand that lead to slow growth in markets. Balanced growth¹² was necessary through government intervention and incentives to industry. Dependency on primary exports initiates export enclaves rather than development. It does not create linkages. Dependency on primary goods exports is a long-term trend that was rooted in colonial era, and levels of exports processing did not differ through time (Firebaugh and Bullock, 1986:334-335; Bhagwati, 1988: 28; Ficker, 2005: 147).

In 1930s, income and employment fell in DCs, so they demanded less primary goods (Conde, 1992:166). The pessimism about trade in LDCs and its role in economic development was justified by low capacity of LDCs to import goods and services. Low demand resulted from shift to high technology and low-income elasticity¹³ of demand for agricultural commodities (Kavoussi, 1985:379). For example, synthetic substitutes for primary products harmed demand for raw materials. However, synthetic substitutes could not be changed by LDCs; they could only adapt their policies to dampened demand (Firebaugh and Bullock, 1986:334-335; Bhagwati, 1988: 28; Ficker, 2005: 147).

¹¹Ragnar Nurkse contributed to export pessimism view. Nurkse believed foreign markets did not sufficiently accommodate imports, so it was elasticity pessimism (Bhagwati, 1988: 28).

¹²Balanced growth stressed the importance of consistency between output growth in sectors, and differential growth in different good demand, when income increases (Thorbecke, 2006:8).

¹³Engel's law stated that different income elasticity of demand exist for manufactures and agricultural goods. As income increases, expenditures on agricultural goods decline, so terms of trade decline (Conde, 1992:163).

Export pessimism was the atmosphere in which development economics emerged. LDCs had small share in markets for manufactures, and it justified inward-looking strategy after WWII (Bhagwati, 1988: 27-31). Trade was zero-sum¹⁴ game. Advanced nations prosper, and backward nations remain underdeveloped. Export pessimism was rooted in Great Depression; primary commodities had lower purchasing power than industrial ones. Primary goods exported were exchanged for small amounts of processed goods imported (Ficker, 2005: 146-147; Firebaugh and Bullock, 1986:335).

Export composition differs between rich and poor countries. Rich countries export manufactured goods, while primary exports belong to poor countries (Firebaugh and Bullock, 1986:333). The same composition is valid in foreign trade, a periphery producing raw materials and semi-processed goods while importing manufactured goods (Kaya, 2010: 1156-1157). In a subordinated position, in the long term, LDCs hoped to reap dynamic benefits of industry. These dynamic benefits were in terms of stable export price, innovation, and skilled labor. However, LDCs would always be under-developed and DCs would attain all profits due to their industrial economies (Salvatore, 1996:22-23).

The study¹⁵ by Raul Prebisch and Hans Singer attributed growth failure in Latin America to international division of labor¹⁶. Latin American countries had to industrialize to benefit from technological progress. Dependency Theory started in Economic Commission for Latin America and the Caribbean (ECLAC), claiming that under-development depends on structure of capitalist system. A country should control monetary exchange, focus more on fiscal policy, have effective governmental role in national development, give priority to national capital, enhance domestic demand and markets, promote industrialization, increase wages to increase aggregate demand, provide social services to impoverished sectors, and establish domestic industry (Ateş *et al*, 2005: 250; Conde, 1992:163).

¹⁴In DCs, powerful organized labor and oligopolistic industries, labor maintained high wages, and production rates were controlled, prices did not decline (Ficker, 2005: 146-147).

¹⁵ Prebisch's theory became a doctrine of *Economic Commission for Latin America* (ECLA), the *United Nations Industrial Development Organization* (UNIDO), and the *United Nations Conference on Trade and Development* (UNCTAD), established to have collective action. In Latin America, interwar major experiments of ISI were in Argentina, Brazil, Chile, Colombia, Mexico, and Uruguay (Waterbury, 1999:327).

¹⁶There is a two-sector economy in less developed countries, with different productivity and segmented markets, traditional sector relates to the economy, modern sector related to central countries (Conde, 1992:163).

There were hopes that developed world would open markets for exports from LDCs, and that through expertise attracted from core, periphery would develop. Between 1953 and 1961, world trade grew by 63 percent to \$ 111 billion, half of which was trade among core countries, and only imports from LDCs were \$ 22 billion (Waterbury, 1999:331-333). This reflected that DCs had direct or indirect role in whether development was promoted or retarded in LDCs, dependent on foreign sphere, economically and politically, through imports of capital-intensive technologies, consumption and education systems (Todaro and Smith, 2006: 6-48).

Dependency theory was politically oriented and viewed underdevelopment in context of international and local power relations, rigid institutional and economic structures, and duality among countries. It believed in internal and external constraints on development, both politically and institutionally. There was a belief in need for new policies to end poverty and inequality (Todaro and Smith, 2006: 103-104).

The development of core is contingent upon under-development and exploitation of the periphery (Borg, 1992:264). This means that economy of periphery countries changes, but it depends on relations with the core (Clawson, 1978:17). Dependency Theory claimed that development models should recognize culture, history, endowments, and experience of each nation. Universality exists, but it can be applied to mechanisms such as capital, technical and operational tools of development, rather than philosophy and orientation (Ateş *et al*, 2005: 250).

1.2.2.3. Externalities and Infant Industry Protection

Externalities are internal dynamic factors (Schmitz, 1984:1), which existed in terms of increased costs and employee turnover costs. When firms operate in a protected industry, they extend training and development costs for permanent employees (Grabowski, 1994:537). Externalities can be technological, which describe intra-firm effects transmitted outside the market system. For example, one firm is controlling costs of another firm through changing its price or quantities of products, which the other firm buys or uses (Schall, 1971: 983).

Linkages occur when one output from an industry is an input for another industry. Linkages would initiate pressures to create new industries, and so on (Firebaugh and Bullock, 1986:335). Linkages to other intermediate products meant other sectors would increase their productivity (Adewale, 2012: 294). Backward linkages could create industries related to capital goods, metals, and machinery tools. Therefore, high tariffs on imports protect domestic industries. The goal of ISI was to avoid dependency on volatile international markets, improve labor skills, and build a diversified economy (Alexander, 1967:297-299; Richards and Waterbury, 1990: 25).

Protection of infant industries was necessary to maintain level of employment, reorient local savings to industry (Conde, 1992:167), and subsidize infant industries, until they can internationally compete, after achieving economies of scale, because they have high per unit cost and prices. Private agents might not establish an industry, because of externalities or dynamic considerations, so temporary intervention would make entry profitable. On longer run, costs decline below imported costs and achieve return. Once production was domestically feasible, import restrictions were set. Infant industry argument was sort of industrial promotion policy. When an industry has a declining cost curve relative to output or experience, a newly established firm will face high cost relative to existing producers already having low cost production; so these new firms should receive subsidies or protection to allow them turn into low-cost production (Grabowski, 1994: 537; Krueger, 1997:4; Noland and Pack, 2005:2).

There were economies of complementary industries, external to the firm and caused by related industries. Industrialization could create a scientific spirit (Mabro, 1967:343; Issawi, 1963:176-177). Moreover, markets automatically expanded. New industries appeared and recruited workers from non-market sectors, or sectors with low wages and productivity. This income was used to buy consumer goods, which meant another market was opened for capital goods. For example, textile-machine industry created steel industry, or fabricating enterprises (Alexander, 1967:302).

The following part will discuss implementation of ISI, easy and complex stages, and problems that emerged. Moreover, reasons behind ISI failure will be presented.

1.2.3. Implementation and Failure of ISI

ISI was elaborated as an inclusive strategy, formulated by Raul Prebisch and Hans Singer, who advised ISI and trade barriers in 1950s. They believed comparative advantage would persist in primary goods, if LDCs adopted free market economies (Waterbury, 1999:327).

The government during ISI focused on centralization of authority, state building, and empowerment in relation to local and international social groups, capital in particular. The goal was development based on industry and redistributive social policies. Policy favored capital or landowners in order to maintain conditions for capital accumulation. Generally, social support in terms of social coalitions is important for political leaders; otherwise, social forces would challenge them and change their regimes. Levels of support and tension for ISI are affected by four characteristics of social coalitions. First, how inclusive is the coalition, in terms of upper class, middle class, and labor. Second, means of inclusion for rural and urban labor, through labor parties or confederations. Third, political institutions mediating interests of social coalition, is it a single party or multiparty system. Fourth, degree of access by members in coalitions to state institutions and rights, such as lobbying legislature, and representation in public institutions (Silva, 2007: 71).

Three policy issues emerged in response to implemented ISI: how to provide the needed protection for domestic economy, how to increase domestic savings and investment rates, and how to design a plan. ISI was carried on by protective duties, fiscal and credit policy, pressures on foreign importers to set up domestic operations, and state owned industries. Governments adopted quantitative measures to allow supply of imported goods and shut out non-essentials; so domestic producers produced these goods and increased profits (Ahmad, 1978:5; Bruton, 1998: 910).

ISI had an easy and a complex implementation phases. LDCs directed ISI to consumer goods, owing to nature of economic structure, available resources, and technology. Import of manufactures was high, so industrialization started, and proportions of imports fell. Replacing labor-intensive goods, not using complex technology, was relatively an easy task for many LDCs (Cohn, 2000: 308-309; Salvatore, 1996:23; Ahmad, 1978: 25-26).

ISI occurs in initial industries such as consumer goods, building materials using simple technology and capital equipment. Afterwards, the movement to industries requiring larger capital outlay and complex technology, such as complex consumer durables and chemical products (Baer, 1972:98).

Economic growth can occur in early stages of ISI, if imports of nondurable consumer goods were replaced by local production. Consumer goods' production employs unskilled and semiskilled workers; it does not require up-to-date technology or complex capital (Balassa, 1971:181). There were some challenging parts of easy stage. Taxes on exports were through overvaluation of exchange rates, so exports were expensive. Effective tariffs increased with degree of processing. This was a step for assembling foreign primary and intermediate parts through backward linkages (Gibson and Ward, 1992:332; Salvatore, 1996:23).

Accumulation and distribution occur under ISI, and internal market has high role in setting prohibitive protection rates (Boratav, 1986, 135). During this stage, size of domestic market should not pose a problem, as imported goods have predictable market size (Hirschman, 1968:3). The belief was that surplus should be exported, after domestic market was saturated (Ahmad, 1978:5), this ultimate focus on domestic markets increased dependency on raw materials and agricultural exports to obtain foreign exchange (Adly, 2013:15).

ISI aimed to develop an internal manufacturing sector and protect local producers (Krueger, 1980:290). There were effects of early stage of ISI. First, quality control was overlooked, because of absent competition. Even if consumers preferred high quality foreign products, this option was no more available, because of purchasing power absorbed by few local producers. Second, heavy advertising was unnecessary, because of available markets. Most advertising was done by foreign firms reflecting expertise of their home enterprises. This meant lack of adequate concern for consumers' reactions, due to increasing prices of goods (Alexander, 1967:302).

The complex stage starts by substitution of intermediate imported goods such as petrochemicals and consumer durables. High protective tariffs of 100-200 percent were present in Brazil and Argentina, which stirred up domestic goods' prices and production inefficiency. Focus was on building new factories and new capital goods, which in turn created idle plant capacity due to shortage of funds needed for importing raw materials. Excessive capital intensity and low labor absorption also existed, as capital-intensive goods did not generate jobs (Salvatore, 1996:24).

Discrimination in favor of manufacturing protected local manufactures. Local prices were raised through higher protection on imports, so firms producing for domestic markets benefited (Balassa, 1971:178). Mechanized production techniques were not suited to physical environment, where rare land and abundant labor exist. Therefore, rural unemployment increased (Todaro and Smith, 2006: 452). However, ISI made it closer for development through changes in labor productivity and technological diffusion (Ahmad, 1978: 26-28).

ISI was a solution for foreign exchange gap. In order to develop consumer goods, foreign exchange would be saved. By increasing exports, growth would occur without increasing foreign exchange demand. However, on the long run, primary goods' exports would not be viable. ISI in consumer goods increased dependency on imports of other raw materials or capital goods (Ahmad, 1978: 26-28). The country industrializing could meet its consumer goods' demand, but would depend on world for capital goods (Issawi, 1963:176-177; Mabro, 1967:343).

Later stages of ISI include current account deficits, inflation, higher wages, and balance of payment difficulties. Latin American countries deepened ISI without redistributive reforms to expand mass production of basic and standardized goods (Cameron and North, 1998:53). This stage was hard due to unavailable capital, machinery, and foreign exchange in LDCs. Moreover, inequality existed in income and employment; high income was limited to industrial cluster. There was slow growth of primary exports, dependency on imports, and failure to raise manufactures exports (Cohn, 2000:308-309; Kaya, 2010: 1153).

Effective rates of protection (ERP) were used as a tool affecting allocation decisions and which goods to be imported. Other quantitative controls were rather a solution for problems such as balance of payments deficits. Balance of payment problems were believed to be monetary, and treatment was based on exchange rate changes (Bruton, 1998: 913; Ahmad, 1978: 3-5). It should be noted that manufacturing employment is influenced by level of economic development as GDP, trade, and economic globalization; through low-technology exports, not raw materials or primary exports (Cohn, 2000:308-309; Kaya, 2010: 1153).

Many countries implementing ISI squeezed agricultural sector, which in turn hindered growth. Industrialization was financed, although exports did not result from this sector, which in turn weakened domestic demand. Price controls, taxation, quotas, nominal and effective rates of protection existed along with squeezed sector (Bruton, 1998:914). ISI policies imposed an "under the table" tax on agriculture, so income declined due to overvalued exchange rates. Exports became less competitive, and subsidies to industry kept prices of domestic products low (Cameron and North, 1998:53).

Agrarian reform received little attention during early phase of ISI. Manufacturers opposed agrarian reform, in order to allocate resources in capital investments. Moreover, changes in status-quo and land distribution threatened private ownership and power. Rural workers did not urge for agrarian reform, they immigrated to cities to work in new industries. The need was mainly for balanced growth that includes growth and diversification in both agriculture and manufactures (Alexander, 1967:302-303; Todaro and Smith, 2006: 47).

In many LDCs, and Latin American countries, agriculture was a source for surplus invested in urban industry, which in turn increased inequality, reduced food self-sufficiency, and created political instability. There was no land reform or redistributive measures in agricultural sector (Cameron and North, 1998:51-53). LDCs had low-income demand elasticity of primary goods, along with lack of capacity for manufacturing and low living standards. Therefore, export earnings did not grow. This meant a need for growing domestic market instead (Grabowski, 1994:536). Negligence of primary sectors led to decline in earnings from primary exports (Salvatore, 1996:23).

ISI when developed, similar patterns of institutional changes and outcomes follow up. Crises varied among countries, but common symptoms were external debt, balance of payment crisis, and inflation (Waterbury, 1999:326). Personal income increases and raises demand for manufactures. This means changes in output would take some forms: manufactured goods could substitute for domestic handicrafts, domestic production could substitute for goods once imported, or new products could appear. Changes in volume, and structure of output would occur (Ahmad, 1978:7). A successful ISI results in substituting both consumer and high-technology imports (Adewale, 2012:294).

ISI failed due to absence of skilled labor and intermediate goods, low demand for output, misunderstanding domestic economy's needs, changing governmental policies, and low utilization rates of subsidized capital. Absent administrative capacity, inability to effectively allocate subsidies or build capital markets, rent seeking governmental officials and interest groups, were all factors that increased domestic production costs (Bruton, 1998: 914-923; Grabowski, 1994:538; Todaro and Smith, 2006: 37). It failed, due to unachieved economic objectives and social conditions that deteriorated (Dupuy and Truchil, 1979:2-3).

Through “learning by doing”, there would have been synergies between manufactures and technology (Adewale, 2012:294). However, ISI prevented learning (Bruton, 1998: 903), increased corruption, and power concentrated in hands of bureaucrats over import licensing, less transparent decision-making, and pull of government resources to guarantee a working system (Krueger, 1998: 1513). ISI failed owing to excessive degree to which it was followed. On supply side, there was inefficient chaotic allocation of resources and protectionism over all industries without clearly defining key industries to protect. Each country should have decided its leading sector or engine of growth (Liang, 1992:448-449).

Unrealistic expectations were set such as solving unemployment or underemployment problems. Labor was exploited due to over-urbanization in cities and hopes for new high-paying jobs (Salvatore, 1996:24). ISI did not focus on international labor division. Therefore, deindustrialization was a concern for countries restructuring their economies. Institutional factors, migration effects, and government policies increased wages in the formal sector (Bruton, 1998: 913).

Loss of efficiency and welfare was assumed by trade theory, owing to departure from optimum choice and narrow focus on tariffs and protectionism. There was no consideration for structural consequences. ISI created structural changes in output and required changes in economic structure. ISI was not about short-term gains in allocative efficiency, it was a correction for long-term chronic structured disequilibrium in trade and production. Import licenses were rather given to ensure availability of goods. There was ignorance for factors related to market imperfection and structural disequilibrium (Bruton, 1998: 913; Ahmad, 1978: 3-5).

ISI was biased to imports of intermediate goods, so supply of foreign exchange grew slowly unlike demand. More restrictions like import licensing and exchange control whipped up black markets and smuggling (Krueger, 1998:1516). The capital was underutilized; there was no knowledge to use imported complex capital. Therefore, productive sectors were unable to grow fast. This meant persistent poverty and low labor productivity, because of small capital to labor ratio (Bruton, 1998:914).

In manufactures, industry grew faster than local demand, but ISI alternatives ceased. Therefore, domestic demand or exports should have increased, but inefficient industry structure impeded it. Low efficiency and high cost of output were caused by static inefficiency of industry (Schmitz, 1984:3). When foreign exchange income increases, local entrepreneurs exploit industrial opportunities. Foreign firms or non-elite status groups had role in failure of industrialization process to achieve intended political and social effect. In preliminary phases, producers of consumer goods were not able to command compared to machinery or capital manufacturers (Hirschman, 1968:8-12).

Leading industries provided their manufacturers and exporters with influence. Landowners and agricultural producers had power due to important role of primary products during the ISI. The needed government disciplines to be taught and adopted were expected to result from ISI. This was due to rationality, training, reliability, and precise operations. However, financial and economic aspects also have effect on policy and governmental level (Hirschman, 1968:8-12).

Bureaucracy and hierarchical structures were seen as results of large authoritative states, which create dependent societies: corruption, passivity, rigidity, and domination by certain groups. This in turn affected growth and prosperity levels; firms lost their profit and efficiency-oriented motivation. These governments imposed orders and restrained individual freedoms. When large-scale organizations exist, they create complexity through their formal procedures and preciseness. These organizations legitimized power in all societies whether capitalist or non-capitalist societies. Therefore, it was argued that small governments were preferred to avoid bureaucracy imposed on incentives and citizens' rights (Cohn, 2000:83; Finnie *et al*, 2006:187-188).

Some countries that suffered from these negative effects of ISI reoriented their economies towards outer-oriented approach (Krueger, 1998:1514), export promotion (EP) (Liang, 1992:447), outward-oriented development (OOD) (Moon, 1998:7). Export led growth was already adopted in countries in East Asia, and other LDCs adopted it in 1980s, in order to restructure their economies towards free market systems (Buffie, 1992:211). It focused on benefits of foreign trade and exports, and depended on individual countries' characteristics (Bruton, 1998: 914-923; Grabowski, 1994:538).

1.3. EXPORT -LED GROWTH AND FREE TRADE SYSTEM

By 1970s, high international liquidity caused by petrol prices, imbalances in external accounts was covered by loans with negative interest rates. Servicing debts was hard for LDCs, so some LDCs shifted towards exports promotion policy. Debt crisis was severe in many developing countries such as Turkey, which reached partial default, because of overvalued exchange rates, high public spending, state owned enterprises, planning and credit subsidies (Waterbury, 1999:335).

Global recession made it costly for governments to continue welfare and full employment policies. Economic growth rates declined globally, so business groups found difficulty in capital accumulation due to redistribution policies (Cohn, 2000:83; Finnie *et al*, 2006:187-188). Problems created by ISI such as fewer exports, deficits in balance-of-payments and dependency on imports of intermediate goods led to policy reorientation by some LDCs (Cohn, 2000:187).

By 1970s and 1980s, many governments switched back to deregulation, and foreign investment, due to the following reasons: First, advanced technology, communications, and transportations allowing Multinational Corporations (MNCs) and international banks to operate globally. Second, finance provided by IMF and World Bank included conditions such as diversion into liberalized economies. Third, the breakup of Soviet Union led transition economies towards liberal policies (Cohn, 2000:83; Schmitz, 1984:8).

International financial institutions had role as well. In 1980s, World Bank and IMF supported trade liberalization. Loans were given to highly indebted countries to increase exports and trade through financial intermediaries and reforming banking system (Salvatore, 1996:30). IMF and World Bank supported Third World through their structural adjustment programs, economic policies, and deregulation (Jreisat, 2006:413-414).

Export Led Growth (ELG) was based on growth of domestic economy and producer incentives reflecting prices abroad. Trade liberalization was shown to be the sole solution for slow growth. It meant equal incentives for all exporting activities instead of special treatment for ISI industries (Krueger, 1998:1514). Export promotion is about removing trade barriers to help countries integrate in world system, through removing price distortions caused by ISI. It encourages investments in industries with comparative advantage, so factor productivity increases (Kavoussi, 1985:380-382; Laux-MeiselBach, 1989:219; Gibson and Ward, 1992:333).

Classical economists such as David Ricardo believed trade would benefit participants due to international specialization (Firebaugh and Bullock, 1986:334-336). It was believed that trade helps exports to expand and achieve competitive position in world markets. Costs would decline because of scale of economies and resource allocation. Moreover, absent high tariffs and overvalued exchange rates would help to have cost advantage, high efficiency, improved production, and competitiveness (Kavoussi, 1985:380-381).

One influencing factor was Heckscher-Ohlin trade theory, which stated that comparative advantage had sources such as capital and natural resources. The state has comparative advantage in goods that use its abundant factor of production. Accordingly, DCs had comparative advantage in capital-intensive goods. It describes a two sector's economy; labour intensive sector with total specialization, and a capital intensive sector which has economies of scale. Specialization was an essential ingredient of development, as under-development was caused by inadequate exposure to international markets. Others believed comparative advantage was not major driver for development. There should be mastery over wider activities range rather than concentrating on one best done well (Rodrigues, 2010:176-178; Cohn, 2000:170).

The theory created arguments of strategic trade policy about intervention and protectionism. If a nation used temporary trade protection, subsidies, and cooperative government-industry programs in semi-conductors and telecommunications, these industries would achieve economies of scale through large production scale (Salvatore, 1996: 34). ELG reduces static costs of protection such as higher domestic prices, rent seeking, and lobbying. It achieves economies of scale, attracts foreign investments, and accesses foreign technology (Salvatore, 1996:27).

Economic structural changes should be based on comparative advantage considerations, as production in comparatively advantageous sectors incurred fewer costs (Bruton, 1998:904). Performance was affected by domestic demand due to high share consumed by local market from industry's output. Afterwards, productivity, scale of economies, and investments rise. External economy would develop and the industry itself would expand and absorb technological change. Moreover, export sector needed to keep always efficient, competitive, high quality production, and modern design (Hsu, 1972:200).

There were various opinions and debates on relationship between ISI and export led growth. Are they complementary or substitutes? This will be discussed shortly.

1.4. DEBATES BETWEEN ISI AND EXPORT-ORIENTED STRATEGY

LDCs were classified into two groups based on trade policy. One group followed extreme protection through ISI that switched their economies away from optimality criterion. The other group adopted ELG to reach equilibrium between international and domestic marginal rates of return (Krueger, 1980:288-289). Trade strategies lie on spectrum with two pillars of ISI and ELG (Liang, 1992:447-448).

NICs¹⁷ adopted inward-oriented path, in resource-rich countries whose industrial production was based on needs of domestic market. Outward-orientation was adopted by small resource-poor countries that depended on global markets to increase their exports (Gereffi, 1989:92).

Both strategies are vulnerable to systemic constraints such as disrupted trade relation or balance of payment problems (Gereffi, 1989: 93). Under ELG, domestic rewards for exporting were at least equal to or greater than those rewards under free trade. ELG could be as ineffective as ISI; both had their shortcomings on the long run. The idea was that both could be considered as various levels for the same development strategy, so trade liberalization was to be separated from trade openness. Therefore, it would be simultaneous implementation for ISI and ELG (Subasat, 2009: 59).

The relation between ISI and ELG was controversial. It was believed they could not be implemented simultaneously due to trade barriers and bias against exports. In two-sector economy, there was a negative relation between both. Hence, if one country increases imports, exports decline. In order to promote exports, imports should be liberalized (Liang, 1992:448-449). Waterbury (1999: 323) believed that successful export promotion had its bases set by ISI. This means both strategies are to be in balance (Waterbury, 1999:323).

¹⁷NICs lied in two clusters: Latin American, Mexico, Brazil, and Argentina. East Asian countries included Taiwan, Hong Kong, Singapore, and South Korea (Gereffi, 1989: 92).

For Greffi (1989: 94-95), both strategies are not mutually exclusive. Except for Britain and Industrial Revolution, all countries had an initial stage of ISI, where protection included manufacturing industries producing for local markets. Moreover, some LDCs adopted a mixture of advanced ISI and ELG, to avoid ultimate dependency on external or domestic markets, and facilitate industrial diversification needed for global competitiveness. They are complementary and interactive (Gereffi, 1989: 94-95).

ISI as a form of state based policy aimed at recovery and economic independence. After ISI achieves some competitive advantages, the country can follow export promotion to leverage these advantages. Countries with successful ELG established an industrial structure beyond consumer goods' production. If the country aspired at success in ELG, it must accumulate industrial experience (Schmitz, 1984:7; Adewale, 2012:294). ELG positively affected economic growth, because demand for produced goods in LDCs increases. ISI encouraged foreign investors aspiring at benefiting from economic rents in protected economy (Hout, 1996:605).

ELG was highly connected to developmental economics. The term growth should not only be a simple referral to increased exports¹⁸, it should include characteristics of the economy in terms of both accumulated and applied knowledge, entrepreneurship and institutions (Bruton, 1998:904). However, the transition process into ELG should be gradual, it should start by turning quantitative restrictions into tariffs to abolish monopoly and rent seeking. Tariffs then are to be reduced, currency should be depreciated, and then social welfare is achieved. Sustainable liberalization policies should be established when macroeconomic difficulties emerge or if domestic crisis appear, or international pressure exists, it should be undertaken as a single move rather than small steps (Salvatore, 1996: 30).

¹⁸Export promotion should be unbiased against exports. However, others refer to it as effective exchange rates for Exports 'EERX' which can be lower/higher than effective exchange rates for imports 'EERM', it can be called " ultra EP/ISI ," so free trade implies neutral incentives but not vice versa (Subasat, 2009: 47).

In order for a country to develop its export sector, domestic demand should have a minimum level of aggregate demand to establish scale of economies and allow for ISI. Sometimes domestic demand is low due to low-income or local production levels. Therefore, at certain level of aggregate demand, ISI becomes a reachable choice. Aggregate demand provides scale of economies targeting both domestic and international markets. When industry is firstly established, the reliance should be on local market by entrepreneurs, because local market is certain and less risky compared to international risky markets. For example, Japan was exporter of textile before WWII, due to its technical efficiency gained from its domestic market and high local demand (Hsu, 1972:199-200; Krueger, 1980:288-289).

ELG may be slow at the beginning, unlike ISI that is easy at initial stages. Expansion of foreign sales may be slow due to hardships related to quality and delivery, and consumer tastes in different markets. By accumulation of production and marketing skills, export activities become easier. ISI in complex stages require large plant sizes in relation to domestic markets (Kavoussi, 1985: 380-382).

Industrial development and export growth was a matter of technological capability. ISI was not only about efficient static allocation of resources. It could be justified to have protection for infant industries. It was argued ELG does not show biasness in favor of domestic market, it rather subsidizes exports at effective exchange rates achieving equity between exports and imports. That is why success of the strategy is linked to its systemic promotion of exports and trade liberalization. Therefore, it is allowable for some preference for rather than only providing neutral incentives (Liang, 1992:448-449).

Hout (1996:611) believed that adopted development strategy changed orientation of primary goods. ISI diverted production factors away from agriculture and raw materials. ISI reduced domestic capital accumulation due to its inward orientation and lack of competition drives for efficient production. ELG was thought to encourage domestic capital accumulation due to faced pressure on efficiency and quality (Hout, 1996:611).

Rationales are same for ISI and ELG. Dynamic effects of industrialization are realized on the long run, through learning by doing and returns to scale. Both strategies are alternatives towards industrialization; they aim at increasing industrial sectors' size. That is why relative advantages of both are not evaluated (Laux-MeiselBach, 1989:219-220). For Hout (1996:604), strategy by governments shaped political and economic order, and influenced interest groups who attempt to protect their own benefits (Hout, 1996:604). ISI allows discretion for bureaucrats who decide which industries to be encouraged or how to allocate foreign exchanges. On the contrary, free trade allow for reliance on the market and inability of bureaucrats to impose their edicts on foreigners (Krueger, 1998:1516).

ISI was believed to be a politician's dream based on national economy's ability to affect economic growth, through discretionary policies. ELG did not consider discretion, and relied on external world. ISI and authoritarianism were seen as twins, it was hard to move towards democracy and free trade (Waterbury, 1999:324). Government failure was bigger evil, so governments had not to steer the economy. ISI and state ownership achieved some success, but generally created crises. On the other hand, ELG was good for financial interests, exports, and skilled labor, but growth rates in labor and total factor productivity were below rates achieved under ISI (Rodrik, 2004:1).

In the 1950s, when comparing countries that followed ISI such as Argentina to countries followed export-oriented policies such as Singapore and Taiwan, latter group grew faster than first group. Around 10 percent of country's national income was wasted due to ISI (Salvatore, 1996: 25). However, difference did not lie in industrial transformation that happened through state-led growth in Latin America or market-led in East Asia, it was lack of coherent and concerted industrial policy in Latin America, compared to East Asia. This resulted in less deeply rooted transformation in Latin America than in East Asia (Ahmad, 1978: 56). ELG also was a way to evaluate performance of domestic firms getting favoured treatment. East Asians focused on exports, international markets and competitiveness; they terminated financial support to underperformers (Noland and Pack, 2005:10).

Many countries ignored their economic structures, and failed to allocate abundant labor efficiently. The shift to complex stage was not an easy task for many countries, due to lack of foreign exchange, or limited knowledge about new technology. Later on, again caused by international events, many countries shifted to export-oriented strategy. Many countries were inconsistent in their shift from ISI to ELG. They implemented incentives without removing import barriers or currency devaluation. In order for a country to have successful trade liberalization, domestic deregulation is required, private enterprise should be supported, and distortions on price, wage, and interest rates should be removed (Salvatore, 1996: 30).

To conclude, the South was in need for foreign investment, new technologies, and export markets. Therefore, when LDCs develop, free trade and capital flows might help their integration into world economy. However, under ISI, closed economy was the norm, along with infant industry protection and high tariffs (Cohn, 2000: 94).

1.5. IMPLICATIONS AND CONCLUSION

This chapter started by a discussion on economic development, how the term emerged, and under which circumstances. It was clear that two World Wars and the Great Depression were influencing factors. LDCs attempted to imitate the West, through strategies and theories advocated by West (Jreisat, 2006:425).

Development is more than economic term. It is a multifaceted process, reorienting and organizing social and economic systems, institutional and administrative structures (Todaro and Smith, 2006: 102).

LDCs were dependent on core for their development. Developed countries recover from economic crises, and then incorporate LDCs into the new system and hinder their industrialization (Ateş *et al*, 2005: 260). In DCs, agricultural output grew at steady rate since mid 18th century. In LDCs, there was slow change in agricultural production methods, diminishing returns to labor and land because of higher number of labor force to save land (Todaro and Smith, 2006: 428). European countries established colonies to create markets for their exports and use their raw materials for industry and army, such as Britain in Egypt (Marsot, 2007:72-73).

In colonies, economic nationalism was the motive behind industrialization. It describes a nation aiming at independent economy to obtain its freedom. Through the belief that industrialization was only means towards these ends, it was considered a socio-cultural transformation in society, especially in middle class (Shechter, 2008:571).

There were domestic factors such as low national per capita income, absent savings, high-income elasticity of demand for food, high population, high labor-land ratio, and low rates of investments. There was no knowledge on how to utilize labor, and no habits of economic development and industrial achievement, any technology and research. Conditions were different such as factor mix, the policies for saving labor –scarce in Europe-, were different from policies saving capital, which is rare in less developed countries (Yousef, 2004:91; Kamrava, 2012:96).

In 1970s and 1980s, de-industrialization and low growth due to growth redistribution among sectors, financial service sector grew at expense of industry. The failure of state-led growth created internal problems such as inflation, food imports, and stagnant industrial sector, declining agricultural production and resource gap for countries with large population (Richards and Waterbury, 1990:241-242; Schmitz, 1984:3-4). In more liberalized countries, transition from primary-intensive to manufactures-intensive exports was more rapid. However, trade openness should be accompanied with functioning institutions, which could increase costs and risks of international trade, if they were ill functioning (Méon and Sekkat, 2004: 1476).

LDCs had inflexible governance, which was unable to manage reforms, regardless of development framework. Therefore, problems of unemployment, poverty, and violence still exist (Ayubi, 1992:90). Institutions do not change rapidly; they affect today's institutions. Therefore, history is important. Institutional change does not always occur in the efficient way. Institutions can restrict rather than facilitate opportunities. Moreover, they help in resource transfer for favored groups (Pamuk, 2010:18-19). Each country is confronted with various conditions, potential capabilities, and socio-cultural specifications. Therefore, one economic theory cannot be applicable to all countries; historical context of development, internal and external framework, no single reform can be universally successful (Kenawy, 2009:588).

2. IMPORT SUBSTITUTION INDUSTRIALIZATION IN MODERN EGYPT

"Egypt's Main Enemy has been Egypt." Hansen (1991:254).

Through the first half of 20th century, Egypt did not develop its political or economic system. Changes began in second half of 20th century. Egypt had a unique history, changing religions, language, diverse political and social systems (Roussilion, 2008:2). Egypt¹⁹ lies in amid deserts, where people lived and worked (Abdel-Malek, 1964:47). There is fertile soil in Nile Valley and Delta. The soil is suited below level of Nile, so drainage and gravitational irrigation were possible. However, desert lies in above Nile levels, so water lifting is required (Hansen, 1991:439).

Egypt had an agricultural economy, but it was not endowed by national resources. It relied on sources of power such as oil and gasoline, raw materials as salt, cement, and manganese (Issawi, 1963:4-5; El-Kammash, 1968: 20-25; Hansen, 1991:37). The rain was scarce except for the Nile, so lack of water resources can be noticed. Egypt had a unity through years; it can be seen as an oasis surrounded by sea and desert, the flat land created easy route for invaders²⁰, once sea or desert defenses had collapsed (Issawi, 1963:4-5; El-Kammash, 1968: 20-25).

In the last decades of 18th century, Egyptian markets were penetrated by European factories; factory-made European manufactures replaced pre-industrial based manufactures (Panza and Williamson, 2015: 79). International trade grew in the 19th century in Egypt. About 90 percent of exports and 70 percent of imports in 1913 were with Britain (Owen and Pamuk, 1998: 4).

¹⁹Egypt's location in between three continents Asia, Africa, and Europe made it through history prey for foreign conquerors, passing by Albanian, French, Macedonian, Roman, French, and Ottomans between 1517 until 1882, and British (Hansen, 1991:37; Teoman and Kaymak; 2008: 323).

²⁰In 1915, Turks reached Suez Canal and Germans reached Al Alamain in 1942 through desert defenses. Through all times, irrigation was planned for the whole country. Egypt had racial and temperamental homogeneity, which set it apart from neighbors (Issawi, 1963:4-5; El-Kammash, 1968: 20-25).

Cotton was an important source of revenue since first Millennium. The Ottomans isolated Egypt from the world, and it was unaware of revolutions occurring globally (Issawi, 1963:19), until Europe began industrial and finance capitalism through extending political and economic power to Near East (Yale, 1958:425). The modern Egyptian state began by Mohamed Ali in 1805, and continued with British colony in 1882, until 1952. This will be discussed below.

2.1. MOHAMED ALI: EGYPT FROM OTTOMANS TO BRITISH (1805-1882)

Mohamed Ali²¹ founded modern Egypt, both economically and institutionally. Egypt had low social²² conditions. He established a controlled economy, changed land tenure, and removed tax farming. Direct taxes were received by the government, and irrigation system was improved. State owned weaving workshops. Textile factories were set up, and hand weavers worked for them. Long staple cotton was introduced, and Egypt competed with France and UK. In 1830s, cotton exports were 94 percent of total exports. Ali developed communications to assist international trade, and used state monopoly through fixed prices of crops then sold at higher prices. He modernized the army²³ to obtain independence from Ottoman Empire (Marsot, 2007:66; El-Kammash, 1968:39-43; Issawi, 1963:21-22; Teoman and Kaymak; 2008: 326).

Cotton was the main input for European textile industry. Early industrialization plans in Egypt targeted military hardware through military industrial complex. Factories imitated imported goods such as gunpowder and cannon. Imports from Syria and Lebanon of silkworm and mulberry and wool industry were based on imported cashmere goats. Ali attempted to find international markets for these goods (Marsot, 2007:66; El-Kammash, 1968:39-43; Issawi, 1963:21-22; Teoman and Kaymak; 2008: 326).

²¹Mohamed Ali was an Albanian officer who seized power and established dynasty remained from 1805 until 1822 (Marsot, 2007: 66).

²²Educational missions were sent abroad to gain knowledge and learn foreign languages. Mohammed Ali believed education was the only way to implement modern technology (Issawi, 1963: 23).

²³ The army was changed to the European style; French officers were hired, farmers were assigned as soldiers, but senior officers were Ottoman. However, younger officers up to certain rank were Egyptians. There were attempts to modernize and streamline the army (Marsot, 2007: 52).

Perennial irrigation was undertaken on small scale. Water was lifted from the Nile or pumped from under the ground. He introduced perennial irrigation with up-to-date technology. Deep canals were developed to allow for water storage (Hansen, 1991:38-39). Land tenure reforms engendered the new elite consisting of the governor and his family, retains, and Egyptian notables. The land tenure change was a perquisite to transform into cash-economy. However, shortage of work force existed due to the enforcement of incorporation into army. Capitulations required consent of governments toward taxing their citizens. Although industry witnessed changes, machinery and technicians along with factories, level of standards did not increase (Yale, 1958:429; Marsot, 2007:68).

Domestic powerful forces were eradicated, and small farmers had their surplus directly drawn by the system. A monopoly emerged, and the new system created land aristocracy with loyalty to Ali. He aimed at higher agricultural surplus to industrialize and have foreign trade and empower his international position. The planning for irrigation, drainage, and hydraulic system was centralized (Hansen, 1991:23-24; Waterbury, 1999:325-326; Teoman and Kaymak; 2008: 324). Ali intervened to protect domestic market from European manufactures, through non-tariff barriers or subsidies to local manufactures (Panza and Williamson, 2015: 80). Ali was one of earliest rulers to substitute imports of military weapons through building military factories. However, due to penetration of British goods in non-European markets, tariffs were erected. There was a 3 percent tax on British imports. Heavy investments were made in irrigation, factories were built in iron and textiles, and land was redistributed to his dependents. Ali was first to implement ISI, before theories were developed (Hansen, 1991:23-24; Waterbury, 1999:325-326; Teoman and Kaymak; 2008: 324).

The state was the sole planner and provider of inputs; it decided what to produce, at what quantities and prices. Land was granted to family members and officials. Large estates in agriculture appeared. State-sanctioned monopolies made the government an intermediary between merchants and farmers. The beginning was by rice and wheat, and then all commercial crops were included. Forced industrialization and military expansion put pressures on urban and rural population. Agricultural goods were bought by marketing board at low prices, and sold at higher prices, so urban living cost increased (Panza and Williamson, 2015: 82; Ikram, 2006:1-2).

Private urban workshops were closed. Some of the revenues were invested in irrigation and transportation, and by 1830s, a diversified industrial sector emerged in Egypt, with light and heavy industries. There were cotton spinning and weaving, textiles, food processing, coffee roasting, and oil processing. There were market trade relations in Egypt, and peasants were prohibited from selling grains to brokers, fixed prices were set for surplus supplies sold to the state. New commercial network was set up to sell grain to Spain and Portugal (Teoman and Kaymak; 2008: 325-326; Panza and Williamson, 2015: 82).

Farmers in Egypt since Ottoman rule never attained fair compensation for farming activities. They did not get private ownership rights until second half of 19th century (Issawi, 1963:4-5; El-Kammash, 1968: 20-25). Ali was the sole landowner. This meant unequal distribution of ownership and cultivation units. State land was passed to private ownership. This in turn created a landowners class (Hansen, 1991:48). The goal of agrarian form was to keep agricultural surplus in hands of state (Batou, 1993: 283).

It was parasitical class of landowners, which controlled life for more than a century. Bureaucrats and palace sycophants became more powerful through agrarian and financial exploitation. Egyptian peasants and urban workers did not have protection such as European trade unions and social legislation. The lack of knowledge of western finance and existence of many lenders harmed the economy (Yale, 1958:427-428).

Between 1812 and 1840, state-led fiscal policies diverted resources towards industry. After defeat to Ottomans in 1839, ISI strategy transited to laissez-faire until 1930s (Ikram, 2006:1-2). Anglo-Ottoman Treaty prevented high tariffs. However, non-tariff barriers were adopted. Domestic factories supplied military clothing, subjects were forced to buy domestic production, and special stamp was given to domestic textiles (Panza and Williamson, 2015: 80-81). Capital, investment, and labor were provided. Foreign technicians and skilled labor were attracted by higher wages. Industry protection was only a means to substitute imports through monopoly. Capitalist relations were not fully developed, because of monopoly and ban on selling products (Teoman and Kaymak; 2008: 327-328).

In order to integrate a country into world system, it should witness some structural changes. There was gradual removal of restrictions on land private ownership. Foreigners were permitted to buy any land, so that foreign capital took part in Egyptian agriculture. Egyptians under capitulations did not enjoy same rights as foreigners²⁴, and there was no Egyptian business or professional class. Rich members devoted their work into agriculture, while educated ones flew into civil service, irrigation, and railway systems. The goal was to develop capitalist agriculture (Teoman and Kaymak; 2008: 314-317; Issawi, 1963:25-26; El-Kammash, 1968:39-43).

Since Mohamed Ali²⁵, agricultural exports were based on cotton and hydraulic investments. By 1830s, lack of experience created administrative and organizational problems, new technology appeared, but weaving firms did not operate accordingly (Teoman and Kaymak, 2008: 327-328). Egypt reached its maximum of cultivated area in 1897. Other problems emerged such as pests, low quality, and poorly designed drainage systems (Hansen, 1991: 39-65). The focus was to have strong army²⁶ and navy. Egypt was exploited by the West²⁷ (Yale, 1958:429; Marsot, 2007:68).

Since 1858, foreign debt was owing to corruption of monarchs and subordinates along with high interest rates on loans. Egypt relied mainly on cotton exports, and ignored wheat. Foreign capital was attracted to cotton investment. However, revenues were not invested; they were absorbed by domestic demands of higher life standards and population rise (Issawi, 1963:27-28).

²⁴Mixed courts in 1875 were setup to provide legal framework for foreigners' rights. Labor and land became commodities to be sold and bought. Transport and irrigated areas witnessed improvements; Alexandria-Cairo railway was opened in 1853. Suez Canal inauguration in 1869 made Egypt an important route for international trade. Fiscal and judicial immunity favored foreigners, who had ties with European market (Teoman and Kaymak; 2008: 314-317; Issawi, 1963: 25-26).

²⁵ By death of Mohamed Ali in 1849, Egypt was not indebted (Hansen, 1991: 52-56).

²⁶ The 1841 defeat to Great powers and compulsory reduction of the army, Anglo-Turkish convention in 1838 allowed foreigners to freely trade within Ottoman dominions, so competition of European industry led to decline of factories (Issawi, 1963: 24).

²⁷ Egyptian economy was exhausted by global wars; grains were exported to feed British army fighting against Napoleon. Egyptians were not ready yet to protect themselves against European penetration. It could be seen that Egyptian Khedives were victims of modernization (Yale, 1958:429; Marsot, 2007: 68).

To conclude, in 19th and early twentieth century, modern economic development took place. Manufactured exports from Britain and Europe expanded. Labor shifted to agriculture and construction. However, Egypt became a mono-crop exporter (Hansen, 1991:438), until 1952 Revolution, as will be explained below.

2.2. FREE MARKET ECONOMY/PRIVATE ENTERPRISE (1882-1952)

Egypt's role in world division of labor from 1840 until 1952 was as pure exporter of raw cotton (Waterbury, 1999:325). In 1882, Egypt was absorbed by Britain, which viewed it as an agricultural colonial unit. It built dams and canals, achieved maximum allocation of land, but closed down domestic industries. Britain built institutions based on single-crop economy (Pamuk, 2010:22). It did not encourage industrialization in Egypt that was a market for British manufactures (El-Kammash, 1968: 39-43). The British colony created a traditional governance system with absolute family rule (Jreisat, 2006:412). There was no declared industrialization policy in 1903-1907, but industrialization efforts were financed by foreign capital, which benefited from boom in cotton prices (Hansen, 1991:71).

Resources were exploited in favor of European finance and non-Egyptian domestic partners. In early few decades of the 20th century, a group of investors attempted to maintain control over production, distribution of goods, and services, using state's resources and coercive force. In the first half of 20th century, domestic investors had access to state and foreign capital, so private enterprises and domestic industries were created (Vitalis, 1995:2). Egypt had commodity relations based on export production and manufactured consumer goods imports. There was no capitalist production in Egypt until WWI. Egypt was a prosperous country; income and agricultural production rose, but no local industry, caused by constricted domestic market and shortage of savings (Clawson, 1978: 18).

The monetary system was inefficient until 1914. Egypt had an adequate infrastructure in communication and transportation before WWI. National Bank of Egypt (NBE) was built in 1897, as private foreign bank. It began serving as central bank in 1951 (Hansen, 1991: 448). National Bank²⁸ of Egypt (NBE) was not a central bank; it did not set discount rates, or provide last resort for deposit banks (Hansen, 1991:41-52).

During WWI, sharp fall in prices of commodities led to deteriorated terms of trade and decreased real value of exports. Cotton constituted 80 percent of total exports. High ratio of foreign debt to GNI did not allow for increase in real national income. The rising population consumed cereal production. Shortage of imported manufactured created a need for industrialization (Issawi, 1963:35-36). When cotton prices declined, landowners shifted to industry, and became industrial capitalists (Clawson, 1978:19).

There was no capitalist production in Egypt until WWI (Clawson, 1978:18). It always had rare resources, rapidly increasing population, corruption, inefficient public sector, lack of investments, shallow industrial sector, income inequality, and absence of entrepreneurship and innovation. It was never an easy country to rule (Marsot, 2007:176). There should have been structural change in non-industrial sectors: social overhead capital in transport to be built up. This allows for market creation, state control, and exploitation of natural resources. Afterwards, a revolution in agriculture to keep modernization process. Imports should be financed by efficient production. Capital imports can be accessed through higher foreign exchange (Biersteker, 1990: 482).

In 1923, Egypt became a constitutional monarchy²⁹ with limited parliamentary system (Hansen, 1991:37). It won its independence, but the King, British High Commissioner, and smaller parties along with Wafd³⁰ Party were main actors (Owen, 1992:132-133).

²⁸Reserves of private banks were kept in London until WWII. During WWI, gold imports were cut off, and NBE note became legal tender. Until 1940s, Egypt followed gold standard of pound sterling (Hansen, 1991: 52).

²⁹ Ten general parliamentary elections occurred until 1952. There were attempts to make winners other than Wafd. This made different set of rules in every election (Owen, 1992:132-133).

³⁰ Al Wafd started as delegation under leadership of Saad Zaghloul in 1918. It presented Egyptian demands for independence in London, at the Peace Conference (Hansen, 1991: 61).

Nationalists³¹ struggled to build a politically modern and independent Egypt. Modern government³² was shaped in the mid-nineteenth century. British colony increased efficiency in public administration, but ignored low echelons (Hansen, 1991: 37-59). In 1902, the Agricultural Bank was built to serve small farmers through short-term mortgage loans, but it was liquidated in 1937. Bank Misr was established in 1920. It created Egyptian bourgeoisie and helped in credit and industry sector. Major economic activities except international trade and agriculture were owned by foreigners, but Misr Bank helped Egyptian participation in trade and industry (Issawi, 1963:40-41).

The Bank depended on medium-size landowners for initial capital, and managed governmental loans to industrial investments. Post WWII, it was an important development bank (Hansen, 1991:88). It was a holding company and an investment bank. Local manufacturers called for consumers to support cause of "buying Egyptian" (Shechter, 2008:573). That is why it was a consolidation for industrial bourgeoisie in Egypt, who aspired at Egyptian industry (Vitalis, 1995:8).

Landowners were major investors in Misr Bank, and owned 87 percent of capital in Spinning and Weaving Company. It opposed any foreign partnership. However, it accepted foreign partners and seek foreign technology, which threatened to establish competing firms. Entire economy was dominated, printing press, button factories, linen-spinning mills (Clawson, 1978:20; Vitalis, 1995:8). In 1924, Egypt had textiles and handicraft industry. In 1931, there were 174 leather tanneries. Local artisans produced soup, suits, tents, cigarettes. Small-scale cigarettes³³, confectioneries, and glassware had small capital and employed small numbers (Tingor, 1980: 106).

³¹Economic nationalism is an old term in Egyptian society that founded its national identity. It originated during Urabi movement (1881-1882) when there were calls to build a national bank (Shechter, 2008:573).

³² Khedive Ismail improved public administration in alignment with European lines (Hansen, 1991: 37-59).

³³ Greek entrepreneurs who migrated from Turkey after Ottoman decree in 1876 established modern cigarette industry in Egypt, and it became a state monopoly. When British officers publicized their quality in Europe, it became an exported good, with 2 percent of total value of exports in 1919 (Tingor, 1980: 107).

Misr Spinning and Weaving Company that was established in 1927 became the largest industrial enterprise in the Middle East. It had twenty-seven industrial, commercial, and financial firms. It had common investment and management strategies and regulated relations among sectors and their views on social and economic policies (Beinin, 2008:310-325). It was expected to establish cotton industry, but high quality³⁴ textiles and fine fabrics had a limited domestic market. Consequently, production was not developed for exporting (Hansen, 1991:89).

Egypt once had yields of crops that were highest in the world: extra long staple cotton, sugarcane, and peanuts. Some technical changes took place, yields were high, economy was capitalist rural, technical changes were to repair some of damages caused by British (Richards, 1980:304). In 1918, Commission on Commerce and Industry called for building an industrial development bank and following ISI in industries like ceramics, sugar, and fertilizers. It called for protective tariffs, but no autonomy was granted until 1930 (Waterbury, 1999:327; Issawi, 1963: 43-44).

The Commission provided a report suggesting ISI to be financed by Egyptian and foreign capital, through gradual Egyptianization of skilled labor. The society embraced this strategy, and projects beneficial for the nation were adopted and eschewed nationalism (Beinin, 2008:310-311). It was a call to end dependency on imports, increase employment, and avoid one-crop exporting (Hansen, 1991:137-138). Economic and political arrangements existed among tradesmen, bureaucrats, politicians, and British consuls. After capitulations were abolished, Egyptian tradesmen had larger power compared to foreign capital. Factors such as poor drainage, low international prices, shortage of fertilizers, income inequality, and land distribution affected growth negatively (Beinin, 2008:320).

Egypt did not develop a strategy to cope with world events. Egyptian cotton was sold at organized commodity markets, at positive but low prices, which deflated price of imports and exports, and deteriorated terms of trade (Hansen, 1991: 75).

³⁴In 1938, there became a joint venture with British company, Bradford Dyers to produce textiles of high quality (Hansen, 1991: 89).

There was no social dynamism dividing Egypt from a modern Europe. There was a submissive economy integrated into world's markets. Private ownership, commoditized labor, capital accumulation, bureaucratic commercial and industrial enterprises were features of the economy (Beinin, 2008:329-332; Clawson, 1978:20).

In 1933, 77 percent of assets in manufacturing and commercial firms had foreign partners. In 1930s and 1940s, laws required Egyptianization of firms. In 1947, law stated 51 percent of capital 40 percent of board of director, 75 percent of employees, and 90 percent of workers to be Egyptian. Imports increased, but exports declines, the technology, machinery, and expertise were imported. The government extended its control span over companies through Egyptianization Law in 1947 allowing for local management and financial control. By WWII, Egyptian industry provided 100 percent of sugar, salt, cigarettes, 90 percent of cement, soap, and shoes, 80 percent of matches and furniture. There was self-sufficiency in consumer goods before WWII (Clawson, 1978:21; Shechter, 2008:573).

During WWII, there was natural protection against foreign competition. Moreover, local demand expanded by Allied military authorities and personnel. Some infant industries received protection. Industrial output increased by 35 between 1939 and 1945. Egypt preserved its neutrality until last months. There was decline in living standards caused by shortage in necessities. Employment increased, around 200,000 Egyptians were employed by Allied Forces. Egypt accumulated foreign reserves during wars, but expenditures by Allied forces and loans from National Bank of Egypt negatively affected the economy (Hansen, 1991:96-97).

Some positive changes were related to factory industry: skilled labor and technicians, continuous improvements in transport due to modernized railways, removal of direct tax, and reduction of debt during war. The government supported firms through prohibitive duties, duty exemptions of capital imports, credit advancement, flexible treatment for treatment for depreciation charges; vocational training, fiscal assistance and control quality. However, price controls, quantitative restrictions on imports, cotton imports' prohibition, and multiplicity of authority negatively affected efficiency (Issawi, 1963:196-197).

Balanced industry existed. During interwar years, industry gross investment was the same, but increased by 50 percent after war. Unlike agricultural investment that declined. Egypt followed a balanced growth strategy in the 1930s, but shifted towards industrialization after WWII. There were no well-planned growth rates or employment ratios in capital output (Hansen, 1991:71). There was a pre-dominant free enterprise economy; state directly intervened and supervised all aspects related to irrigation and railways. Egypt exhibited unlimited supplies of labor. In 1948, there was an estimation of 50 percent of agricultural labor to be withdrawn without harm to production (Mabro, 1967:324).

During WWII, land distribution was on top of social agenda due to population growth, urbanization, limited cultivate area, and unemployment. Many proposals were made for land reform, to divert resources towards manufacturing, but dominant landowners opposed (Beinin, 2008:310). In WWII, imports declined and large-scale exports by allied troops increased demand for industrial products, textiles, preserved food, and mechanical industries. Agriculture, society, and politics were dominated by large landowners. All shipping, railways, and services in Europeanized areas served cotton. Most of Egyptian capital was controlled by foreigners: the Suez Canal Company, the National Bank of Egypt, Shell Oil Company (Beinin, 2008:331; Issawi, 1963:38-41).

There was division within bourgeoisie: identity, function, or sectorial location. They were not able to act in their collective interests. There were rival business groups and powerful private institutions. Large-scale private capitalist institutions were facilitated by colonial enterprise and coordination between landowners or merchants with European investors (Vitalis, 1995:8-9). The centralized autocracy made the government an initiator of any business to be thought, along with general mistrust of government and governors. Not only political oppression, but also economic exploitation was the fate of Egyptians (Issawi, 1963:195-196).

Social side was ignored. After independence, a law in 1923 made education free and obligatory. The majority of graduates were employed by government sector. The lack of initiative and risk taking, undernourished students, changes in educational system and overcrowded classes led towards poor quality of education. The education system was not adequately developed both under British regime and after independence (Hansen, 1991:25; Issawi, 1963:195-196). Low human capital endowment was an obstacle to economies of scale in industrialization (Thorbecke, 2006:15).

Yale (1958:432) believed that British colony had left some positive changes. Modernization efforts were fast-paced in all life aspects. British skilled administration and civil servants trained Egyptian government to get rid of bureaucracy. There was no more harsh treatment for peasants, law of order was maintained, foreign capital inflows increased, the property was specified to upper class and foreigners. The British paved the way for social and economic revolution led by free officers in 1952. Egyptian economy interacted with West during first half of 20th century. Production structure shifted to cotton production rather than food production. Foreign modern financial institutions undertook commercial transactions, Egypt took its part in global economic system; the new social order was created by Britain (Yale, 1958:430-432).

2.3. A STATE-LED ECONOMY (1952-1971)

The revolution in 1952 was voice of people³⁵. It was socially backed. It was first time for Egyptians to rule since time of Pharaohs. The new regime was common to all Egyptians in terms of religion, culture, and language. The end of monarchy signaled an end for British intervention. A government that is 100 percent consisting of Egyptians was expected to act in favor of society (Marsot, 2007:72; Yale, 1958:436). A mixture of agrarian capitalism and feudalism initiated the anti-feudal coup. The Egyptian economy was capitalist since last quarter of the 19th century, as cotton exports increased, and wage-earning labor was used (Abdel Malek, 1964: 45).

³⁵British occupation created Anti-West nationalist movements. Arab Nationalism was successor of Egyptian Nationalism of 19th century (Marsot, 2007: 72).

Monarchy was abolished and Republic of Egypt³⁶ was declared on June 18, 1953. The Revolutionary Command Council consisted of men from low and low-middle class. The parliamentary³⁷ rule was ended, because it was corrupt and incompetent. Political parties were dissolved; liberation front was established in 1953 to signal a single party reign. The public expected a return to parliamentary life, but division³⁸ among officers prevented it (Yale, 1958:436-437; Marsot, 2007:128).

Gamal Abdel Nasser used the state to build a political base due to absent political organization. The regime increased distributive rewards to create a political constituency and gain support of opposing groups (Cooper, 1979:483). He aimed at internal stability and welfare, with political activities classified into three categories: create and maintain political power, introduce social, economic, and political changes, and to develop independent foreign policy (Çoban, 2007:44).

Three stages occurred in Egypt, a semi-independent state, in which agrarian bourgeoisie cooperated with foreign capital to rule the society. The first stage lasted from 1952 until 1956. Second stage was from 1956 until 1961. The final stage was from 1962 until 1970 (Abdel-Malek, 1964:38).

2.3.1. The First Stage (1952-1956): Start by Land Reform

Development strategy by revolutionary leaders was based on some keys. Modernization and industrialization were keys for better life. Capital was to be diverted away from agriculture by voluntary or forced methods. Modernization of agriculture was to increase productivity, and strengthen its role in national development. Moreover, containment of any opposition forces such as powerful landowners. Finally, small cultivators would be supported to realize social justice and political wisdom (Harik, 1984:43-44).

³⁶Naguib was a president and prime minister, while Nasser was deputy prime minister and minister of the interior. There was a three-year's transitional period to think of governmental form to follow (Marsot, 2007:128-128).

³⁷The Wafd and monarchy lost credibility because of personal behavior of King Farouk, humiliation of British hands, and corruption in upper party positions (Yale, 1958:436-437).

³⁸ Mohamed Naguib cooperated with political leaders and civilian ministers to set laws such as agrarian laws, abolishing 1923 Constitution and building permanent council for development of national production. Naguib's supporters aspired for parliamentary government, and Nasser's supporters demanded an authoritarian rule (Yale, 1958:436-437; Marsot, 2007:128-128).

Nasser used three measures to shape agriculture: land reform, investment decisions, and price policies (Richards, 1980:305). Public sector had to grab economy's resources and direct them into SEEs. Goods were produced at affordable prices and controlled by the state. Although they had low quality, life quality generally improved. Employment for thousands was guaranteed, so political and social stability were maintained (Rutherford, 2008:133).

By 1952, Egypt had no hereditary landed aristocracy. The Law of September 1952 was the basis for wealth redistribution. Before reform, 2000 owners out of 2.8 million owned 20 percent of total land, while 2.6 million owned 36 percent of land. The land reform destroyed power of large landowners through redistributing land to farmers (Marsot, 2007:152). By 1952, Egypt had more than half of its labor force as rural workers. Agriculture contributed one-third to GNI, industry was 15 percent of GNI (Harik, 1984:43-44).

The 178,000 feddans of royal family were expropriated without compensating, so the state made high profits. In 1952 Law, Article 3, there was compulsory reduction in agricultural rents, which benefited around four million peasants, whose income increased by 50 percent. Under parliamentary regime³⁹, landowners were politically powerful and resentful to any reform. Land reform established a cooperative system for beneficiaries and regulated relations between landowners and peasants (Mansfield, 1973:672; Roussilion, 2008:338).

Owners of excess land were allowed to sell it at price fixed at seventy times the land tax, through a limited time of month and a half, which starts after law's promulgation. Land unsold was requisitioned by state in return for indemnities fixed at ten times its rent value; including value of machinery even trees (Mansfield, 1973:672; Roussilion, 2008:338). Nasser faced chaos in cotton, budget, and balance of payments. The cotton exchange was closed in 1952, and reopened in 1955. Government manipulation and private speculation during Korean boom and collapsing world prices harmed Egyptian cotton trade (Issawi, 1963:51-53).

³⁹The Wafd had funds and resources, public support, and historical background since WWI. The Law of Political Parties obligated the Wafd to share their programs publicly, internal organization, and funds to Minister of Interior (Mansfield, 1973:672-673).

Incentives were used to encourage private investments. However, capital was rather directed to construction activities. Agricultural cooperatives were introduced and farmers were obliged to membership, abiding by rules concerning prices, marketing, and crop rotation. The government gradually increased its involvement in economic sphere. In 1953, the Permanent Council for the Development of National Production was created to compromise representatives of both sectors, coordinate projects, and divert local capital towards industry (Abdel-Malek, 1964:40; Harik, 1984:45; Issawi, 1963:52-54; Ikram, 2006:3).

Production cooperatives were obligatory for private agriculture holdings. Prices of sold lands were financially favorable compared to nominal compensation for old owners. Cooperatives were supposed to enforce rationality in crop rotation, provide seeds and fertilizers, and market agricultural products. Lands that exceeded fixed ceiling were distributed among landless cultivators. The system was compulsory for all villages and export crops in 1960s, with a cultivator bearing whole responsibility and government helping through cooperative services (Harik, 1984:44-45; Hansen, 1991: 124-125).

Table 1. Changes in holdings of small landowners (five feddans or less)

Year	Number of Owners	Total area held (feddans)	Average holding per owner (feddans)
1961	2,919,000	3,172,000	1.08
1965	3,033,000	3,693,000	1.20
1975	2,693,264	3,948,165	1.50

Source: Harik (1984: 47).

Table 1 shows that average holding for small peasants, with five feddans or less increased from 1.08 feddans in 1961 to 1.20 in 1965, and 1.50 in 1974. Small peasants increased after reform in 1952, but declined by 1974 (Harik, 1984: 47). Landless labor (non-tenants) was worse, as reforms decreased their employment, as these tenants receiving small plots depended on family members, and constituted large proportion of rural population, but they decreased after reform (Richards, 1980:305-307).

Small peasants owning less than five feddans rose from 35.4 percent in 1952 to 54.8 percent in 1964 (Podeh and Winckler, 2004: 21-22). Tenants with five work animals participated in government and animal insurance. Tenants with more than fifteen feddans obtained seeds. Farmers with less than five feddans were not allowed to plan profitable crops. Government bought crops at prices that are 20/25 percent of international price. There was no mobilization or competent cadres, so gap was larger between poor and rich peasants, directly profits increased by rich ones, while indirectly crops were consumed by tourists or middle-urban class, cotton was reduced, foreign exchange was in shortage, and wheat imports increased (Richards, 1980:307). Population growth did not allow land reform to achieve expected benefits. After 1975, the rural sector received attention and new framework was setup to fix institutional and national system's shortcomings. Institutional reform focused on local government (Harik, 1984:53).

Farmers received low prices, because of cooperative marketing. High taxes were an implicit burden on farmer. Small farmers produced crops such as wheat and cotton. Large farmers grew crops uncovered by price controls. Therefore, output of fruits or vegetables was not subject to cooperatives regulations, which in turn increased their profits (Levy, 1968: 100-101). Favorable treatment targeted well-to-do farmers, who normally were rich. They were first to receive scarce inputs. Crop consolidation required small peasants to plant cotton all in one year, and wheat in one year. Peasants were in need for cash or credit, supplied by rich peasants (Richards, 1980:305-307).

In 1961, about 10 percent of land cultivated was redistributed, and less than 250,000 families benefited. Large landowners did not sell extra land to peasants. The number of proprietors with less than five feddans could have risen from 35 to 49 percent of landholdings at end of 1950s. Links of intermediate proprietorship were created between micro holders and large holders. In 1961, limits were 100 feddans per proprietor, after it was 200/300 per family. Renting feddans was prohibited, and 2.50,000 feddans were redistributed, 45,000 feddans were added from sequestered individuals (Roussilion, 2008:344-345).

There was strict control over crops of cotton and rice, purchase of portions of output, and control over purchases of seeds and pesticides. Land reclamation increased the cultivated area by less than 15 percent, and it was of less productivity. Political mobilization of peasants was done through political participation and peasants becoming leaders. Finally, rural community received services, development facilities, schools, and supply of technical and medical staff in rural areas and minimum wages laws (Harik, 1984:44-45). The reform was only profitable to those who already had stake, the upper segment of low-income group due to restrictions on better forms of wealth distribution. Land reform involved 16 percent of cultivated land and redistributed 13 percent to around 10 percent of total rural families. If equal shares were received by each rural family, plot would have equaled 1.8 feddans, which could do better in terms of subsistence (Ikram, 2006:9).

Cooperatives were somehow successful (Mansfield, 1973:672; Roussilion, 2008:338), because managerial functions of landowners were now done by state agencies. The pesticides, inputs, and tractor services were provided at subsidized prices (Richards, 1980:305-307). However, it generally failed due to incompetent bureaucrats and overstaffing. It provided poor-quality services and inputs; it was biased towards better-off farmers (Hansen, 1991: 124-125). For Harik (1984:44-49), performance of cooperatives could be acceptable, if institutions performed part of the business. There was overload on cooperatives; it was responsible for designing agricultural mechanization capacity, marketing of products, and determining cultivation services. Responsibilities were added without available personnel, work was not done, fear of responsibility existed, and peasants faced bribery and poor performance (Harik, 1984:44-49).

Mechanization process improved regular operations and timeliness. Animal power was replaced by machines. However, productivity of labor in agriculture declined. The cotton leaf worm attacked the crop and reduced it by 4 percent in 1961⁴⁰. Agriculture had negative conditions such as bad climate, lack of cooperation between farmers and authorities along with lack of enough pesticides (Issawi, 1963:60-61). Medium-size landowners did not witness changes in their shares of cultivated area. However, the reform never aimed at elimination of landlessness problem, due to land scarcity and limited amounts of redistributed areas. In 1969, the final ceiling of 50 feddans meant high income and landless people still exist, absence of follow up information about distributed areas or number of misappropriated persons, if ceilings were lower by ten feddans, landless problem would have been solved. Expectations set were not so realistic and impressions were basic for judging (Harik, 1984:46).

There was no urban class support for the regime, and bureaucracy was adopted by engineers and decision makers. Moreover, peasantry had no chance for mobilization campaigns of large-scale masses. Land ownership differed from farms as distributive units. Rich peasants did not get land directly; it was distress sales made by larger landowners. Government was not effective in restricting their power, tenancy laws were enacted, and leases were in written form and minimum of three years, while rents were not to reach more than 7 times the land tax of 1949. These landowners used wage-labor to direct exploitation of their lands, and were in most cases evading laws and wage relations (Richards, 1980:305). There was an alliance between officers and small landowners emerging after agrarian reform. They formed an intermediary between regime and villagers (Podeh and Winckler, 2004: 21-22).

⁴⁰In the 1960s, there was conflict between reclamation (horizontal expansion) and vertical expansion (drainage of old land). There was no consensus between Soviet engineers and civil servants of Ministry of Agriculture and Irrigation. Unfavorable soil condition led to high costs for lifting water above 10-20 meters. Only 58-60 percent was cultivated, of 912,000 feddan reclaimed since 1953. Poor management and using state farm models tailored to Soviet were reasons behind failure (Hansen, 1991:155).

When looking at industry before revolution, Egyptian economy developed a national industry during WWII. However, the colony, internal corruption of monarchy, and political parties did not support the effort. Egyptian society was formed by “colonial capitalism”, which favored categories of social class and the state (Beinin, 2008:320). In Egypt, motive behind ISI was boycotting imperial goods of countries that dominated Egypt (Shechter, 2008:574).

The state was responsible for investments in infrastructure and social services. During first four years, the emphasis was on private sector. The Federation of Egyptian Industries demanded low taxes and custom duties on raw materials and high protection through higher tariffs on domestically produced goods. There was tendency for partnership between government and private sector (Ikram, 2006:2). Productivity was to be increased through credit, fertilizers, and less interest at harvest. All were support shapes for land consolidation, private entrepreneurs, and cooperatives to provide mechanization and finally flood control. Large-scale cultivation was used through private ownership of small and medium sized estates, through mechanization, pest control, and land consolidation (Harik, 1984:44-45).

A small industrial sector operated in manufacturing textiles, processed food, and small appliances. About 60 percent of investments were by foreigners. In 1955, iron and steel complex was set in Helwan, and then a cracking blast led to loss of time and money. The location was remote from iron sources; it was based on political considerations. Gradually, some jobs were provided, and imports declined. Economic goals were unrealistic, one reclamation project was to be between Cairo and Alexandria, and loans were negotiated due to shortage of funds bureaucrats (Marsot, 2007:142).

In 1952, ownership of economic sectors was transformed to hands of the government; direct taxes increased and high revenues of SEEs, social services extension, less income inequality, fixed salaries in government. The share of industry in GDP was 20 percent, the army controlled economic and political aspects of life. GDP was estimated to grow at 3.5 percent annually during 1952-1974, and per capita income to rise by 1 percent annually. The government became an equity owner in new industrial firms (Ikram, 2006:7).

In 1954, Production Council was established to evaluate large-scale and capital-intensive industries to which joint private-government ventures were suggested. Sequestered foreign enterprises were banks or businesses in insurance. They were organized under the Economic Organization, a semipublic company, which supervised first industrial five-year plan in 1957. It was believed that industrialization would solve employment problem (Hansen, 1991:122-129).

In 1953, Law No. 430 provided 7 years exemption of profits' taxes, if the firm helped economic development, and five years if the company was already existent, but increased capital. A fund was established to market cotton in and outside. It was compulsory for companies with capital higher than 10,000 EGP to be a member in industrial chambers. The government appointed not less than two directors. The government established permanent council for production to propose and evaluate new projects (Issawi, 1963:53-54). Raw materials were scarce and expensive; lack of adequate transportation, water, poor equipment for mining. Agricultural raw materials were in deficit, and basic ones were not available or of inferior quality (Ikram, 2006:10).

The government adopted welfare policies to realize egalitarianism (Ayubi, 1992:92-94). The parliament was dominated by landowners that controlled peasants. An illiterate rural society was not ready for democracy. The government undertook reforms in education, health, employment, and labor legislation. Daily minimum wage increased from EGP 0.125 to EGP 0.250 in 1953, but came into action in 1960 due to system of fringe benefits. Insurance system financed by employer for industrial workers was introduced to improve their conditions. Moreover, profit sharing was also introduced, 25 percent of net profits were to be shared among employees (Ikram, 2006:10; Owen, 1992:28-30).

2.3.2. The Second Stage (1956-1961)

The High Dam project was one of agricultural investment policies, emphasizing land reclamation and drainage (Richards, 1980:309). It was expected to increase cultivated area from 20 to 25 percent and provide cheap hydroelectric power to industrialize (Mansfield, 1973:679). UK and USA⁴¹ promised to provide USD 70 million supporting the first phase, with later aid from World Bank. Many conditions were tied to this offer. One- third of government revenue was to be allocated to the project. The government could not obtain foreign debt without World Bank approving. However, disbursements were divided into separate phases, and there was Western pressure related to Arab-Israeli dispute. In July 1956, the offer was cancelled (Ikram, 2006:4).

Until 1956, the Suez Canal never affected the economy because of shares owned by France and Britain (Roussilion, 2008:355). The Canal was nationalized in July 26, 1956. Britain blocked Sterling assets, USA blocked dollar assets, while trade was blocked. The Canal started receiving revenue in 1960. Egypt received trade and aid from East⁴². The country fell into foreign exchange shortage. However, competitiveness of manufactures increased between 1945 and 1952, as indicated by IMF (Hansen, 1991:99). Egypt turned into closer relation with Soviets, which provided arms, technical assistance, foreign exchange, and funds. Egypt provided labor and materials, advanced to expect from a developing country (Mansfield, 1973: 681-682).

ISI led to realization of High Dam, building of steel and iron complex at Helwan, adoption of welfare-state policies through expanding civil service and public sector, providing employment to graduates in public sector (Shechter, 2008:574).

⁴¹The role of Egypt in establishing Non Aligned Movement was a convincing factor for USA to cancel its aid for Aswan Dam (Roussilion, 2008:339).

⁴² The vagueness of the regime's political identity was criticized by the West. The Egyptian government opposed joining a military alliance with Europe or USA, and so Egypt purchased weapons from Czech (Roussilion, 2008:339).

There must have been mobilization and incentive systems for landless peasants, to control corruption and ensure adequate performance. However, solutions were limited to social and ideological boundaries not more (Richards, 1980:304). Heavy industry received high priority. The state was not ready to give up social base's standard of living improvements for funding industrialization. The funding was for outsized industries, and agricultural primary products were only imported by socialist bloc (Roussilion, 2008:352-353).

A new Constitution in 1956 defined the framework for private sector's operational scope. British and French assets were sequestrated and managed by State Economic Organization set in 1957. It had full control over foreign banks, commercial agencies, and insurance companies. Half of commercial bank loans were concentrated in seven commercial banks, and 68 percent of insurance business transactions were concentrated in five insurance companies. About 20 percent of labor force was employed and third of aggregate output was solely by industrial sector. The organization turned them into domestically owned joint stock companies within five years. National Planning Committee was established to plan for long-term social and economic development (Ikram, 2006:5).

Nationalization process allowed public ownership for industrial sector, which means employment, wage, projects, and techniques were all based on planning. Employment increased because of less working hours, higher wages, profit sharing, and fringe benefits (Mabro, 1967:331). The government increased its share in national income. It was 35 percent in 1959 and 60 percent in 1962. Capital distribution was more unequal than income (Roussilion, 2008:345). The state was a senior partner with important bourgeoisie groups. Therefore, there was coalition between military and industrial bourgeoisie, which was only limited to economic issues, as political control and decisions are to remain only in military hands (Abdel-Malek, 1964:41).

The Ministry of Industry was established in 1956, and allowed an economic development organ to manage nationalized economic and commercial establishments and infrastructural projects (Roussilion, 2008:345).

In 1957, half of manufacturing output was produced by capital-intensive sectors. Investments were in industries with limited labor substitution for capital. Industrial structure changed between 1952 and 1960; production in paper increased by 145 percent, 100 percent in cement, and 66 percent in oil refining, total output increased by 60 percent (Mabro, 1967:343). In the 1950s, tariffs increased because of protectionism and revenues considerations. Effective protection rates were 100 for tobacco, textiles, and leather products, 20 percent for food and furniture, and negative rates for beverages. There were other measures such as licensing, price controls in order to constraint imports (Hansen, 1991:99). In 1957, Law No. 153 prevented any insurance firm to be established without state permission (Issawi, 1963:57).

The state financed heavy industry, and private sector was to finance light industries. However, no up-to-expectation investments were made by private sector. That is why the 1959 laws made it compulsory for firms to invest 5 percent of profits in state bonds with ceiling of 10 percent dividend to shareholder, of nominal value of share. Misr Bank and National Bank were nationalized in 1960, and they became socialist institutions working on development plans (Kenawy, 2009:589).

Until 1961, private properties of foreigners were nationalized. National Bank⁴³ of Egypt (NBE) was nationalized and was followed by banks and insurance companies (Marsot, 2007:143). National Bank was monopolist of note issuing, lender of last resort and control authority over bank rates; it was rather a Central Bank (Ikram, 2006:6), and as custodian of government's fund. The government controlled Misr Bank due to its importance. It was the first Egyptian company to be nationalized. In 1961, the government took over import and export trade. Progressive tax system was introduced, and individual shareholdings were limited to 10.000 EGP (Mansfield, 1973:681). In 1961, Law 117, 118 and 119 allowed state's direct control over financial apparatus and non-agricultural production means (Roussilion, 2008:345).

⁴³Nationalization of NBE was due to its refusal to comply with program of first five-year plan (Hansen, 1991:114).

Unity with Syria⁴⁴ had negative impact on Egyptian economy (Marsot, 2007:141). Different social and political structure of two societies was clear. Syrian bourgeoisie⁴⁵ were large portion and their effective role could not be underestimated. The military group penetrated the Syrian economy. There was a monopoly in political power, and fears of industrial bourgeoisie against policy of the regime (Abdel-Malek, 1964:41).

Between 1952 and 1973, public infrastructure and social services were areas of focus, while private sector was restricted to agriculture, real estate, and informal economy. SEEs had monopoly over banking, manufacturing, foreign trade, and transportation. This intervention was institutionalized in National Charter of 1962, subsidies were provided for many goods, and employment was guaranteed for those with secondary school diploma (Alissa, 2007:2-3).

Subsidies in Egypt influenced all citizens. They were like wages, which varied to skills and rank. Higher income meant higher subsidy, so those who were better off benefited more. Food subsidies constituted small part and were equally distributed, so major part was to non-food items. Benefits targeted middle and high income groups; the reform should not only focus on reducing subsidies, solving price/wage distortions, as it will face opposition from state and bureaucrats. The state regulated supply and prices of consumer goods, so economic distortions heavily appeared (Harik, 1992:481-482).

The regime offered employment and subsidies, while tried to achieve rapid growth. Lack of sufficient resources hindered both goals. The welfare state was a means through which the state maintained stability. Capital needed for investment was diverted, to meet increased population, increasing at 2.8 percent annually (Rutherford, 2008:135).

⁴⁴When Nasser was invited to unity with Syria, he hesitated due to risks involved. However, he believed it was a first step towards Arab unity (Marsot, 2007:141).

⁴⁵Middle class merchants in Damascus rejected nationalization and preferred an open political order (Rutherford, 2008:132).

2.3.2.1. First Five-Year Industrial Plan (1958)

The 1956 Constitution stated that development must be planned. In 1958, a Five-Year Plan was made and the state provided 60/61 percent of funds in heavy industries. The main condition was to increase net investment from EGP 34 million to EGP 45 million annual averages between 1957 and 1961. Debate revolved around role of foreign investment. Foreign shareholders were granted a majority control in domestic firms (Ikram, 2006:2-5; Mansfield, 1973:680).

The plan focused on four goals: establish basic industry, meet main industrial goods' demand, promote exports, and build regional balance in industry distribution. The period of the plan was based on economic and social development planning. It signaled the national planning start. The plan was initially ten-year plan, but only first plan was applied. Growth was 8.9 percent and 3.5 percent in 1961/1962, because of weather and loss of cotton crop. About 34 percent of investment was directed to industry. However, there was a wide lack of information to indicate degree of competitiveness of Egyptian industry. The plan aimed to double GDP to reach 40 percent by 1965 and national income by 1970 (Issawi, 1963:64-66; Kenawy, 2009:589-590).

The government gave attention to development (Levy, 1986:98). The plan addressed all sectors: investment, exports, imports, consumption, and employment. The state set goals, techniques, and growth rates. About 90 percent of capital formation was provided by state, imposing its priorities on development agenda. Economic planning was on firm basis, which is regulated by the market. There was focus on heavy and strategic industries, but also on consumption patterns, encouraged by the welfare state (Abdel-Malek, 1964:45).

In 1951, numbers employed in public enterprises were 350,000, and in 1965, it reached 1,000,000. Governmental ministries rose from 15 to 29. Third of non-agricultural labor force was employed in government. Moreover, total number of military members in 1955 was 80,000 and rose to 180,000 in 1966 with 90,000 paramilitary police. The government exports as a share in GDP rose from 18.3% in 1954 to 55.7% in 1970 (Owen, 1992:24-25).

In 1961, the productive apparatus of public enterprises was completely defined. Companies with 50 percent shared by the state were divided among 39 sectorial-based “general organizations”, directly supervised by relevant ministries coordinating their activities through a plan. Specialized sectors were responsible for nationalized banks, and external trade was under state control (Roussilion, 2008:345-346).

Private sector was supposed to provide 55 percent of locally funded investment. However, expectations were unrealistic, private sector could not increase savings from EGP 87 million in 1959/60 to EGP 157 million in 1960/61 (Rivlin, 2004:274). ISI was fully defined. There were close ties between large monopolists, and the government, providing concessions, tariff barriers, and subsidies. Globally, ISI was part of national movements in Third World (Shechter, 2008:573-574). A sustained growth was expected in Egypt in the early 1960s (Levy, 1986:98). In 1960, 77 percent of population was potential work force, but only 32.6 percent was actual labor force, concentrated in tertiary sector. There was 21.7 percent in infrastructure, 10.6 percent in commerce, 54.3 percent in agriculture, 10.6 percent in manufacturing. This reflected the limited nature of manufacturing sector because of concentrated ideological, economic, and political power in hands of technocratic bureaucrats (Abdel-Malek, 1964:45).

In terms of internal consistency, there was exaggeration in targets of growth from 4.5 to 7.2 percent in a country with similar conditions. There was underestimation of population growth, means exaggerated national income. Nationalization process led to less efficiency, so capital-output ratio decreased, and capital depreciation was high. The tendency was to make new capital investments rather than efficiently using available capital. The relation between resources and demand was not based on accurate figures. The government attempted to raise savings and achieve social equality through controlling business class and decreasing surplus, but it increased mass consumption. Higher expenditures by government acted in the opposite side. The plan ignored indirect requirements of foreign exchange, caused by increased imports in some sectors. New industries lacked scales of economies, and they produced only for domestic market. Export performance was weak and revenues were not sufficient for paying debts (Rivlin, 2004:274-276; Issawi, 1963:69-71).

There was gap between planning and policymaking. Guaranteed employment led to over-staffed public enterprises and absent efficiency. The plans made were too vague to include such targets without considering actual resources availability (Rivlin, 2004:275). They did not involve deliberate export promotion; domestic demand was only investment criterion in industry. There was ignorance for social profitability (Hansen, 1991:130). Lack of up-to-date information on parameters or input-output ratios led to estimates based on guesswork. Agricultural sector's income through exports was transferred to industrial sector. It was also used for processing industry needs for food industry; through small quantities and low prices, control was over whole consumption of GNI (Kenawy, 2009:590).

The plan lacked procedures of methods by which targets to be realized, and the traditional econometric model relating variables; it neither included updated input-output tables specifying quantity relationships between variables. It rather followed the Soviet Union models of material and labor balances backed by synthetic balances, and equating needs and available resources in key branches. The plan included target of doubled national income in 20 then 10 years. The targets and foreseen plans were set by authorities, armed forces, and planners. Needs for investment and expected output were attempted to align with targets. Many talented economists and statisticians, foreign experts as well helped in linear programming. Capital goods sector should have been developed by planning, but it did not happen, due to sole focus on welfare society (Abdel-Malek, 1964:45; Issawi, 1963:70-73).

The land reform aimed to divert investments towards industry. However, no redistribution occurred. There was a decline of 25 percent in industrial investment declined by 25 percent, from LE 28 million in 1952/53 to LE 23 million in 1953/54 (Rivlin, 2004:274). There was cropping ration and high rural population densities. The concentration on land reclamation had cost highly per reclaimed feddan. Cost was 480-1000 EGP, while estimations were 165 EGP. There was poor soil and low crop yields. There was miscalculation and assumptions that new land is as fertile as old ones. Funds after 1967 were scarce and capital constraint existed. The military bureaucratic mentality was reason for failure; problems of old lands were intractable. Agricultural trade deficit had some elements: domestic demand for rice and wheat increased due to higher percentage of population in cities (Richards, 1980:308).

Expansion of cultivated land was limited by technological capacity to utilize Nile's water. Egypt was an overpopulated country relative to its arable land (Beinin, 2008). The High Dam was built along with construction projects, but construction rather than manufactures could have solved employment problem. Unskilled labor was transferred from rural to urban areas, where 73 percent of industries existed in 1960. It was expected by Lewis that size of agricultural sector would not change, and that more labor could freely shift to industry. However, the population growth was an obstacle to adequate labor reallocation and measurement of absolute labor decline in agricultural sector, only percentage of active labor in each sector was measured (Mabro, 1967:332). The Dam was only significant in electricity and public utilities between 1965 and 1974 (Hansen, 1991:14). Lands were converted to perennial irrigation rather than basin. Other cropped lands had no drainage consumption, because of absent funds and engineers. In 1970/1971, when investments took place in public drains and pumping station, it was inadequate as water supply increased (Richards, 1980:309).

The Dam was expected to increase perennial irrigation and cropping in Upper Egypt that followed basin irrigation, increase rice cultivation, shift maize cultivation from to hot months of June-September, and increase water supply for Western Desert reclamation. However, results were disappointing, due to water logging and overwatering. Although further investments were nominated by Soviet engineers to avoid water rise, they were delayed because of war and foreign exchange shortages (Hansen, 1991:154).

2.3.3. Third Stage (1962-1970): The Era of Socialism

In 1952, 13 percent of GDP and 28 percent of gross capital formation was attributed to public sector. While in 1960, 74 percent of gross investment and 18 percent of GDP was by public sector. Although the socialist character of policy was evident, it was believed that non-ideological base existed. Therefore, it can be stated that 1956 and Suez Canal nationalization was the turning point in economic policy. It was not until 1960, when the five-year plan unleashed the nature of expected economic system (Ikram, 2006:5), and socialist transformation. However, it was a policy of trials and errors rather than a defined ideology (Ayubi, 1992:95-98; Owen, 1992:70).

In 1961 and 1963, the property of wealthy families sequestrated, and the entrepreneurial class was destroyed. All nationalized enterprises were consolidated into one hundred and sixty joint stock companies under control of eleven general organizations. Price controls converted these firms into loss making, instead of profit-loss concept. There were output and productivity targets set for enterprises in parallel, and as metric for efficiency (Hansen, 1991:125-126). Tariff system in 1962 imposed a protectionist quota for firms ensuring ISI: 22 percent on food, 599 percent on steel, and 990 percent on leather. Socialist laws on regulating labor utilization, wages and prices increased unemployment and lowered productivity (Kenawy, 2009:591).

In the 1960s, ISI was in meat and cereals; export promotion in rice and cotton, non-tradable goods were produced. After 1973, domestic demand increased, cotton cultivated areas declined, animal feed, and cereals increased. ISI in agriculture was a production policy rather than an investment (Hansen, 1991:129-130). In August 1963, 228 enterprise was nationalized in industry, transport and mining. There was compensation for shareholders in shape of state bonds with 4 percent interest, and payment in 15 years. In November 1963, 177 companies in internal transport and arms factories, and 6 land companies were nationalized (Abdel-Malek, 1964:42).

In 1966, the main reliance became on supplier credits, increasing annual debt service payments. After war in 1967⁴⁶, import restrictions were used to close foreign exchange gap. There was no plan of enhancing exports' competitiveness. Imports were reduced by 20 percent between 1966 and 1967, increasing unit costs in industry (Ikram, 2006:7). Most resources diverted away from productive investment, and foreign policy prevented the country from loans (Rutherford, 2008:135).

⁴⁶In 1967, with absent air cover and many regiments in Yemen, Egypt fell into Israel's hands that reached Suez Canal's shores, West Bank in Jordan and Golan Heights in Syria. With three-quarters of air force destroyed and 12,000 men killed, Egyptian army lost (Marsot, 2007). Three countries declared cease-fire after USA and Soviet Union intervened, but Israel kept invasion. Israeli troops bombed airbases along continuing operations in Syria and Jordan (Coban, 2007:48-50).

The role of private sector became minor in terms of investments, production, and decision-making. It was argued that “Arab Socialism” was factor behind takeovers. In May 1962, Nasser presented the *National Charter (Al-Mithaq Al-Watany)*. He stated that economic development must not rely on individual efforts, but rather on socialism. The Charter set an outline for economic activity’s provisions. There would be public ownership of economic infrastructure, and majority of heavy and medium industries. Banks and insurance companies are only confined to public sector. Private ownership sphere was constrained to land, construction, and light industry (Ikram, 2006:7-8). In 1962, 1/6 of privately owned land was controlled by ministry of agrarian reform. The government was responsible for agricultural credit and selling to farmers (Kenawy, 2009:590).

Until 1963, in building and landowning sectors, private enterprise was dominant; its share to national income in 1962-1963 budgets was 65.8 percent, with only 34.2 percent done by public sector. In agriculture, private sector’s share was 93.8 percent, 87.5 percent in building, 79.1 percent in commerce, and 56.4 percent in industry (Abdel-Malek, 1964:43). The state imposed its participation by 51 percent in middle-scale economic units’ capital ownership and administration (Abdel-Malek, 1964:41; Roussilion, 1998: 345). Agrarian reform was purely a political agenda. The reform never managed to equalize personal distributions. Between 1964 and 1968 public investment declined by one-third (Ikram, 2006:10-12; Roussilion, 2008:285).

USA provided Egypt with food aid program between 1954 and 1966. Wheat shipments helped maintain internal stability. Egypt fed its labor force by American aid, while industrialized by Soviet aid. In 1965, USA retaliated against sending 40,000 men to Yemen, so it interrupted food program. The interrupted wheat shipments accelerated the financial crisis in Egypt. In 1965-1966, imports of wheat and flour were higher than exports to western markets (Roussilion, 2008:354-355).

After defeat in 1967, Nasser declared building Supreme Control Commission to supervise public sector, but it was only an extra layer to bureaucracy and politicization of public sector (Cooper, 1979:491). Three-quarters of export trade and whole import trade were confined to public sector; the rest was left for private sector. Internal trade was done by private sector; on the condition that public sector receive at least one-quarter of this trade over eight years (Ikram, 2006:7-8).

The state controlled all aspects in the economy except for agriculture and retail trade. After 1967, Nasser shifted the economic policy away from socialism. The policy promised expansion of private sector due to lack of finance, so many joint companies were established, and the state's share was 25 percent of total capital (Ayubi, 1992:95-98; Owen, 1992:70). Foreign debt increased, and about 80 percent of military stock was lost. Private sector was somehow supported to perform some projects. That is why it is argued that open door policy was rooted in Nasser's time and not purely invented by Sadat (Marsot, 2007:150). In 1969, individual ownership of land declined from 200 to 50 feddans. Properties of around four thousand of small elites were sequestered. However, these decrees did not harm mass of people with no land (Marsot, 2007:144).

Nasser abolished parties in 1953; he established series of national allies to guarantee popular representation: Liberal Rally in 1953, National Union in 1956, and Arab Social Union in 1961. Liberation Rally was to be the only legitimate political organization, helping people select representatives and restructure society, through mottos of order and work, national unity, and democracy (Çoban, 2007:46; Owen, 1992:28). Nasser declared cleansing party system. He believed open debate would cause delay for economic and social reform (Rutherford, 2008:131).

The Arab Socialist Union (ASU) emerged after breaking union with Syria. ASU aimed to encourage mass participation, but it was manipulated by its administration, denying its autonomy. It was established to manage political activity and represent all social forces; workers and peasants had 50 percent in committees' seats. There was political and intellectual confusion due to oversimplified definition of new emerging society. The ASU was a guarantor, emphasizing the importance of industrial development, hydraulic imperatives toward centralized management of agriculture, and rationality in managing public affairs (Roussilion, 2008:347; Abdel-Malek, 1964:43; Marsot, 2007:144-145).

Unions and associations had two choices: either to be disbanded or re-shaped according to new regulations and system requirements. These actions created monopolized political sphere in favor of preferred party. The Confederation of Egyptian workers was established along with other groups with compulsory membership. There was control over trade unions and their demands, which could not be demanded by strikes. The social division of citizens into groups and associations aimed at determining which roles were expected from each member through modernization process (Owen, 1992:28).

Socialist Revolution as a term appeared in 1961, because of nationalization waves. It started by nationalizing firms engaged in foreign trade, closing Alexandria cotton futures market, and exclusive right granted to State Cotton Authority to buy cotton. Moreover, takeover of 44 firms in basic industries, banks and insurance companies, expropriation of half of 86 firms' capital, the passage of shareholders' assets in excess of LE 10,000 to public sector. Property of 167 then 500 wealthy Egyptians was sequestered (Ikram, 2006:6-7). It was a version of socialism, based on secularism, and classless corporate society. Nasser prioritized industry in consumer goods to meet domestic demand, provide foreign exchange, and employ labor (Hansen, 1991:115).

Economic aspects of socialism were as follows. First, economic infrastructure should be owned by the state. Second, insurance companies and banks, and industries, small, medium, or heavy should be publicly owned. If private sector existed, it should be supervised by the government. Third, imports and three quarters of exports trade should be publicly owned. Fourth, ownership of land should distinguish between exploiting and non-exploiting ownership (Mansfield, 1973:680).

Socialism was not a question of free choice, but rather due to aspirations of masses and world changes. Socialism was ideal due to political crisis and social discontent. It was Nasser's dependence on Eastern Bloc, which forced him to adopt socialism. Nasser wanted full transformation and needed social and political support. It is believed that socialist components were only a response to challenges faced by the regime. As main concerns were national independence, state building, and mobilization of masses (Çoban, 2007:51-52; Podeh and Winckler, 2004:14-27). Nasser stressed the meaning of socialist measures and set their doctrinal translation of scientific socialism, and political interpretations by establishing ASU (Abdel-Malek, 1964:45; Roussilion, 2008:354).

When the Cold War took place, neutrality was needed to support the economy. Popular support was needed, but the state apparatus had to impose itself on forces of change. As a populist leader, Nasser searched for neutralism or nonalignment. This approach in foreign politics is to locate a route between West and East. Nasser had flexible attitude towards superpowers regardless of different ideologies. For example, during the Cold War he preserved a neutral position to manipulate USA and Soviets (Podeh and Winckler, 2004:27; Abdel-Malek, 1964:45; Roussilion, 2008:354).

Laws had social character: employment allowance, wages, reforms, intervention in setting prices. Public sector developed while private sector was neglected, subordination of agricultural sector, old equipment and inflationist policies, external loans, wrong foreign policy caused failure of Nasser (Kenawy, 2009:590). Socialist components were gradually implemented due to political challenges whether internal or external. There was imitation for Soviet style in building single military revolutionary command, which then formed a Liberation Rally, followed by a National Union. Political control and higher growth were achieved by technical devices (Ayubi, 1992:92-94).

Egyptian development policy gave priority to regional causes and noneconomic developments outside and inside, there was no civil service and economic success was not prioritized (Rivlin, 2004:278). The failure of economic policy may be attributed to vague goals set by the regime, struggling in face of imperialism, feudalism, and exploitative capitalism (Podeh and Winckler, 2004:25). The external focus on foreign affairs delayed adequate economic, social, and political reforms (Mansfield, 1973:678).

There were frequent wars. The Allied operations harmed the economy due to shortage of fertilizers and disrupted crop rotation. Industry somehow benefited from artificial protection and increased demand of Allies. Yemen War (1962/67), Israeli wars (1967/73), caused much harm to the economy: oil fields in Sinai were lost, defense expenditures increased, Canal was closed, inequality and poverty accelerated (Hansen, 1991:253-254). Nasser created a closed economy based on barter trade with East Europe; agricultural exports in return for industrial imports. However, export revenue was not sufficient to pay for imports (Richards and Waterbury, 1990:241-242).

Egypt was one of radical cases of socialism, public ownership, wealth redistribution, and ISI. The Soviets promoted industrialization in Egypt as it looked forward to reorienting trade away from West (Waterbury, 1999:333). There was paradox in economic ideology; capitalism and private sector existed aside by socialism and state-led economy. Participation was mainly by small group of bureaucrats rather than masses of people. Regardless of all mistakes surrounding Nasser's regime, he established welfare state in Egypt and attempted to support peasants and workers (Marsot, 2007:154-155). Nasser erected a soft state, in which economic issues did not receive enough priority. He maintained basic consumption levels to avoid imposing burdens on citizens (Podeh and Winckler, 2004: 21-22).

It was believed that capitalism would only strengthen political power of class that owned resources. However, if it was the case, it meant capitalism existed rather than socialism, in terms of society dominated by certain class, or negation of class struggle. Socialism rejected exploitation; it aimed to create economic equilibrium among citizens to have justice and equality in opportunities for preserving national unity. In order for a country to take-off into sustained growth and control any internal conflicts, masses should be politically mobilized. The state attempted to serve and satisfy influential groups differently (Podeh and Winckler, 2004:24-27; Roussilion, 2008:333).

Since 1952, individual value norm and liberal social order diminished. Politics was no more voluntary exchange: political parties were banned, organized interest groups and professional syndicates were destroyed, and patron-client system was established. Nationalization, sequestration, and land reform destroyed any possible opponents. Nationalization destroyed entrepreneurial class and powerful families (Hansen, 1991:249-250). The regime did not share power with other parties due to its power. Socialism in Egypt was a mixture of etatism and welfare policies (Ayubi, 1992: 98).

Subsidies⁴⁷ were a way of supporting consumers through price controls. Welfare-oriented policies aimed at equity in income and wealth. The state provided means to mobilize masses through income distribution and supporting economically dependent citizens. Subsidies were monetary policy to adjust price and wage levels, and were an administrative means used by policy makers in solving economic problem (Harik, 1992:481; Levy, 1986: 98).

Nasser followed socialism⁴⁸ with efforts towards solidarity. Nasser believed he could imitate Atatürk's efforts in building a harmonized society. Socialism was embodied in the community to remove class conflicts caused by class inequalities (Richards and Waterbury, 1990:197). The government followed aggressively developmental investment policy, a populist consumption policy to improve living standards. The state was provider of last resort (Cooper, 1979:482).

It is believed by some that "socialist" or "revolutionary" regimes were mixture of etatism and welfare policies. When described as socialist, it was satisfying domestic elites. In Egypt, socialism was a political attempt for national independence. Therefore, Nasser adopted socialism and tight planned economy (Podeh and Winckler, 2004:5-6). The crisis in Egypt was of corporatism and populism rather than socialism. This means emerging new needs of entrepreneurs and capital owners aspiring at credits and facilities to undertake their investments, so a hegemonic crisis occurs as no single group can dominate, coalitions appear but no single coalition dominates (Ayubi, 1992:97). Socialist regimes attempted to achieve income equal distribution, but land ownership and rural incomes were unequal (Gemmell, 1985: 57-58).

⁴⁷ Subsidy defines support of the price, in which portion of cost is borne by another part than the recipient. It is the state; it subsidizes production inputs, services, and goods. The direct cost can be borne by either the government, or private producers (Harik, 1992:482).

⁴⁸ Socialism is an ideology considering the state as main agent responsible for economic planning and management, allocating resources and setting priorities for the economy. There is structure of institutional practices result from socialism. However, socialism never declared the state as producer. According to Marx, socialism means feathered away state through retained harmony between forces and relations of production (Ayubi, 1992: 89).

Table 2 shows that total savings increased from 8 percent to 12 percent, from 1950 to 1970, total consumption declined from 88 percent to 76, and total investments increased from 13 percent to 18 percent. Consumption, although declined, it was small decline due to subsidies provided. During 1950s, nationalization provided employment opportunities and accumulated profits for investments, in projects. In 1950s and 1960s, private enterprise was weak to increase savings or investments (Podeh and Winckler, 2004: 258).

Table 2. Shares of Consumption, Savings, and Investment in Egypt's GDP, 1950, and 1970

Structure of GDP (%)	1950	1970
Share of total consumption	88	76
Share of total savings	8	12
Share of total investment	13	18

Source: Podeh and Winckler, (2004: 258).

Social and economic policy measures were suspended⁴⁹, production, quantity, and quality of services declined (Roussilion, 2008:354-355). Nasser sacrificed growth for military. Private consumption did not decline, but investment was sacrificed (Hansen, 1991: 453). The Revolutionary Command Council had no ideology, philosophy, or political program. There was no clear view of the society they were willing to form. There was only frustration with monarchy corruption and the inability to eliminate British colony. Egypt witnessed many economic systems, which were never based on clear philosophy (Rutherford, 2008:131; Ikram, 2006:1-2).

During Nasser's time, policy measures were only a reorganization of interests led by political motives. In order to create a modern state, economic and scientific management were necessary means, along with valuing work and human capital, distribution of individual incentives (Cooper, 1979:492).

⁴⁹ Nasser faced external constraints related to Palestine and Zionist entity, and internal constraints of increased military expenditures. Egyptians were asked to bear military expenditures if they did not want capitulation to Israel (Roussilion, 2008:354-355).

There was accumulation of unfinished projects, little consideration for economic profitability, ignorance of project evaluation and economies of scale and exporting sector, focus on consumer goods, planning was handed over to foreigners, unrealistic prices, and cost estimates were set (Hansen, 1991:127). Egypt had one untapped resource, which was the desert. It shaped 95 percent of the country. Cheap electricity from Qattara depression could have been used to lift water. Methods of distil sea water by harnessing solar energy was successful in many countries; it was experienced in Egypt in 1962 (Marsot, 2007:167; Issawi, 1963: 129-130).

Egypt has a unique position when it comes to agriculture. Within a century, Egypt witnessed four stages: introduction of cotton and irrigation by canals, expansion of cotton cultivation during American Civil War, and British undertaking irrigation works. Although Egypt had a sophisticated system of irrigation and labor-intensive production, it had cotton dependency, unequal property distribution, small-scale farming, and large number of intermediaries. Drains were present, but needed deepening and pumps. When schemes for agriculture and flood control were applied, they were designed outside Egypt. Therefore, the country faced high outlay of foreign exchange and could not generate hydro-electricity. The country kept letting floodwater into the sea, so it lost 30 million of river 80 million cubic meters (Issawi, 1963:34-37).

The contribution of one sector to GDP growth depends on its relative size and growth rate. Agriculture had contributed insignificantly to total growth after WWII. It grew at 22 percent between 1952/1953 and 1959/1960, and then it declined to 8 percent between 1974 and 1981/1982. During 1960s, three-quarters of agricultural investments were to reclaim Western Desert. Unfortunately, less than two-thirds of this land was cultivated, with marginal returns. The lack of adequate land settlement policies led to unexpected results. The mechanical approach and lack of knowledge led to failure (Hansen, 1991:121).

Poor groups did not benefit from nationalization. Landless and poor people did not benefit in direct way, but they had improved standards of living (Levy, 1986: 99). State-led growth and planning lasted for nearly ten years. The planning concept was a tool of scientific management practices, production for local market was to increase, high protection and prompted certain industries by the state, planning had no consideration for cost and price, or to which criteria did the state decide industries to promote (Owen, 1992:232). Although Egypt had industries with natural advantages such as domestic supply of raw materials, these industries had low domestic cost and were competitive until nationalization started. However, textiles were not competitive, because high quality cotton textiles were not suitable for domestic market (Hansen, 1991:163).

Agriculture deteriorated, because of rising subsoil water caused by High Dam, which did not allow for replacement of silt. Expensive fertilizers were not afforded by farmers. The abolishment of silt harmed fishing industry in delta. On the other side, fishing industry in High Dam and Lake Nasser satisfied domestic needs, and was expected to set up canning and fishing factories. Another opportunity was a system of agriculture around Lake Nasser due to subtropical climate resulting from evaporation. However, due to lack of funds it was not done. Increased moisture harmed archeological sites due to destroyed stones. The cultivation in Nile River was always limited due to topography and available water, even after High Dam was built, no much variation in cultivated area existed (Marsot, 2007:167; Issawi, 1963: 129-130).

Excess labor was to work in industry and service sectors, which would improve labor absorption in industry. The fact is underemployment only shifted among sectors and areas, due to population growth. Labor wages in industry increased due to economic and non-economic factors: government intervention and labor union pressures (Mabro, 1967:331). Private consumption and growth expenditures were kept low, according to limits determined by balance of payment deficit and national output (Levy, 1986:100). The revolution achieved success in industrialization, heavy and light manufactured goods were developed, and industrial workers received many privileges, while farmers benefited from extended social services (Mansfield, 1973:680).

Employment opportunities were expected to increase, but no effective timely measures were taken against population growth. Rural progress was slow; cooperatives did not succeed as expected, no active political participation or freedom (Harik, 1984:45). Low-paying occupations such as agriculture had a declining labor force portion, while manufacturing and public sector had increased labor proportions (Levy, 1986:100).

The state depended on distributive consumptive economic policy; it did not have independent political power due to conflicting interests and politically weak state. The state did not manage economic interests inside the state. Nasser's government never considered consumption contraction or temporary stabilization, not to be faced with political choice between constituencies of the regime (Cooper, 1979:483).

The cutting into private sector was so extreme in Egypt (Roussilion, 2008:345). In Egypt, socialism was based on political and institutional considerations (Ayubi, 1992:92-94). Terms of trade, surplus in agricultural sector was absorbed by government, taxes, control over exports, selling high and buying cheap, planting according to rotation system, a means of exploiting farmers when trading crops based on government-determined rates. Land reform was highly beneficial to agricultural system, inflow of personnel, infrastructure, services, and goods to rural areas. It was difficult to extend agricultural land, urban growth, brick making, new cities, and industrial sites (Harik, 1984:51).

To summarize, from 1952 until 1973, the economic structure exhibited the following features: The state controlled agriculture through cooperatives, which were responsible for selling inputs and buying crops. The private sector operated in small-scale industry and wholesale trade. The government had some partnerships with foreign oil firms in petroleum. Price and cost controls started during WWII, expanded in the 1960s, and affected all sectors of the economy, such as housing and industry. The goal was better income distribution and resource mobilization. Price controls were used to reduce cost of living, but they were also a means to increase consumption through subsidies (Harik, 1992:481).

2.4. OPEN DOOR POLICY (*INFITAH*) (1973-1980)

Anwar Al Sadat began his era⁵⁰ with “Corrective Revolution”. He dissolved power centers to recover state institutions and abolish Nasserism. In 1973, Sadat reshaped Egypt through breaking its past. It became new country in areas like political parties, peace with Israel, and Open Door policy (*Infitah*). War conditions and investments for military, equipment, stagnated factories in Suez Canal area and losses due to its blockage increased (Kenawy, 2009:592; Roussilion, 2008: 359).

Impetus behind *Infitah* was the slowdown of economy. In 1973, growth rate declined by 3 percent. A 9.8 percent fall in value-added in mining sector, 15 percent fall in construction. In 1973, civilian labor force was 10 million, 89 percent of which was employed. There was underemployment in urban areas in services sector. This was accentuated by immigration of labor to cities. Guaranteed employment in government sector defused the unemployment problem (Ikram, 2006:13).

The Constitution⁵¹ in 1971 was of Arab Republic of Egypt. There was 50 percent membership quota for farmers and workers in electoral positions. ASU adopted multiparty system that would not harm 1952 Revolution’s gains. The transformation into pluralist political structure allowed for tight control over institutions. No laws were issued to prevent government intervention in electoral process. Therefore, ministry of interior and government officials supervised the process. In 1977, a new Parties Law was introduced and mentioned that new parties cannot be based on religion, class, and geographical basis (Roussilion, 2008:343-368; Owen, 1992:136).

⁵⁰Sadat's legacy started in 1973 after he won war, and regained eastern bank of the Canal. Sadat became "Hero of the Crossing." Therefore, he freely set his policies (Kenawy, 2009:592; Roussilion, 2008: 359).

⁵¹Law was originated solely from Shari’a and the president’s designation to be confirmed by People’s assembly. The Muslim Brothers supporters were freed and allowed to created Islamic associations, hoping they will defeat Nasserism and Marxism left (Roussilion, 2008:343-368).

The army was no more a threat to political system. There was sort of sacred goal⁵² regarding unanimity. In 1967, inadequate arms Egypt received were cause of defeat. Internationally, Soviets helped Egypt rebuild its army⁵³. However, *Infitah* cancelled alliance with Soviets. Egypt was again dependant, but on West. There was no willingness from Soviets to confront USA in the Near East. Internally, there was budget deficit, currency shortage, lack of raw materials, lack of machinery and factories performing at third of their capacity (Owen, 1992:64; Roussilion, 2008:360-361).

A new economic policy was chosen to cope up with changing conditions: *Infitah* was introduced in 1974 in *October White Paper* presented to People's Assembly. The approach showed outline of policy redirections in economic and political systems. Egypt would adopt an "outward looking" policy to obtain foreign aid. The public sector would remain a main body, through undertaking major projects and assisting foreign and domestic investors. Private sector would be a productive agent, receiving stability to maximize performance (Ikram, 2006:17).

Al Sadat believed the problem was not structural, but rather short-term fiscal fall, so the solution was capital accumulation. Reforms were a technique to leverage easy inflows of funds, eliminating the need for structural reform. Subsidies were 2 percent in 1971, and 13 percent in 1980. Bureaucracy was 1.2 million employees in 1970 and 1.9 million in 1978 (Rutherford, 2008:135-136). He initiated a weak structure based on external funding, remittances, oil revenues; the productive capacity of Egypt did not increase (Adams, 2000:264). During *Infitah*, constraints on foreign exchange were loosed, new funds were available, and there were no pressures for public reform or structural changes (Ikram, 2006: 26-27).

⁵²Sadat believed Egyptian blood was enough shed by Arab cause. Therefore, he gave up United Arab Republic (Owen, 1992: 64; Roussilion, 2008:360).

⁵³ Egypt had its first agreement with Soviets in 1948 and France. In 1973, there was 100 percent of trade with Soviets and Eastern Europe. The shift occurred in late 1970s to West, because of international and military constraints (Hansen, 1991:144).

Infitah ensured a leading public sector, monopoly over infrastructure, (Kenawy, 2009:593). Egyptian economy was characterized by high population growth, low GDP growth, stagnation, deficits in balance of payments, high consumption, low domestic savings, high imports and structural problems, price distortions, production inefficiencies, and absence of adequate policies. However, the passive concentration on traditional hardships was main reason Egypt failed to recognize its transformation and future challenges (Choucri and Eckaus, 1979:783). The main principles of *Infitah* were trade liberalization, privatization, devaluation of exchange rates, reorganization of banking sector, and raising prices of public goods such as fuel and electricity. It aimed to attract capital, maintain leadership of public sector, and provide incentives to foreign investors, and flexible pricing (Kenawy, 2009:592; Roussilion, 2008:359-365; Richards and Waterbury, 1990:241; Owen, 1992:116).

The government promised a large-scale privatization of SEEs. However, it feared job losses. There was no totally transferred ownership of stocks (Gray, 1998:100). The state reformed public sector through fixing prices at below cost levels, to create balance between exports and revenues. There was surplus of labor in SEEs due to absent new investments (Mabro, 1967:343). Sadat believed *Infitah* would allow private sector to expand, while public sector would support other projects. The plan for 1976-1980 set priorities to a modern industry, labor-intensive and high value agriculture, development of tourism, oil, and energy (Hansen, 1991:116). Between 1970 and 1971, it was a training period considering social, cultural, and legal aspects. Between 1974 and 1981, there was an application period and realization of changes. Consolidation of public sector, reduced bureaucracy, less government control, abolishment of certain institutions, new directions for ministries, private sector expanded through facilities, such as tax exemptions (Kenawy, 2009:593).

The composition and origin of rent changed after mid-1970s: rent, oil, tourism, migrant remittances, and Suez Canal were main revenue sources serving debt and subsidies. In 1974, system of “import without cash transfer” was established and allowed appropriation of rent within black markets informally, so foreign currency was no longer obtained through official banking channels (Roussilion, 2008:377-378; Gray, 1998:91-93). The import policy allowed importation for personal uses, and there was follow up through foreign exchange policies (Mabro, 1967:343).

Liberal attitudes towards foreign capital were reflected by laws allowing foreign capital with majority of shares control over firms. Law on mining and quarrying granted new concessions to foreign petrol companies and extensions. The aim was to increase USA aids. In 1974, Law 43 on foreign and Arab investment was voted by parliament. It prioritized sectors for investment and privileges to investors. It included profit repatriation, tax exemptions between five and eight years, and customs exemptions on machinery. Public sector monopoly was no more allowed, foreign banks were able to operate, joint ventures were established between public sector and foreign firms, but were considered part of private sector. This type of association was preferred; it generated revenue increases, improved working conditions, and rationalized production. Sequestration was put to an end, and property returned to many original owners (Shechter, 2008:571; Roussilion, 2008:360-361).

Law No. 43 allowed tax concessions to foreign private firms, exemptions from labor laws, import/export licenses, exchange rates controls, and distinction of foreign companies in free zones, such as Free Zone at Port Said. Luxury goods were heavily imported, so domestic goods were not demanded. Egypt suffered from large idle capacity in inefficient public sector. Short-term credits and international borrowing increased commercial interest rates and wheat imports from USA (Alissa, 2007:3; Richards and Waterbury, 1990:241). There was capacity underutilization of 14 percent in 1973 and reached 32 percent in 1974 (Ikram, 2006: 17).

Economic liberalization increased demand for high-income elasticity goods. Cotton output decreased because of corrupted cooperatives and selective price controls. Crop yields declined due to drainage and lack of animal food. There should have been a shift to high value crops such as vegetables to use land efficiently and increase employment. Problems of infrastructure prevented large-scale production (Richards, 1980:312). Tourism was major sector privatized, the state recapitalized public property for benefit of private interests; dividend on resources such as land, raw materials or public finance were partially or totally given up by the state to support private sector. Large public enterprises operating in foodstuff were also privatized to benefit from increased prices. Egypt had always a centralized state, which did not identify intermediaries, which can help it maintain global control over collectivities or public order (Roussilion, 2008:377-378; Gray, 1998:91-93).

In 1973, consumer price index (CPI) increased by 7 percent. The reaction of the government was to adopt a "two-tier" price scheme for some goods such as sugar. However, local prices stabilization costs increased. A total trading loss of \$228 million was registered by General Authority for Supply Commodities. This was over eight times amount of loss in 1972, which was \$28 million. In 1974, CPI increased by 10 percent, owing to increase in price of livestock goods. There was official reported understated inflation, which was estimated to be between 20-25 percent in 1974 (Ikram, 2006:14).

Subsidy system caused trading loss amounted to 29 percent of current expenditures, which totaled \$ 1.26 billion. In 1974, the government borrowed from abroad and from local banks, it was about 12 percent and 48 percent of overall deficit. Pension funds and social insurance financed remaining amount. Money supply increased by 29 percent while real GDP increased only by 4 percent. The inflationary pressures affected wages, which increased without parallel increase in output. In 1974, there was an increased price of import foodstuff, weak Western demand for Egyptian exports and slow foreign aid. Goods trade deficit was \$1.75 billion, while exports slowly increased to \$ 1.67 billion (Ikram, 2006: 15-16).

The output by private sector was one-third of the public sector in 1970. In 1976, the ratio was 43%; reflecting a declining private industrial output. Heavy industries were controlled by public sector, but industrial production of private sector slowly increased. The private sector in Egypt was always a complementary assistant or residual sector for public sector, it got excess inputs remaining after public sector had met its needs (Choucri and Eckaus, 1979:787; Richards and Waterbury, 1990:242). Share of public sector in industrial production in 1979 was 68 percent; it declined to 37.1 percent in 1981. After *Infitah*, public sector still owned large percentage of manufacturing industries around 60 percent, construction, transportation and banking sectors (Ayubi, 1992:95).

The peace treaty with Israel was on hopes that Marshall Plan would be offered by USA. American aids started, because Egypt was important to its national interests. Since 1979, \$ 1 billion in civilian aid and military credit were compensation for lost relation to Arabs. USA helped the country build its infrastructure. USAID mission included many experts and advisors. American wheat ships constituted 27 percent of annual consumption in 1980. Frozen relation with Arabs destroyed the main goal of *Infitah*. Western and Japanese technology imports did not support productive capacity; they were for long-repressed consumption wants (Roussilion, 2008:362-365). Exports to OECD⁵⁴ countries of merchandise became 53 percent, after it was 28 percent in 1965. Exports to Eastern Bloc declined from 38 percent in 1965 to 7 percent in 1985 (Richards and Waterbury, 1990:241).

There were structural rigidities in the economy, exports were stagnant, and ISI was still major development strategy (Kuntay, 2014:12-15). During Nasser's era, private sector was small; eradication of foreign capital and nationalization created a relatively closed economy. *Infitah* aimed at more incorporation of Egypt in global economy and attraction of foreign investments (Gray, 1998:94). Through 1970s, public sector had growth rates of 10 percent; total factor productivity of labor increased through increased capital to worker ratio. Egypt became West oriented in its foreign trade. There were structural changes in national policy reflecting more openness to private sector. There was no consideration for implications of economic restructuring. New policies meant new allocation and ownership trends over resources (Choucri and Eckaus, 1979:787; Richards and Waterbury, 1990:242).

High revenues from oil exports were used as price supports for peasants and subsidies. Consumption of meat and poultry increased. The government supported domestic meat industry, which needed feed grains and protein meals imported. After oil crisis, the food consumption rates did not decline (Ateş *et al*, 2005: 256).

⁵⁴In 1976-1977, the Gulf Organization for the Development of Egypt (GODE) by Saudi Arabia, Kuwait, Qatar, and Abu Dhabi offered grants for paying off short-term debts and allow free importation of intermediate goods (Ikram, 2006:17).

Agriculture did not receive much priority in investments, the average investment was 14 percent compared to 18-20 percent in later 1960s. Real wages declined, daily wages in agricultural sector were affected by supply and demand in the free market system (Ikram, 2006:17; Adams, 2000:264).

After 1974, private investment increased, and represented one-quarter of investments, with half of capital is foreign (Hansen, 1991:148-149). Domestic saving rates increased to 8.5 percent, and investments rose to 35 percent in 1974. Foreign debt in 1974 was \$ 3 billion; liberalized imports created a balance of payment deficit of \$ 1.2 billion. There was lack of sufficient investments in non-tradable nELGected goods such as housing. In government, wages were based on seniority and accordingly they increase (Richards and Waterbury, 1990: 242; Adams, 2000:264).

Economic liberalization gives opportunity for political and social groups to emerge and impose their demands (Choucri and Eckaus, 1979:787; Richards and Waterbury, 1990:242). During *Infitah*, new rich groups appeared due to trade with oil-exporting countries and Europe (Shechter, 2008:571). Although *Infitah* removed the dominant patron-client system, old families returned into scene and connections remained an important aspect (Hansen, 1991:31). State bourgeoisie were in high positions in public sector. They benefited from comparative advantage they enjoyed by accessing informal decision-making channels in governmental service sector and ministries (Roussilion, 2008:377-378; Gray, 1998:91-93).

Social dissatisfaction increased, and negative aspects of *Infitah* were unleashed. *Infitah* was thought to destroy local industry, due to foreign pressures and loss of autonomy. It was argued that national capital funds should stimulate domestic industry, and that capital was wasteful due to its allocation in consumption sector (Shechter, 2008:572). There were fake promises about freedom. Political parties opposing the regime were closed. Assembly only agreed to government's decisions or opposed in ways preferred by Sadat (Marsot, 2007:162-163).

Black market⁵⁵ existed and benefits went only to the rich. The announced decline in subsidies and return to real pricing was expected to deteriorate living standards, and increase prices from 15 to 45 percent. After three days of social unrest, the decision was cancelled, and 10 percent increase in salaries and pensions was promised. Hunger revolt was one of governmental fears in Egyptian society (Roussilion, 2008:362-365; Owen, 1992:116).

The effect of reforms on losers and winners is a matter of stronger side affecting politics, and is always about winners, such as public sector managers and trade unions were against liberalization. However, they had little impact on policymaking process. The losers were not strong enough to oppose the government (Gray, 1998:106). There was a 50 percent debt relief along with social fund to facilitate reform (Hinnebusch, 1993:159-160). Egypt was indebted to Western financial institutions. Exports of petrochemicals, food imports, and technology were needed to industrialize. Although Egypt was not an oil-exporting country, it depended on oil-producing ones through labor remittances, grants, and cheap oil supply (Ateş *et al*, 2005: 254).

Decision-making was based on interaction among government, bilateral donors, and multilateral agencies. According to IMF, worst three points were lack of sufficient qualified officials to policy, due to long period of socialism, lack of coordination among ministries, and lack of economic proactive strategy. The external aid was accelerated from Arab countries, USA, and Japan, which offered economic assistance programs. Total disbursement of official grants and loans in 1981 was \$1,602 million. The government did not plan for effective use of resources (Ikram, 2006:26).

Although the first response to a crisis is reforming established arrangements to increase efficiency in SEEs, policy makers lacked the experience on market economy. IMF provided analytical support, although caution existed due to lack of understanding of local economy, and unrealistic expectations about reforms. IFIs blamed Egyptian authorities for not following policies. Protectionist ISI measures might be partially dismantled as well. Initial reform efforts in Egypt were not successful in enhancing economic efficiency or defusing the crisis (Ikram, 2006:26; Waterbury, 1993: 26).

⁵⁵Underground economy was generating about \$ 2.1 billion in 1980 (Adams, 2000:264).

There was a need to distinguish separate actors such as state, private sector, foreign capital so that attention can be tailored to sectors individually, but the assumption was a consolidation among them (Ayubi, 1992:100). Clearly, Egypt was forced into reform under pressures of USA and Western world. However, the reform package was untailored to domestic conditions and needs. The package gave priority to foreign investors and creditors rather than domestic labor or economies. This in turn led to stagflation and deindustrialization. The package did not consider backward or forward linkages between public and private sector. Private sector was not capable of financing strategic industries due to its shallow role in economic sphere. Therefore, competitive markets and factor mobility assumptions were unrealistic (Hinnebusch, 1993:160-162).

IMF reform in Egypt was a clear failure. The reform was due to external pressures. There are very rich people, who used the deregulation process to their ultimate benefit, while others remained impoverished, 25 percent of active population was unemployed. Egypt became a rentier economy, and activities were reoriented by external finance injection. Egypt should have designed its own plan, based on its priorities such as reducing poverty and unemployment; GDP growth targets were to be set. Subsidy cutting was expected to affect poor families. Therefore, the country should have developed its own proposal and through negotiations with IMF, a compromise would have been reached. However, lack of time prevented this. The fact that IMF was a western body meant that public might not support Sadat in his policy direction (Ikram, 2006: 27).

Political motives shaped economic reforms in Egypt, which has limited democratization that created political institutions through which interests are incorporated within policymaking process to generated public consent on shared costs of reform. Sadat's Open Policy created a rich class rejecting to have high tax burden, therefore the state relied on oil revenues and remittances to cover deficits in budget (Hinnebusch, 1993:159-160).

There was lack of consensus on meaning and ramifications of reform among major stakeholders. Egypt was in need for adequate investments in building dynamic and efficient institutions in public and private sector, civil society and coordinate reform in economic and social areas. Transparent institutions are important for maintaining long-term economic growth and promoting equality and productivity, emphasizing social contract between state, private sector and the civil society (Alissa, 2007:1-2).

It was expected that some shocks occur before things improve. There was an issue of how to incur least policy changes, while getting maximum loans. Egypt was in actual need for funds to close budget gap. It was expected that less reliance on external funds would result due to less expected deficit, and finally the country was in need for credibility criteria to attract investments (Ikram, 2006:26-27). *Infitah* negatively affected national self-reliance. Any difficulties were expected to cease through more opening to stimulate freedom and stability in new capitalist economy. It was a break up point between state and citizens (Shechter, 2008:574).

Egypt was a gas exporter since 1976. It had phosphate rocks for its needs, and low-quality iron. The focus on oil shifted the focus away from long-term problems (Hansen, 1991: 22-41). Oil boomed prices along with peace treaty with Israel, transit revenues from Suez Canal, and remittances generated much revenue for the Egyptian economy (Roussilion, 2008:362-365; Owen, 1992:116). The Dutch Disease was caused by increased oil revenues and inflows of foreign exchange (Richards and Waterbury, 1990: 241-242; Adams, 2000:264 (Hansen, 1991: 22).

To conclude, there were six characteristics of Egyptian system during 1970s. There was large migration of workers to Arab countries, understated growth rates, an emerging private sector that necessitated further liberalization, wider scope for welfare policy ensuring distributive equity, conflicting opinions for and against open policy, and finally appearance of political groups gaining public attention but do not have political power (Choucri and Eckaus, 1979:784).

2.5. Hosny Mubarak: A New Reform Era (1980s)

Budget deficit, BOP deficit, and external debt were problems during 1980s. Currency revenues declined due to international loans, weak financial market, bad economic relations due to high taxes, and price controls (Kenawy, 2009:594). Mubarak⁵⁶ faced the mess remaining from Nasser and Sadat contradictory regimes. The public sector was major agent in economic life along with debts and deficits resulting from *Infitah* that did not generate expected investments (Hinnebusch, 1993:159-160). The government attempted to control imports and consumerism trends, empower investments, and generate employment. The solution was taxation to generate revenues, but only bureaucrats were capable of paying taxes. However, it was unclear which strategy should be followed, whether total free-market economy or keeping welfare state (Marsot, 2007:170-174). By 1980s, Egypt was not able to continue ISI or to achieve *Infitah* adequately (Shechter, 2008:572). The economy was lost in between socialism and capitalism. Resource distribution, social basis of the regime, and class structure prevented either system from taking over (Richards, 1980:303).

Years were needed for rooted structural change in public sector and distorted incentive system. The ultimate focus has always been on domestic demand. Mubarak allowed the military an economic role, which had association with businesses both domestic and foreign, and oppressive measures were lessened (Hansen, 1991:252). Law on investment in 1981 led to 2.6 percent average growth from domestic private capital and 4 percent of foreign capital in 1983 until 1987. However, two-thirds of shares were owned by state. The modest role of private sector was due to lack of monetary policy changes, overvalued currency, negative impact on exports, negative interest rates, decline in foreign currency income, and speculations among sectors. The open door never managed to be a real reform (Kenawy, 2009:593). As reported by the World Bank, the economy was in stagnation, although the Ministry of Planning reported annual growth of 3 percent in real income per capita, for 1981/1982 and 1986/1987 (Hansen, 1991:5).

⁵⁶ Mubarak was a vice-president of Sadat, and before that, he was air-force officer during Nasser's time. Mubarak had a good reputation in integrity and efficiency (Marsot, 2007:170).

Egypt became dependent on foreign resources and aids, devoted to meet consumption subsidies. Investment proposals were not up to expectation. Sixty-six projects were registered. Total capital amounted to EGP 36 million and 3,450 employees. Investments were concentrated in tourism, banking, and investment firms. Participation of the West was needed in political and economic terms. Subsidies on consumer goods increased to face inflation, but led to budget deficits, 33.6 percent of current expenditures were on subsidies (Roussilion, 2008:362; Richards and Waterbury, 1990:241).

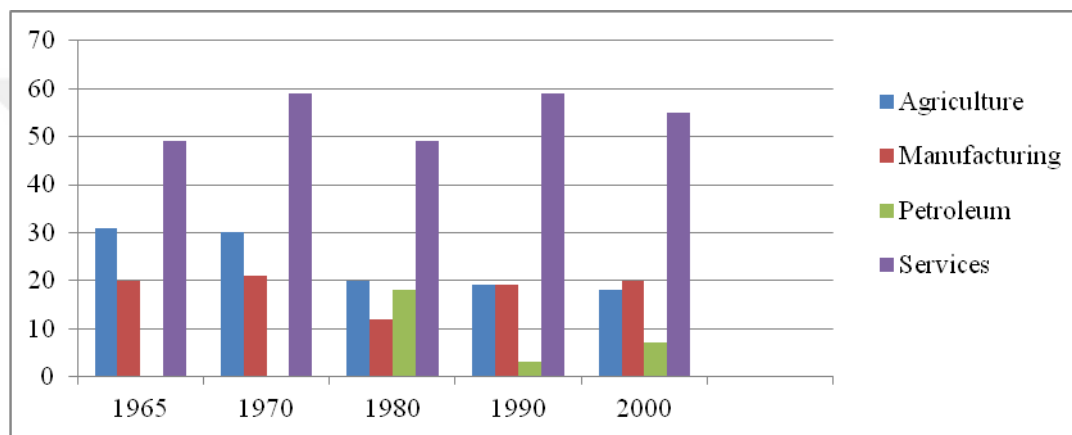
The import sector increased, and manufacturing sector declined. This signals the weakness in Egypt's economic structure. Secondly, the increased consumption shares in GNI, which reached 91 percent from 1952 to 1986 (Hansen, 1991: 22). Mubarak slowed down the pace of reform due to social, economic, and political conditions (Kuntay, 2014: 12-15). In the mid-1980s, oil prices dropped and import capacity declined by 12 percent. Gulf had lower demand for Egyptian labor, unemployment increased, and terrorism incidents lowered tourism revenues. Therefore, borrowing was the solution (Rutherford, 2008:136). In 1980s, reforms aimed at privatization and reducing role of the government. The relative failure of privatization in Egypt was one reason for slow development in labor productivity and slow process of selling government's firms (Adams, 2000:269).

Egypt increased consumption without a parallel increase in productive capacity. Egypt was in need for Arab⁵⁷ market, to which it used to export 80 percent of total exports. Arab countries depended on Egyptian labor and expertise in many professionals (Marsot, 2007:162-163). The increase in private consumption between 1981/1982 and 1986/1987 was politically motivated, through investment that was sacrificed. The trade and finance sector increased in share of GDP. It was 9.5 percent in 1955 to 20.1 percent in 1983 (Hansen, 1991: 19).

⁵⁷Egypt is only alive with support of Arab world, otherwise it would be only overpopulated and poor. That is why Mubarak attempted winning Arab side, which was always in need for leadership and political guidance (Hansen, 1991: 19).

Budget deficit was around 15-20 percent on average in 1980s. In 1976, total debt was \$ 10 billion, \$ 17 billion in 1981 and \$ 40 billion in 1987. The IMF granted drawing rights of \$ 325 million with conditionality, subsidies to be eliminated, agricultural prices liberalized, price of electricity and petroleum-derived products to increase. Reforms were not undertaken by the government, it was only letter of intent signed by the government, and unimplemented recommendations. Egypt was indebted to USA with \$ 600 million of military weapons (Rutherford, 2008:138).

Figure 1. Structure of Egypt' GDP, 1965-2000 (percent)



Source: Ikram, (2006: 88).

Figure 1 shows structure of GDP, starting by 1965. It shows that in 1965, service sector had largest share of GDP, around 50 percent, manufacturing represented 20 percent, and agriculture 30 percent. In 1970, percentages did not witness change. In 1980, petroleum appeared as share of GDP, agriculture and manufacturing declined, while services increased significantly to 60 percent (Ikram, 2006: 88-89). Agriculture amounted for 35 percent of GDP in 1954; half of labor force was working in agriculture (El-Kammash, 1968: 20-25). Roadwork and construction in the Canal did not require skilled labor. Construction was the largest sector in 1960s (Levy, 1986:100).

2.6. Implications and Conclusion

To this end, Egyptian economic and political spheres were analyzed. External forces were against Egyptian will of national independence and economic freedom. Since Muhammad Ali, French-British coalition forced the abortion of state-led growth and adoption of free trade (Shechter, 2008:571).

From second half of twentieth century until 1990, Egypt witnessed three paradigm shifts in economic policy. Role of state in economic life and country's position in international market were changed. In 1952, the first shift occurred through end of British colony and revolution. Feudal and semi-feudal relations ruled over rural provinces. Private sector was dominant in commerce and small industries, and government slightly intervened to control foreign currencies and protect national industry (Alissa, 2007:2). Egyptian industrial structure was monopolistic, protected industries and small number of firms existed, markets were limited, entrepreneurs were small in numbers, and imperfect capital markets. Employment in industry increased only because of government pressures (Mabro, 1967:343).

Egypt attempted for half a century to develop based on industrialization target, but it did not change from infancy. The Dam increased employment, absorbed building materials, increased investments in electricity and public utilities. However, no large projects followed up. After 1974, investments in tradable goods and export industries were made, but there was no manufacturing industry or exporting sector (Hansen, 1991:153).

Even if new industries were created, they would not transform Egypt into industrial country due to consumption patterns (Abdel-Malek, 1964: 45). Egypt was in need for effective reforms and institutions (Kuntay, 2014: 20). Egypt's development was not a function of nationalist political rhetoric (Beinin, 2008:328). Egypt had a large informal economy, which was not included in any reform program. Therefore, reforms did not succeed. It became part of Egyptian political economy. It was considered as means for survival by class near subsistence. Public sector officials were benefiting from both sectors (Shechter, 2008:574).

Nasser was modern analogy of Mohamed Ali. Both adopted state-led economy, which focused on regional and international role of Egypt, industrialization and national army. Meanwhile, Sadat was modern analogy of Khedive Ismail. *Infitah* was thought of as betrayal to 1952 revolutionary goals. Ismail's policy was betrayal to development goals; he ignored public interests and independence in favor of speculators and tradesmen close to foreign powers. Their successors swayed policy from its goal. After Sadat, Egypt was a hybrid mix based on contradictions and determinations of preceding regimes (Roussilion, 2008:335-336).

Although between 1958 and 1964 poverty rates declined, income increment was not received by population under poverty line. The bulk of income was directed towards those above poverty standard. Income inequality was severe. However, few years later, and due to deteriorating economic conditions, income inequality declined (Levy, 1986: 90). Rent seeking was common in Egyptian politics. Rent describes an income that would cease to exist under perfectly competitive system, which is in or about being in equilibrium. Rent differs depending on institutional aspects in the system itself. Before 1952, rent was in form of increased tariffs or government-subsidized loans to private business. Under Nasser, rent was in form of salaries to merit, informal rationing, privileges to officers (Hansen, 1991:249).

After Charter of 1962 and October Paper of 1974, political Economy of Egypt was shaped by social compact between rulers and ruled. Goods and services were provided in exchange of political rights (Hansen, 1991:116). In public sector, there was deviation of leadership by leaders, who detached themselves from working class to exploit it. Reducing state intervention meant liberalizing technocrats rather than reducing public sector. For any policy, there should be stated intentions and structural impact. Therefore, it must not be class biased. The regime was weak to execute all intended goals, both in Nasser and Sadat era. Conflict between economic and political interests made public sector as treadmill controlling the economy, and made the private sector a center of economic activities (Cooper, 1979:495). Nasser and Sadat era had absent effective institutions, and rule based on alliances and network of clients, authoritarianism, repression, and absent communication (Marsot, 2007:162-163).

The government followed a parental style; it depoliticized people and social groups. The parental government provides goods and services, but apolitical population has increasing consumption. The government would be unable to keep its pace or increase new obligations to even out any inefficiency in old obligations (Hansen, 1991:117). Egyptian government has prioritized its own survival over other considerations, so all kinds of guided transformations of political process focused on government survival. Reforms focused more on political rather than economic considerations, so reforms were in finance, trade, tax reforms, and price controls. Liberalization had to focus on enhancing judicial reform, labor laws, and efficiency of SEEs (Gray, 1998:105-106).

Egypt was the perfect environment for cotton, a labor-intensive crop, due to warm weather, depth of soil allowing long roots to deep stick, and reliable water supply. However, the country was not successful in increasing production due to drop in yields, high water table level, and pests. Egypt faced competition from Mexico, Peru, and India. Soil during wars was exhausted due to lack of fertilizers and over-planting of cereals. Egypt could have planted plants that need small amount of water. Egypt had always a wasteful agriculture, time, seeds, illiterate farmers, and cheap labor. Egypt is an agricultural country; its policy was always shaped by its climate, location, and factor endowments. The country should have focused on labor supply; soil, climate, fruits, poultry, and dairy production. In Egypt, resources were fully exploited except for desert (Issawi, 1963:40-41).

Reasons behind agricultural problems in Egypt are as follows: class structure, resource distribution, social bases of Nasser and Sadat's regime. There was no mobility of peasants and no decentralized incentives. Sadat inherited Egypt with shortages, deteriorating infrastructure, foreign debt. Agricultural output constituted about 50 percent of industrial output. In 1974, Egypt was net importer of agricultural commodities; exports of cotton and rice declined (Richards, 1980:304-305). The fragmented land meant less return due to reduced size, this can be valid for large landowners, but for small peasants, their numbers increased at expense of large landowners. Unequal subsidization took place by granting loans regardless of holding's size, loans were in proportion to holding, so larger holding's owners got higher loans, and after 1961, they were free from interest. It can however be argued that loans offered small farmers to produce and not to see credit as punishment (Harik, 1984:4).

In Egypt, developmental activities were conceptualized, designed, and implemented in accordance with bureaucracy. Economic and social development was hindered by overstaffed enterprises, low productivity, red tape, and ineffectiveness, which reflected mismanagement of national development (Jreisat, 2006:415-416). Egypt is a labor exporting country. In development literature, if a country was endowed by labor force, it should engage in labor-intensive production techniques. However, in a country like Egypt, low quality of education, surplus labor market, high student to teacher ratio and lower salaries for teachers reasons negatively affect human capital as natural resource in Egypt. This means it is unable to use its resources efficiently or effectively. This in turn was translated into low growth rates, food security problems and worsening income distribution (Richards and Waterbury, 1990:75-94).

In Egypt, the limited nature of democracy was due to two structural factors: dynamics of rentierism: the state enjoying high autonomy and the population receiving goods in return for acquiescence; a declining state resources relative to demand. The second factor is the emergence and expansion of bourgeoisie associated with liberalization and they represent an important stress factor towards political liberalization. Bourgeoisie were created by the state and maintained their existence by being alliance to the state, they did not have interest in political liberalization except for safeguarding their economic position. Therefore, state and bourgeoisie were threatened by genuine democratization (Nonneman, 2001:141-142).

Table 3 summarizes the economic paradigm in Egypt starting from 1929 until 1970s. Between 1929 and 1955, private enterprise and free trade described the institutional setting; development process depended on agriculture and exporting. After 1955, there was a transition, with no major changes in development strategy. Etatism was followed between 1960 and 1965; public sector began to intervene. Between 1965 and 1973, public sector increased in size, and war economy witnessed deterioration, because of military considerations. After 1973, the economy moved to open door policy, with still big public sector and other revenue sources from Suez Canal, petroleum and workers' remittances (Hansen, 1991:10).

Table 3. Summary of Egyptian Economic Transition

<i>period</i>	<i>Institutional Setting</i>	<i>Basic development strategy</i>
1929-55	Private enterprise, free trade, moderate-sized public sector (WWII)	In agriculture, mainly export promotion (public investment); in industry, import substitution (protection)
1955-60	Period of transition	Essentially unchanged
1960-65	Etatism, peace economy, strongly increasing public sectors, first five-year plan	In agriculture, export promotion, and import substitution; in industry, import substitution
1965-73	Etatism, war economy, large public sectors	Subordination to military considerations
1973-	Etatism, peace economy, <i>Infitah</i> (partial liberalization), large public sectors	Import substitution in agriculture and industry; in oil, Suez Canal, and tourism, promotion of export-oriented activities; migration of workers

Source: Hansen, (1991:10).

3. IMPORT SUBSTITUTION INDUSTRIALIZATION IN TURKEY

Between 1838 and 1841, free trade treaties with Europe did not allow Ottomans to protect their producers, and led to capital penetration. The Empire was a net importer of grains, cotton textiles⁵⁸, and intermediate goods. Anatolian provinces exported agricultural products and raw materials. European manufactured goods and textiles prevented any attempts for industrialization (Pamuk, 1981:26; Hansen, 1991: 301-305). The Ottomans modernized fleet through technological training, and built a modern cannon factory, and industrial establishments in textiles and paper (Batou, 1993: 287). However, there was no modern industrial sector. Industrial production was based on flourmills, cloth, raw silk, and cotton yarn. These activities represented 78 percent of industrial activities (Boratav, 1981:165).

Foreign capital and non-Turkish ethnic groups dominated investments in railways and public utilities. There was a shift to cash crops away from subsistence crops. This was commercialization of agriculture. Manufacturing activities emerged by the end of the 19th century, but lack of tariff autonomy prevented better performance (Pamuk, 2010:17-21; Mehmet, 1983:59-60). This reflected disarticulation, as infrastructure focused on external markets (Boratav, 1981:165). Internal troubles, foreign aggression, and independence requests by other countries destroyed the Empire (Kili, 1980:383). Young Turks⁵⁹ initiated a multiparty constitutional monarchy. Their economic vision concluded that state should take the lead in economic sphere, and that economy collapsed due to European imports. They aspired at reviving industrialization. The Empire was dissolved in 1918 (Hansen, 1991:293-294; Waterbury, 1999:329).

⁵⁸ In the 19th century, cotton was main component for commercial agriculture in many western Anatolia districts. Balta Leman (Anglo-Ottoman) commercial treaty in 1838 harmed yarn productions. Raw cotton production flourished because of USA civil war of 1861-1865 (Teoman and Kaymak; 2008: 322).

⁵⁹ There were four wars and a counterrevolution. Young Turks issued industrial legislation and ended Islamic approach to politics. In 1923, the transition was completed by creation of the Republic (Hansen, 1991:294).

Turkey had an agrarian economy. Law of Encouragement of Industry in 1915 allowed the government to raise tariffs. Before WWI, income gap between Ottomans and high-income countries in Western Europe and USA increased⁶⁰. During WWI, industrial output declined, but government's control scheme was shaped (Pamuk, 2010:17-21; Mehmet, 1983:59-60; Hansen, 1991:294-305).

After the Empire fell, the economy was affected by remaining debts' settlement and old levels of customs (Naş, 2008:9). The infrastructure was disrupted by wars and labor shortage in agriculture. There was limited number of industrial installations to be damaged in Anatolian, as they were mainly in Istanbul. Skilled workers, entrepreneurs, and managers immigration indicated loss of industrial and commercial expertise. Departure of Greeks and Armenians weakened the Turkish industry (Zurcher, 2004; 196). The low GNI in 1923 was caused by low manufacturing capacity and disrupted production (Hiç, 2009:2).

3.1. A New Republic: Free Market Economy (1923-1929)

In 1923, Turkey became a nation-state. However, change occurs only when a country witnesses a transition (Ahmad, 2008:226-227). Republic was established by Mustafa Kemal Atatürk. Lausanne Treaty was signed with an expected expiry in 1929, preventing the country from selecting fiscal and foreign exchange rates. In 1924, Turkish population⁶¹ was around 13 million (Naş, 2008:9; Owen and Pamuk, 1998:13).

⁶⁰ During 20th century, gap between Western Europe, USA, and LDCs was large due to industrialization. Wars and Great Depression led to lagged record behind East Asia and Southern Europe, but better than Latin America and Middle East (Pamuk, 2008:269).

⁶¹ Epidemics and famine increased mortality rates, around 20 percent. Hundred thousands of Armenians and Greeks emigrated from Anatolia to Soviet Union, USA, and France. Migrants were about 900,000 of Greek Orthodox were exchanged for Greece Muslims who were 400,000 (Zurcher, 1992:166).

Lausanne removed privileges and capitulations. Therefore, some foreign enterprises were nationalized. However, the government was abided to keep tariff rates set at 1916: 5 percent on imports and 12 percent on exports. Ottoman debt⁶² payments were frozen until 1929. Agreement was reached in 1928 to pay debt between 1929 and 1953 (Hansen, 1991: 311-320).

The Republic was based on war-destroyed economy: WWI, Balkan War, and War of Liberation (Buğra, 2007:39; Zurcher, 2004:166-176). USA considered Turkey as frontier economy, with abundant resources and uncultivated land. Therefore, agricultural expansion was cornerstone of development strategy (Hansen, 1991:257-258). In 1924, Agricultural Institute was built. Atatürk emphasized importance of agricultural industry, agricultural banking and cooperatives, and mechanization. Reforms targeted agricultural sector with up-to-date technology and educated workforce (Keskinok, 2010:174-175; Bayar, 1996:774).

In 1923, Anatolian peasants made up 80 percent of population. They won War of Independence, but they were illiterate and unable to choose properly. That is why their participation was a long-term goal. Atatürk believed that when reforms take place from above, they are transplanted in society's roots. If reform started from below to the top, it would fail, as every individual would follow personal interests. Therefore, the program had to start from above downward, so that institutions and reformers could guide people on right direction. Kemalism started from problems supported by Atatürk to problems that might create controversies. The first thing was to define national community and territorial boundaries. After a homogenous community was created, political institutions could exercise authority and impose reforms (Zurcher, 2004:182; Kili, 1980: 384-385; Pamuk, 2010:17-21; Mehmet, 1983:59-60).

Atatürk decided to found an industrial base by building industries in cement, basic metals, and textiles. The Izmir Economic Congress was held to lay down basics for economic philosophy for the new state (Günçe, 1967:3).

⁶²Ottoman debt was to Germany, a defeated nation, so the debt of 720 million USD was informally written off. However, Ottoman debt was apportioned to debtors in Lausanne Treaty, and five years later 65 percent of debt fell on (Buğra, 2007:39; Zurcher, 1992:166-176).

The Congress stated that Industrial banks would be built, and credit facilities would be introduced. In 1925, the Bank for Industry and Mining was built to establish industrial and commercial institutions and provide related facilities (Günçe, 1967:4; Naş, 2008:9). Majority of industrial establishments were owned by foreigners or minorities. Among 282 establishments, 22 were state owned (Naş, 2008:9). Strategic sectors of defense and transportation were nationalized through their worth paid, commercial banks kept operations, however, due to lack of financial resources, nationalization efforts went slowly (Hiç, 2009:9).

The Republic suffered from budgetary deficits, lack of networks to establish links to West, and absence of sound economic thinking (Mehmet, 1983:51; Okyar, 1979:326-327). Turkish National Trade Association (Milli Türk Ticaret Birliği) was to be established, as suggested by business groups. It suggested state intervention, reform of commercial law and income tax, state control over foreign exchange market, and prevention of monopolies and foreign influence (Finefrock, 1981:375-376).

In 1924, İş Bankası (Business Bank) was built through mixed capital. The state owned share of 58 percent to finance emerging private industries, create a capitalist class, and develop private industry through credit financing or direct participation. Industrial engineers were educated and technically trained. Domestic products were transported at lower rates through land and sea (Günçe, 1967:4; Naş, 2008:9).

In 1927, Law for Encouragement of Industry was issued to assist private sector. It reduced tariffs, offered subsidies (Hale, 1980:103), and defined enterprises needed by the new economic system, whose goal was mass production. Mining sector received some privileges, with more privileges given to big operational scale mines. Other facilities related to land grants, charges exemptions, or stamp duties free securities were devoted to build industrial enterprise. Moreover, necessary raw materials, but domestically unavailable were freely imported (Hiç, 2009:2; Naş, 2008:9).

This law helped strengthening the Turkish bourgeoisie class receiving government support. Government gave big projects to contractors. Economic and political power of private capital increased (Karasapan, 1986:30; Günçe, 1967:6-7). However, it did not have an opportunity to perform as expected, because of the Great Depression and etatism (Singer, 1977: 2).

Turkey transformed from rural to industrial economy, a process that increased political and economic power of industrial groups, which shaped transition in ways beneficial to their interests (Çetin, 2010:6).

The concept of secular state, which responds to economic and social needs of people, was core idea of Kemalism reforms⁶³. Secularism was not in terms of Godless state, it meant state would not assume a religious role, in order to avoid social and political divisions. Supremacy of national willingness (Ulusal Egemenlik) meant the state would not safeguard certain cluster; its duty was improving people's lives, promoting reforms in social, economic, and legal spheres (Mehmet, 1983:51).

Agricultural exports increased during 1920s to Europe and USA (Hansen, 1991: 317). A reduction of 30 percent of shipment rates was introduced. A subsidy of 10 percent of total output value was received by enterprises as long as their prices exceed alike imports by no more than 10 percent. Moreover, the government established monopolies in some major industries such as tobacco, salt, oil, fuel, and insurance, while other public facilities were operating as semi monopoly such as transportation and national lottery (Hiç, 2009:2; Naş, 2008:9).

The initial strategy planned to rely on private sector and not to finance industrial growth through taxation of peasantry. In 1924 Constitution, it was announced that private property and free enterprise were major keys for the state. Atatürk stressed the importance of economic independence for national sovereignty. Ankara was selected as the capital for considerations related to Anatolia development and distribution of public services. Creating of new capital and building new industrial cities were important issues in development planning (Keskinok, 2010:174-175; Bayar, 1996:774). The focus of government was on internal policies and reforms. It was a general speech setting an overall situation rather than specifics of economic development (Okyar, 1965: 99-100; Mehmet, 1983:50).

⁶³In the first years, Kemalism focused on political and cultural reforms to build a modernized Western country. He adopted Western legal codes, secularized education, and adopted Latin alphabet (Bayar, 1996:774).

The Ottomans did not allow powerful landowners class to emerge. Tithe (Uşr) was a burden on small peasants. It was a predetermined percentage of agricultural output. During first years, focus was on political consolidation and social reforms. In 1924, tithe was 22 percent of government's budget revenue and 64 percent of direct tax revenue. In 1925, Tithe fiat tax and animal tax (Agnam) were abolished. It reduced burden on small peasants and alleviated poverty. Agriculture used to serve public debt, so a major source for revenue was gone. Therefore, urban population was highly taxed, purchasing power declined, and import restrictions increased (Pamuk, 2010:23; Zurcher, 2004:196-197; Hiç, 2009:2; Hansen, 1991:299-316; Singer, 1977:1).

During 1920s, Turkey had resource constraints and Ottoman based infrastructure, it was a free-market oriented economy. In 1928, there was drought in Central Anatolia. Atatürk consolidated his political position through Lausanne Treaty. The assembly and controlled elections were dissolved. Republican People's Party (CHP) took over the Defense of Rights organization. CHP was a civil agency to design national policy and modernize the society. Six principles (*Altı Ok*) were part of the constitution in 1937 (Zurcher, 2004:166-182; Kili, 1980: 384-385; Buğra, 2007:39). CHP Third Congress in May 1931 approved them. In 1937 Constitution, they were incorporated as second article (Mehmet, 1983:50). These principles are Republicanism⁶⁴, Nationalism⁶⁵, Secularism⁶⁶, Populism, Reformism⁶⁷/Revolutionist (Devrimcilik), and Etatism (Kili, 1980:387-391).

⁶⁴Republicanism was sole way realizing national sovereignty. Republic was established by people and for people, not group. The identity change to nation-state was a result of Sultan's collaboration with occupation forces. The intensive educational programs were to plant roots of Republic in young generations (Kili, 1980:387-388).

⁶⁵Nationalism described secular state, which differs from Middle Eastern nationalism depending on religion. Nationalism denied any rights for individual or organization to rule over others. It was anti-imperialist and populist, believing that all nations should be independent; it had a humanitarian trait, which was not racist. Turkish nationality was about the degree a person committed to goals and ideals of Turkish Republic. Nationalism did not trample on rights of other nations; it admitted responsibility for the past (Kili, 1980:387-388).

⁶⁶Secularism was a breaking line between traditionalism and reformism. Religion was believed to be an obstacle for modernization (Kili, 1980:391).

⁶⁷Reformism described protection of Kemalism and modifying its tenet when needed, or commitment to social and Cultural Revolution to modernize Turkey. It was called *-İnkılapçılık*, defining a commitment to state-led growth and change (Zurcher, 1992:182; Kili, 1980:391-392).

Underdeveloped market forces determined interest and exchange rates. Short-term credit and foreign capital financed domestic infrastructure. The state had minimal role limited to stimulation of private capital, setting up banking system, and developing infrastructure (Pamuk, 1981:26; Naş, 2008:9). There state could not protect infant industries, owing to Lausanne. In the 1920s, one-third of firms were joint ventures with foreigners, on the condition that investors did not seek political concession. The Law for Industry offered incentives to new industrial establishments. There was monopoly in sugar, tobacco, oil, and harbors. Monopoly rights were not exercised directly by the government; foreign and domestic firms were granted rights under favorable terms (Hansen, 1991: 314; Hale, 1980:103; Boratav, 1981: 168).

Indirect tax on consumer goods increased; a new 10 percent tax was imposed on domestic industrial products, and prices of goods produced by state monopolies increased. Manufacturing share was 10 percent in 1923/25, and 8-9 percent in 1927/29. Demand increased for building materials. Moreover, agricultural expansion increased demand for consumer goods. The country matched budget expenditures with revenues from agriculture, custom duties, and income tax. Between 1926 and 1929, expenditures as percentage of GDP were between 12-15 percent, from which 17 percent allocated to investment and state enterprise's transfers. On the monetary side, absence of monetary policy and central bank was another obstacle. Turkey had its central bank in 1930, but did not have monetary policy (Hansen, 1991: 316-449; Naş, 2008:9; Okyar, 1965: 99; Boratav, 1981: 171).

The world's demand for foodstuff and raw materials declined, and terms of trade favored manufactured goods. Foreign trade suffered due to falling prices of agricultural exports such as tobacco, and cereals. Living standards deteriorated, tax burdens increased, and society was dissatisfied. The foreign exchange crisis, decreased flow of foreign capital, and due date of first installment of debt initiated protectionist policies (Okyar, 1979:327; Owen and Pamuk, 1998:13-17; Naş, 2008:9; Pamuk, 1981:26). However, the state already took steps towards protectionism before 1929, through controls on foreign exchange and foreign trade (Pamuk, 2010:23; Zurcher, 2004: 178).

The government attempted to attract foreign investments and provide incentives for some industries such as textiles and cement. Moreover, new railroads were built, so construction industry flourished (Owen and Pamuk, 1998:16-17). The growth in agriculture between 1924 and 1929 led to yearly average GDP growth of 10.8 percent, due to allocated idle capacity, while growth in industry was less, despite of incentives. Transportation was a way to marketing and commercialization of agricultural output. In 1927, domestic gross industrial production was 550 million TL. Imported manufactures amounted to 187 million TL (Naş, 2008:9; Okyar, 1965: 99).

Although the government supported private sector in 1920s, resources needed to promote industrialization were not owned by private single entity. Private industries did not have financial strength. The modern industry was only transferred through wholesale import of technology and plants (Pamuk, 1981:26; Naş, 2008:9). Technology was either imported, or remained from Ottomans era (Singer, 1977:3). During the Great Depression, large landowners suffered, producing for local market and abroad. Small peasants marketed low share of their output, facing limited losses. The economy stagnated between 1927 and 1929, GDP declined in absolute terms and no major structural changes took place in industry share. There was shortage of private capital and entrepreneurial talent (Hale, 1980:103). Post Great Depression, the liberal economic policy was no more adequate, due to highly poor infrastructure and lack of private capital (Maxfield and Nolt, 1990:68).

The failure of laissez-faire was owing to inability of private sector to carry on needed level of investment, and large-scale industrialization in Soviet Union, so the government assumed direct responsibility in planning and producing. Accordingly, etatism emerged. Turkish planners followed the Soviet Union experience. Soviet Union promised help through credits for capital goods. The Soviet Union group visited Turkey in 1931 to draw a plan on industrialization. Recommendations were on iron, steel, textiles, and chemicals (Okyar, 1965: 99; Bayar, 1996:775).

3.2. State-Led Growth and Initiation of ISI (1930-1950)

Agriculture was the most important sector, which recovered to pre-WWI levels only in 1930 (Zurcher, 2004:166). Agricultural development was to improve life standards of rural population, and increase supply of raw materials. The government increased commercialization and exportation in agriculture, and subsidized input markets to increase usage of tractors. Transport network was improved through highways to create integrated local markets (Hansen, 1991: 314-316).

Turkey's exports were in better position compared to other LDCs, but its terms of trade were harmed as well. Import tariff imposed in 1929 kept prices of manufactures high, while agricultural products declined in prices. The local industry improved in terms of profitability, but interventionism was better for industrialization, owing to absent trust in capitalist model (Hale, 1980:103). Industrialization was based on private entrepreneurship, and government intervention when needed. ISI was done in areas like sugar, textiles, and cement, domestically available. The government could increase prices in monopolies and abolish any quantitative restrictions on foreign trade (Hansen, 1991: 313). Etatism (Devletqilik) was a nation-building⁶⁸ strategy, and was the backbone of CHP through its six pillars of social and economic development. Its overall goal was socio-economic development through higher standard of living (Mehmet, 1983:49-50), and protection of individuals from destructive agencies (Hale, 1980:107).

Kemalism emerged during War of Independence. Afterwards, the reform period to transform the society started. It was a defensive modernization to keep traditional society and build new institutions aside by old ones (Kili, 1980:392). The revolution was supported by social groups such as landowners, merchants, and tribal leaders. Peasants' support was important, as there was no urban industrial class, due to absence of industrial base (Hansen, 1991: 312).

⁶⁸Reform was based on nationalism, but also on reception of legal codes and methods of other modern nations in building institutions. Nationalism and democracy did not contradict; institutions were built to establish a nation (Kili, 1980:388). Nationalism was psychological and political force, which the leader had to consider (Yale, 1958:426).

Etatism was not socialism, as private ownership was still present, but state took major stake in projects, that private sector could not afford (Zurcher, 2004:197). Etatism was not based on future vision; it was rather based on necessity. Atatürk emphasized private ownership (Okyar, 1965:101).

Until second half of 1932, there was no clear content for etatism. The government was major investor only in railways, it did not have significant activity in productive field, and it was safeguarding the internal market (Boratav, 1981: 172). There was bureaucracy among civil society, military, and the state. By this time, there was no Turkish bourgeoisie or working class conflict. Therefore, etatism and populism were means to develop labor and capital organizations (Sakallioğlu, 1992:712).

Kemalism, through its unity, authority, and equality patterns, was a turn in Turkish history. Dualist institutions and goals were removed, elite was mobilized, and education was developed. Free education was the main tool for social mobility and change. Education policy increased base of political elite and created modernizers of Turkey. Individuals with official status such as civil servants and intellectuals were an important part of modernization, which also depended on the modern secularized society (Kili, 1980:391).

Etatism as a concept was accepted in 1931 by CHP general assembly. In 1933, etatism was introduced through First Five-Year Plan in 1934, and in the Constitution in 1936. State Economic Enterprises (SEEs) operated in manufacturing, transportation, mining, and energy. Etatism stated that the government would regulate the general frame of economy in areas where private sector lacks efficiency or capital (Kili, 1980: 390). After maturity of private enterprise in an industrial sector, it would be totally left for private sector (Hiç, 2009:9). It described industrialization policy that focused on consumer and intermediate goods (Pamuk, 1981:26).

Etatism weakened ties between Turkey and capitalist world. However, dependency remained. Capital accumulated in hand of bourgeoisie who benefited through their market monopolies, import license to SEEs, credit from state banks, and contracts for major projects (Pamuk, 1981:26).

Protectionism allowed the country to accumulate capital needed for industrialization. Partnership between public and private sector created high productive projects. Government protected the economy in face of external capitalism, through its non-capitalist strategy, inspired by Soviets (Naş, 2008: 24-25).

There was lack of capital, expertise, and successful economic development models. Elite accepted the market economy until the Great Depression. Afterwards, the shift was towards central planning and controlling (Kili, 1980:390). Turkish etatism was built on import-replacement industries and state control (Hale, 1980:100). It focused on regulating functions of state more than stabilization. Etatism did not have many effects until after 1930s. SEEs actively operated after 1933. The negative Ottoman experience with budget deficits and large external debt was one reason behind cautious strategy; it was not a planned strategy as in Keynes's philosophy to generate aggregate demand through devaluated currency and expansionary policies, it rather focused on closed autarkic economy with increased central control through state sector (Pamuk, 2008:280; Naş, 2008:13).

Ottomans left a legacy of looking up to the government. Although etatism was created within a revolution, it was a return back to old mentality of rigid state control. Self-reliance in development strategy was another core principle of etatism. It was articulated through centuries of economic penetration and exploitation under capitulations. Consequently, Kemalism disfavored foreign capital and trade. Therefore, Turkish development strategy was unlike those of LDCs after war. Most countries relied on free trade, while Turkey had anti-trade bias (Mehmet, 1983:53).

Etatism adoption was not a smooth process, as disagreement existed about goals and implementation (Okyar, 1965:98). Radical-reform nationalists believed it was an alternative to capitalism and its principles described populism (Hale, 1980:105). Soviets assisted etatism financially and ideologically. After Atatürk, fears were uprising that private enterprise would be destroyed, but CHP defined etatism as strategy allowing state to undertake general steps towards public interest, while private enterprise would be vital in undertaking projects (Mehmet, 1983:52).

In 1939, law stated that SEEs would be turned over to Turkish entrepreneurs, but this did not happen until 1950s. When drawing the second industrial plan, Bayar stated that welfare of public and industrialization drive could not be left solely to private initiative, as it required at least two centuries. He admitted the support to private sector in order to industrialize. Etatism was therefore a temporary expedient to establish economic infrastructure, help accumulate capital and establish entrepreneurial skills, and then open the way for private enterprise (Hale, 1980:107). State was closely defined with the party. CHP did not have a separate ideology, or organizational personality; it was rather bureaucratized (Zurcher, 2004; 177).

In 1932, the Kadro⁶⁹ (Cadre) believed the state should establish and plan the economy, in terms of transport, infrastructure, and credit institutions. Social duty lied on the state, which prevented social class conflicts. This harmony would eliminate any privileges (Hale, 1980:105; Naş, 2008:14). Groups advocating economic liberalism argued that private sector needed protection until it could compete internationally. Groups for economic etatism believed in state planning, but in gradual removal of state's role. The Kadro supported a non-capitalist path, and centralized state through SEEs. However, all views agreed on need for industrialization. The matter was degree of intervention rather than intervention itself (Hale, 1980:105; Naş, 2008:14).

In 1930, main goals were self-sufficiency and internal market-orientation in agriculture and industry. In 1933, Sümer Bank was responsible for project development and management, beside its banking activities. Relationships among production units were to realize goals of economic and political independence. Laws aimed at liquidating feudal ownership, and granting land to farmers. These laws were to achieve equality and access to public services (Keskinok, 2010:174-175). In the interwar period, ISI was the major development strategy. However, agriculture shaped more than half of the GDP, while manufacturing was 12 percent (Hansen, 1991:267).

⁶⁹Kadro was established by Şevket Aydemir and some associates. It was a monthly review, which was published, and confirmed that revolution started a reform, which did not end, and that faster changes were needed. A group (Kadro) would be trained on how to perform these reforms and finally planning would be inclusive to all fields of life (Hale, 1980:105; Naş, 2008: 14).

During 1930s, political considerations preceded economic efficiency and rationalization concerns. The aim was internal regional development and freeing peasants from feudal obligations. Urban planning was a major step in development agenda. All privileges to foreign nations were abolished; rehabilitation of railways, ports and transportation, establishment of Bank of Commerce and Bank of Industry, and nationalization of stock markets. By half of 1930s, more than 80 percent of foreign trade was under quota system (Pamuk, 2008:275; Keskinok, 2010:174; Pamuk, 2010:23).

In 1938, Law No. 3436 provided a legal framework for SEEs that could return to public through issued equity shares. Price mechanism regulations and profit maximizing were common for public and private sector. The link between two sectors in area of money and finance aimed at a sustainable stable economy. In 1940, law set a fixed scale of salaries in SEEs, and connected them to salaries in central government administration, to have parallelism between employees. Before this time, salaries were independently determined in SEEs. When inflation occurred, high salaries in private sector led to personnel loss in public sector due to stagnant salaries (Okyar, 1965:106). In 1940s, high government expenditures were financed through higher taxes and money supply. (Naş, 2008:18-19).

Between 1927/29 and 1937/39, agriculture grew at 6.2 percent, and accounted for 49.8 percent of GDP. On the other hand, industry had growth rates of 10 percent, but represented 9.5 percent of total GDP. Until 1931/33, public investments were mainly in railways, communications, and transport. Under etatism, the scope expanded to agriculture, health, education, and industry. In the interwar period, 50 percent of investments were in agriculture and railroads, while 25 percent was into industry (Hansen, 1991: 330-332).

SEEs helped apply mixed economy framework (Öniş, 1991:164). The private sector was encouraged and flows of foreign private capital increased; liberal system focused on private enterprise, investment, and production. Foreign trade was protected recourse to public investments. SEEs undertook social productive infrastructural and super-infrastructural fields. The focus was on establishment and expansion of basic agricultural and industrial goods (Hiç, 2009:20).

Between 1923 and 1943, the public sector handled major industries such as paper, sugar, and iron (Sayek and Selover, 2002:209). Due to increased number of SEEs, a legal framework was needed to standardize their practices. In Law No. 3460, SEEs were defined as enterprises with state-owned capital. Each enterprise could set up subsidiary organizations and compete with private firms, allowing for establishing mixed companies. Enterprises behaved as business and were responsible for their capital through administrative and financial autonomy. Profit was the main motive for each enterprise. On legal side, they had separate legal entities. Moreover, every enterprise followed a certain ministry. SEEs were superimposed in many sectors (Okyar, 1965:102-105).

Goods of SEEs had low prices, which did not cover costs. Reduction in real wages was to reduce expenditures in GNI (Arıcanlı and Rodrik, 1990:1345). SEEs signaled management rigidity, bureaucracy, high losses, and inefficiencies due to increasing government intervention, banks did not have financial or monetary autonomy (Kamrava, 2012:97).

SEEs would start a development process, but then a mixed economy should appear. Resource allocation would be based on supply and demand, and private sector would operate. Efficiency and equity were complementary goals. Efficient economic management in economic sectors would create equality, and efficiency would ensure that customers' needs were met by supplied goods in the market. The state should focus on minimizing social and economic inequalities rather than involving directly in the production (Mehmet, 1983:55).

SEEs incurred financial losses and obtained credits from Central Bank. SEEs were intended to be autonomous and free of bureaucracy. However, ministries intervened with administrative decisions. This led to loss of initiative and flexibility. In etatism, government could stop increase in prices, due to its control over main sectors, and set up price controls through legislation and constraining profit margins, or preventing SEEs from raising prices. SEEs should have behaved as business firms, but their decisions were politically based. However, they developed managers and engineers who helped develop private industry (Zurcher, 2004: 198).

There were some contradictions resulting from dependency on SEEs. First, industrialization based on SEEs promoted monopoly and prevented market competition. High cost local industry was developed through credibility to protectionism. However, SEEs did not abide by the main goal, which was to "take-off" then hand it over to private sector. They were rather institutionalized and serving elite. Therefore, inefficiency and mismanagement and high subsidies were severe causes of failure (Owen and Pamuk, 1998:28; Mehmet, 1983:47).

Industrial employment was framed as national duty. However, agriculture was still a main activity for peasants; working in industry or mining was as part-time, especially in times of low demand for agricultural labor. Moreover, SEEs using agricultural inputs preferred direct contact with small farmers through input provisioning, rather than expert advice. This was called “peasant-worker phenomenon” (Buğra, 2007:40).

The government attempted to take over foreign firms operating in public services, and to increase capital inflows, but efforts were not successful due to the world economic crisis (Owen and Pamuk, 1998:17-18). The government built enterprises such as Ziraat Bankası in 1937 and Agricultural Supply Agency (Türkiye Zirai Donatım Kurum) in 1943 (Singer, 1977: 39). In 1941, transactions tax was applied to manufactures, domestically produced or imported, and to banks and insurance companies. The government focused on yields rather than equity or economic consequences of taxes (Singer, 1977: 12).

Domestic manufacturers emerged due to attractive conditions under import repression. A recovery in countryside led to increase in agricultural output, although international prices were low. WWII did not directly involve Turkey, but GDP declined by 35 percent, and exports of wheat decreased by 50 percent, full mobilization took place, imports declined, and most resources were allocated to army (Pamuk, 2008:280).

National Defense Law (*Millî Korunma Kanunu*) was passed in 1940, allowing for unrestricted government control in setting prices, imposing forced labor, and acquiring materials. Living standards deteriorated; black market, exploitation of farmers by importers and traders. The wealth tax (*varlık vergisi*) was introduced in 1942. However, application was disastrous; tax assessment was made by local councils and government officials, there was no fixed rate, which made traders and non-Muslims pay ten times higher tax than Muslims. Non-Muslims were not allowed for payment spreading, so they sold their properties, those unable to pay were either departed or sent to forced labor. In 1944, wealth tax was abolished due to criticism by Britain and USA (Zurcher, 2004: 199-200).

The law on national protection harmed farmers and tradesmen, increased numbers of those entitled to army was about 2 million in 1939 and 18.6 million in 1945; they were mainly workers or farmers. Farmers were forced to sell half of production to “Turkish Grain Board” (Toprak Mahsulleri Ofisi) (TMO). The private sector was harmed due to intervention, controls, penalties and wealth tax, absence of labor rights and social security (Hiç, 2009:16).

TMO offered reasonable prices for larger farmers and peasants. It bought commodities from intermediaries, and aimed at a guaranteed market for producers. Moreover, it sold commodities at lower prices to consumers, this was an aspect of social justice, and sold to institutions such as hospitals and schools. However, high expenditures increased losses and its deficits were transformed to the treasury. It depended on imported grains to keep stable consumer goods’ prices (Singer, 1977: 221-222).

During WWII, quotas were unrealistically high, so peasants were forced to sell grains to Office of Soil Products⁷⁰ (TMO), even if their families cannot find food. Therefore, some cases of rural starvation were recorded. Inflation was caused by monetary policy; the Istanbul cost of living index changed from 100 in 1939 to 354 in 1945, a 23 percent annual increase. Increased domestic money supply was main reason for budget deficits (Hale, 1980:109).

⁷⁰ The government built the Office of Soil Products (TMO) in 1938 (Hale, 1980:109).

The mobilization process drafted men from all sectors. Resources were low in supply, government policies did not encourage production, for example, the system of forced delivery of agricultural products at low prices, and 10 percent tax on soil products (Hansen, 1991:335).

The decline in industrial output was caused by shortage of imported machinery and raw materials. Agricultural output declined, because of adverse weather, grains diverted to black market, and shortage of labor. It was a global crisis, which Turkey could not influence. However, the government should also be blamed, as growth was its responsibility. Ignorance of agriculture caused public discontent (Hale, 1980:109). Urbanization and open political regime helped urban industrial groups to share power with elites. There were macroeconomic and political instability. After WWII, industry leaders were family holdings and large conglomerates acting in most sectors (Pamuk, 2008:281).

WWII had positive impact as well. As world prices rose, Germany and Allies increased demand for Turkish exports. Turkish imports were constrained to emphasize protection (Singer, 1977:14-15). After WWII, the economy recovered. It was better than Middle East, Africa, and South Asia, but worse than Southern Europe and Latin America (Pamuk, 2010:18). Demand was high for economic reforms, flexible management, autonomous state enterprises, and a distinct private sector (Kili, 1980:390).

3.2.1. First Five-Year Industrial Plan

The first five-year plan was drawn in 1933 with technical and financial support of Soviets, and was approved in 1934 (Richards and Waterbury, 1990:25-26). There was an interest-free loan⁷¹ up to \$ 18 million, and repayment was in form of unspecified product quantities. Five-year plans and public investments were instruments of development policy to reach take-off stage (Mehmet, 1983:52).

⁷¹In 1934, a loan agreement between Turkey and Soviet Union was signed to support industrialization (Finebrock, 1981:377).

Soviet delegation in 1932 wrote report on Turkish industrial development, and the \$8 million gold aid to industrialization program (Zurcher, 2004:197). The report by Soviets⁷², by Soviet Professor Orlov shaped the first industrial plan, but only superficialities of Soviet planning were adopted. Nation and state were one inseparable unit, and the elite was a guarantee against any trials to deviate etatism, and it was never tolerant to struggle among elements of national production, workers, and employers (Hale, 1980:104-105).

The plan was set up after nationalization of foreign companies. Main needs of the country were development, protected markets, and industries internally developed. There was proposal for building 20 factories, efficient investment and foreign trade arrangements, integration of transportation system to meet industries' needs. Industry's locations were selected based on proximity to labor force, security, housing opportunities, and raw materials (Keskinok, 2010:179).

The plan established SEEs in steel, iron, glass, and chemical products. It aimed at producing consumer and producer goods using available domestic resources, increasing employment through better allocation of labor surplus, and building factories serving some sectors such as: paper, iron, steel, and chemicals. In 1933, Sümer Bank replaced State Industrialization Office and Industrial Credit Bank to supervise and execute the plan (Günçe, 1967: 13-17). The Eti Bank was expected to work on acquisition and improvement of mines, whether state-owned or foreign. The focus was on capital goods and heavy industry (Singer, 1977: 9).

Moreover, strategic nature of six goods was declared, three whites: textiles, flour, and refined sugar, three blacks: coal, petroleum, and iron. They were sold by state monopolies. State revenues were obtained through customs and profits from agricultural monopoly. In 1933, the Republic was ten years old. It was first nation of "Third World" to define its planned economy (Finefrock, 1981:377; Waterbury, 1999:333).

⁷²Inonu was impressed by factories built in Stalin's era. The Secretary General of CHP Recep Peker, in 1931 visited Italy and praised Fascist institutions in a report. Atatürk predicted that this course of action would take place after his death (Hale, 1980:104-105).

Between 1933 and 1939, real GDP increased on average by 8 percent annually, compared to 3.2 percent between 1927 and 1932. Turkey used foreign exchange to import investment goods and domestically produce intermediate technology consumer goods. Investment goods amounted to 20 percent in 1928 and 42 percent in 1939, while textiles, clothing, and sugar amounted to 44 percent in 1928 and 19 percent in 1939 (Hale, 1980:108). Industrialization-driven policy had to be sustained when successive development policies were considered. There was propensity towards economic nationalism, which emerged since the formation of the Republic. In 1937, total industrial output grew at 10.3 percent in 1937 and 15.7 in 1938. On the other hand, agricultural sector grew slowly, due to biased selective price controls in agriculture, reflecting imbalance of etatism. Financing industrial projects was through taxation and forced savings. This enlarged economic and political gap between rural and elite clusters (Mehmet, 1983:53; Naş, 2008:18-19).

Although Turkey borrowed to execute the plan, it used capital domestically accumulated (Singer, 1977: 2). Foreign capital was in form of credit loans and grants. In 1930, the American Turkish Investment Corporation granted the first loan of \$ 10 million in return for monopoly in matches and lights, along with annual interest of 6.5 percent for twenty-five years regardless of loan payment. The second loan was from Soviet Union with amount of \$ 8 million, and zero return for twenty years. Moreover, the equipment was selected by Turkish government, repaying in TL for Soviet Union buying Turkish goods. UK and Germany gave loans during span of the plan 1934 until 1939 (Günçe, 1967: 13-17).

The plan, however, did not reflect a well-planned industrialization model. Selection of industries was based on pure economic criteria such as domestic raw materials availability and essential imports' substitutes. Turkey had a historical comparative advantage in textiles, steel, iron, paper, and cement. Therefore, investments targeted consumer and investment goods industries. Moreover, noneconomic factors such as cultural, social, and strategic considerations affected the implemented policy. Iron and steel plants represented strategically important investments for railways and armaments industry. Two plants were located in Istanbul, while majority of new fourteen plants were located in central and western Anatolia. This distribution of new plants aimed at spreading benefits of industrialization (Finefrock, 1981:382; Okyar, 1965:102).

3.2.2. Second Five-Year Industrial Plan (1939-1944)

In 1938, second five-year plan planned for building 100 enterprises, deepening industrial base, developing backward areas such as Eastern Anatolia (Bayar, 1996:775), and extending ISI scope. However, WWII led to abandonment of the plan. The industrialization priority was set clear in first plan, which emphasized a start of state-led growth (Naş, 2008:19).

A draft was prepared in 1936 and accepted in 1938. It included projects of mining, fuel trade, chemicals, engineering industry, foodstuff, and regional electricity plants. The plan aimed at achieving the maximum utilization of natural resources of mines, land, and sea, using domestic raw materials to develop industrial zone through establishing electric power station, modern port for steel and coal, and improving infrastructure of railways and transportation, building factories for agricultural equipment, meat canning, cement, sugar, housing projects, and aluminum factory (Bayar, 1996:775). The plan paid attention to poor areas, so a spinning factory was to be built in Erzurum, cement plant in Sivas, and sugar refineries in eastern regions (Singer, 1977: 9). The goal was to realize positive effects of industrial development over agriculture, through establishment of mining, electric stations, heating industry and chemical industry. These plans were not solely industrial, they were social, and national inclusive plans (Keskinok, 2010:179).

Five-year plans had a leading role in industrialization and capital accumulation. Easy stage of ISI used unskilled labor, which produces nondurable consumer goods. Turkey expanded its agriculture production and exports through liberal trade between 1947 and 1953. The ISI and its inward tendency were achieved by SEEs and heavy interventionism. Therefore, the domestic aggregate demand grew steadily (Çeçen et al, 1994:39).

The main difference between First and Second plans lied in emphasized areas. Second plan focused on capital and producer goods along with public works, it focused on solving individual problems through analyzing Turkish economic policy. Major advisors and partner firms were British. The plan was assessed by to-be aid granting countries and top governmental authorities. Major sectors included agriculture, power, communications, and cement (Günce, 1967:19-20).

However, both plans did not draw a comprehensive development plan, due to limited goals. There was no economic analysis covering national income growth. They included investment and output targets for listed industries. Banks had to operate as normal banks; they could open branches and accept public deposits. Majority of resources was from government loans and budget allocations, so they were more like state holding companies (Hale, 1980:101). Both plans addressed the question of what development should be, rather than estimating potential development. The main dimension was industrial development due to benefits of manufactures (Keskinok, 2010:179).

3.3. MULTIPARTY SYSTEM AND ECONOMIC PERFORMANCE (1950-1960)

Atatürk adopted some strategies on political and economic sides. On political side: single party system and bureaucratic military. On economic side, monopolist state to collect revenues (Owen and Pamuk, 1998:13-15). One party system with no contest was the ideal condition for etatism (Bayar, 1996:775).

The Great Depression created hostility between peasants and merchants. The government was affected by global collapse of capitalism in the early thirties (Hale, 1980:103). Kemalism favored traders and entrepreneurs, seen as backbone of modern industrial society, while small farmers and workers were marginalized. In 1936, Labor Law promised insurance and safeguard measures, but it prohibited formation of labor unions and strikes, so wages declined in 1930s and 1940s (Zurcher, 2004: 200).

The system discovered that an ideology and basis for reforms should have been explained to people to convince them and build institutions to support it. Therefore, CHP limited the scope of political parties to certain purposes and interests of groups (Ahmad, 2008:228-230). Authoritarianism flawed after 1925. There was no space for competition; social discontent was unexpressed, because of single party system, corruption, and absent competition among bureaucrats and politicians. Lack of communication with population was felt during the Great Depression, as the crisis was not seriously mentioned in assembly. Movement to multiparty system was a step to regain public confidence (Pamuk, 2010: 23; Zurcher, 2004: 178).

The Liberal Republican Party (Free Party) (SCF) was established in August 1930, under leadership of Ali Fethi Okyar, suggesting more emphasis on free enterprise, and targeting private enterprise. SCF⁷³ initiated political debate about liberal economic policy versus interventionism (Pamuk, 2010:23; Zurcher, 2004: 178; Bayar, 1996:775; Hale, 1980:103).

SCF believed etatism was a means of restrictive interventionist state. On the other hand, CHP believed etatism was the way through which development goals were realized. However, discussions continued in less free fashion. The focus of discussion was no more about whether the state should intervene in economic sphere or not, the focus became on forms state intervention should take. Due to support from groups opposing secular Republic, the party was dissolved in November of the same year (Hiç, 2009:7-8).

Atatürk replaced İnönü with Celal Bayar⁷⁴, as etatism began to be marginalized. İnönü attempted to harmonize opposition within regime, declaring end of party control over bureaucracy, and those local party organizations would no more be headed by provincial governors (Ahmad, 2008:231). Atatürk introduced Labor Law in 1936, which banned strikes and introduced Penal Code of clauses illegalizing any establishment of group or social class that can dominate over other classes, or eliminate basic economic and social order (Hale, 1980:104-105).

In 1938, the Law of Associations⁷⁵ banned labor and trade unions. The state imposed its political ideas on society to achieve social integration. During war years, farmers and small-town merchants increased their incomes through black markets, demanding more rights and freedom to act (Sakallioğlu, 1992:712-714; Zurcher, 2004: 177). In 1940, Customs Administration Law (Orfi Idare Kanunu) prohibited associations and meetings. The National Security Law issued a close regulation of industry, agriculture, and commerce. The struggle was over whom will be winner of votes (Blind, 2009: 41-42).

⁷³ Atatürk allowed multiparty system to absorb social discontent and revive CHP. Atatürk demanded the new party to stay loyal to Kemalism principles. Fethi Okyar established the Free Republican Party (*Serbest Cumhuriyet Fırkası*) (Zurcher, 1992: 178).

⁷⁴ Celal Bayar was minister of economy between 1932 and 1938 (Zurcher, 1992: 177).

⁷⁵ CHP favored a nationalist unified labor; it introduced in 1947 the Employer-Employee Unions and Union Federations Law. The Law aimed to face any union acting national interest. On the other hand, DP supported strike rights (Blind, 2009: 41-42).

In 1940, İnönü declared shift in party's policies towards free-market system. Inonu believed that political stability and multiparty democracy would positively affect economic growth (Ahmad, 2008:234). The National Defense Law in 1940 allowed higher control for the state over economy, private sector, and individuals. Law of Encouragement of Industry was withdrawn in 1941. Therefore, share of private sector in manufacturing industry fell from 80 percent in 1938 to 63 percent in 1950. However, it is logical that the government exhibit more control during wartime (Ahmad, 2008:231; Hale, 1980:111). Under pressures from USA, CHP amended Law of Associations in 1946 and allowed for labor and trade unions (Sakallioğlu, 1992:713; Zurcher, 2004: 177).

There was barter trade with the Soviets and Germany⁷⁶. Turkey attempted to build light and heavy industries, but it was inefficient due to small scale, inadequate supplies of raw materials, and poor infrastructure. Government coordination was needed in credit, monetary and fiscal policies to attract private investments (Maxfield and Nolt, 1990:60). The focus was on investment, initiatives, and state management. The individual voluntary endeavor was still not developed (Thornburg *et al*, 1968: 182-184). Political and economic changes in Turkey were caused by internal and external factors after WWII: dissatisfaction with CHP, agricultural producers and small peasants that suffered taxes and provision of urban areas. Bourgeoisie were privileged but dependent, they aspired to private enterprise. USA emergence shifted preferences towards open economy. Soviet Union had territorial demands, which led turkey to resort to USA, offering Marshal Plan (Pamuk, 2010: 25-26).

⁷⁶ Turkey kept neutral. It had much trade with Germany; it was equal to its trade with remainder of the world (Singer, 1977: 6).

USA was the new dominant power that shifted economic policies towards free market⁷⁷. Many LDCs cooperated with West, especially the Marshall Plan⁷⁸ for economic and military goals during 1948 (Pamuk, 2008:281). Transition into multi-party democratic system was not an easy task (Owen, 1992:86).

Turkey was forced into the system imposed by West. Moreover, fall of powers based on single party was an encouraging factor (Hiç, 2009:12). USA encouraged agricultural exports, manufactured imports, and foreign capital. Landowners, middle and small peasants were dissatisfied with single party (Bayar, 1996:777; Pamuk, 1981:27).

Marshall Plan financed agricultural machinery importation, provided easy credit markets and foreign exchange. Korean War increased imports and exports along with removal of some trade barriers (Pamuk, 2008:281-282; Naş, 2008:20). Turkey adopted liberal and democratic policies to benefit from Marshall Plan and admitted itself to democratic ideals while signing UN charter (Zurcher, 2004: 208- 209).

In 1952, Turkey joined NATO. Foreign policy was no more neutral. Internally, the government was hostile towards social movements. Between 1923 and 1947, the emphasis was on institutions, principles, and intellectual supremacy. While after 1947, focus was on pragmatism, individualism, and up-ward mobility (Karpat, 1964:71). In 1945, a memorandum was submitted by some members of CHP requesting political liberalization, through full implementation of national sovereignty and democracy. Inonu declared that major adjustments in political system would reflect international changes. Mass politics actively replaced single-party elites' politics (Ahmad, 2008:232). CHP gave attention to land reform, but capital was accumulated by bourgeoisie, aspiring at direct political rule to serve their interests (Bayar, 1996:777; Pamuk, 1981:27).

⁷⁷ In March 1947, Truman Doctrine was announced, and that US would support free nations and anti-communist regimes (Zurcher, 1992: 208- 209).

⁷⁸ The Marshall Plan in June 1947 helped European countries rebuild their economies. The plan promised to support Europe, ensure export markets for American industry (Zurcher, 1992: 208- 209).

After WWII, no coalition was between deprived peasants and wealthy bourgeoisie. Peasants' dissatisfaction was used by Democrat Party (Demokrat Parti) (DP) that won in 1950 (Kili, 1980:393). Etatism was heavily criticized. Lack of free enterprise was major failure of etatism, a strategy preferred by bureaucratic-military ruling class. If etatism had allowed for strong private enterprise, a larger powerful middle class would have been created. Industrial plans were not based on logic formulation; they were made for publicity purposes, focusing on political, military sources (Hale, 1980:110).

In 1946, DP was formed and promised total support for private enterprise (Okyar, 1965:104-105). DP was formed by old members of CHP, landowners, financiers, and tradesmen. The realization of poor utilized agricultural capacity and need for private entrepreneurship urged a new strategy for agriculture and liberalization. Soviet threats altered public opinion towards US⁷⁹ (Hansen, 1991: 338). Peasants knew that DP would depend on them to stay in power, and would address their interests. Landowners and industrial class believed DP would support private sector (Singer, 1977: 177). DP blamed past misdeeds on CHP. The dilemma facing DP was in office; they promised end of single party rule, but had to operate within institutions built by its rule (Ahmad, 2008:234).

DP promised to end paternalism, provide religious freedom, and support peasants and restrict etatism, focus on agricultural exports, and integrate economy into capitalist world through closer military and political ties to USA. DP removed taxes on agriculture owing to their promise; growth of GDP was 10 percent per annum for first three years, agriculture grew at 11.5 percent. Korean War increased demand for agricultural exports. However, the agricultural sector was totally neglected, although 80 percent of the population worked in agriculture. The American aid helped to build infrastructure and increase public investment. Mechanization program aimed at commercialization of agriculture in Western Turkey (Bayar, 1996:777; Pamuk, 1981:27; Kili, 1980:393; Sakallioğlu, 1992; Zurcher, 2004: 177; Singer, 1977: 178).

⁷⁹The report provided by American expert M.W. Thornburg suggested eliminating establishments such as iron and steel complex, emphasizing private sector and foreign capital, liberalizing foreign exchange and trade, and developing agriculture (Hansen, 1991: 338).

The political life began to focus on provinces that were untouched by reforms under secular culture. DP was forced by constitution to adopt principles of Kemalism, but it declared a different program based on country's needs (Ahmad, 2008:233). DP improved roads due to their military importance, but transportation needs of the industry were neglected. Agricultural machinery was imported to raise production from available farmland and cultivate more acreage. Tractors and iron plows were imported as sign of capital formation in agriculture. However, there was neglected irrigation, tertiary canals, and shortage of liquid capital and extension services (Singer, 1977: 198- 220).

Imports of consumer goods increased, because of high domestic demand. In 1953, import licensing was issued to face shortage in exchange reserves. Liberation lasted between 1950 and 1953, which was not enough for radical change in productive structure. Industry share increased to 35 percent, agriculture by 13 percent between 1950 and 1958. Until 1961/63, industry grew at 8.5 percent, and agriculture slowed to 2.7 and was no more leading sector (Hansen, 1991: 340). Private enterprises operated along with SEEs, which had a central role in industrialization (Öniş, 1991:163). Mixed enterprises were allowed to eliminate bureaucracy and salary limitations. New enterprises were of limited-liability nature with majority of capital owned by the state (Okyar, 1979:331).

SEEs intervention in political causes created more deficits covered mainly by Central Bank credit. The growth of money supply after 1953 accelerated inflation. Etatism had ad hoc manner and changed depending on conditions. It did not have its own institutional framework. However, it has been linked to Atatürk and to its role in improving Turkish socio-economic life (Bayar, 1996:777; Okyar, 1965:104-105). SEEs were to have a limited scope, and to be sold to private sector. Tax reforms were to increase social security benefits, limit government expenditures, and increase private investments. Export-license system was abolished and import restrictions were reduced. However, there was no significant record of ownership transfer of SEEs into private ownership (Singer, 1977: 179-180).

Turkey began to emphasize agriculture, mining, and infrastructure (Singer, 1977: 179). During single-party era, contracts with the state allowed for capital accumulation, created vertical links with society, and ignored horizontal links among members of same social class. Political elite with victory of DP in 1950s replaced state elite as main policy makers. However, state elite kept their social policies. Political elite reacted against state elite, which controlled economic and political sphere for years. They believed in inefficiency of state policies. Resources were used to win elections. The focus became on economic interests of parties' members rather than society. There was neither social and economic council nor private sector or labor unions to stand against parties' policies (Maxfield and Nolt, 1990:72).

Landowners had economic and social interests, which outweighed their cultural and religious interests. They did not get political support of the CHP, supporting secularism. However, they did not oppose principles of republicanism and nation-state as long as the government does not threaten their local supremacy. The government's power philosophy was bureaucratic and based on traditional approach although its intentions and form were modern (Karpas, 1964:51-53). DP created new class of industrial bourgeoisie; military, industrialists and civilian bureaucrats supported ISI to strengthen their role (Bayar, 1996:777), keep their capital accumulation (Pamuk, 1981:27-28).

DP was loyal to aristocratic elite and well-to-do farmers (Singer, 1977:210). Bourgeoisie aimed at increasing human rights and political representation (Hiç, 2009:14). Other landowners believed extra market for agricultural goods to be opened by consumer goods and textiles. Industrial bourgeoisie had captive market in urban areas; state protectionism, cheap credit, exemptions and overvalued exchange rates (Pamuk, 1981:27-28). The DP granted foreign firms rights to search for oil. The state elite was against "anti-secularist" policies and required indicative planning to guarantee rational decision-making (Heper and Keyman, 1998:264).

Turkey, a country with half of its population as peasants, rural votes were always important for political parties, political regimes were restrictive parliamentary democracy. The support by state to agricultural prices helped middle rich peasants and capitalist farmers to increase their incomes, so they were incorporated into manufacturing market (Pamuk, 1981:28).

Agriculture increased in the first half of 1950s because of equipment used by some large farmers, more hectares cultivated, short-term credits, relief from tax payments, price support programs, and road network extension. Between 1950 and 1960, 2,000,000 hectares were distributed to peasants with no land. In 1950, 72.6 percent of 2,300,000 families owned lands they cultivated, while 21.5 percent owned proportion of the land. Land holdings were fragmented and of small size, rural population was rising, and labor, new machinery were wasted due to scattered plots (Singer, 1977: 218-228).

ISI was not fully applied, as government position was linked to merchants and farmers demands. Financial system was controlled to channel resources to agriculture, but potential industrialists wanted to compensate losses in restricted consumer goods through engaging in industrial sector. They invested in different sectors, such as consumer goods. World Bank in 1953 advised an economic policy shift from agriculture to durable and non-durable domestic goods. The report stated that low level of urbanization and under-developed industrial working class was in need for policy measures (Buğra, 2007:40; Milor, 1990:6-7).

It was assumed that worker's ties with villages should be abolished, if an industrial working class was to be developed. DP followed price support systems, purchase of certain crops, and mechanization on farming. SEEs continued in irrigation, manufacturing, and transport. There was no central planning, as it was not in accordance with economic liberalism (Mehmet, 1983:54; Buğra, 2007:40). Agricultural output increased due to state policies, the distribution of lands and opening of communal pastures to poor peasants. However, the government changed its approach into a more interventionist one. The first example for a populist economic policy was adopted to redistribute wealth and income, and achieve short-term growth (Pamuk, 2008:281-282; Naş, 2008:20).

Turkey was not able to export manufactures into European protected markets. Exports of minerals such as chrome iron and oil increased. There was mutual agreement on importance of foreign direct investment and foreign aid. Credit policies were criticized as reason for inflation and that funds should be diverted towards productive industries. DP supported commercial interests closely tied to agricultural sector, so urban industrialists did not support it (Maxfield and Nolt, 1990:60-62; Karasapan, 1986:31).

In 1953, world prices for agricultural products declined and trade deficits increased, lower exports output by 15 percent, per capita income decreased by 11 percent. It was a paradox, agricultural commercialization for increased growth, and negative effects of world crisis. Gap between demand of imports and foreign exchange revenues, trade controls were imposed, freezing credit importation and restrictions on international transactions and imposing import licenses. The government began effective protection in urban industrial sector, incentives to meet domestic market demand, imports on consumer goods, led to growth of industry from 11.8 percent to 16.3 percent in 1952 until 1957, and agriculture declined from 43 percent to 38 percent (Milor, 1990:6-7).

Between 1951/53 to 1955/57, average yields decreased by 20 percent. The incremental yields declined because of expanded crop area by one-third. In the second half of 1950s, crop, and cultivated areas stagnated, so growth of agricultural GDP declined. The stagnation of yields during 1950s was weakest point in DP era. The efforts should have been on increased cultivation of farmlands and cultivate new areas. However, neither CHP nor DP considered this possibility (Hansen, 1991: 263-344).

USA and World Bank helped establishment of Industrial Development Bank of Turkey to fund and supervise industrial projects. Most of funds were to commerce and construction, rather than industry, subsidies for agricultures that are sold at prices lower than market prices. DP government kept its economic boom, through short-term borrowing and bilateral economic aid, the large agricultural projects were receiving funds although shortage of foreign credit sources. There was pressure from IMF, USA, and OECD to adopt different economic policy planning to rationalize public investments, control macroeconomic balances of economic growth and use foreign aid adequately. Projects selected on basis of their contribution to balance of payment, with no criteria for selection, so it was a “project-by- project” basis, with no coherent goal and direction (Milor, 1990:10-11). American aid was helping factor in creating middle class, involved in commercial work. After the republic, middle class was formed from wealthy families, which were close to the state, so their position was not challenged (Karpat, 1964:67).

USA proposed a plan focusing on agriculture, credit, foreign exchange rates, and trade. It proposed farm prices to be lowered through increasing cost efficiency, but Turkish government offered price supports to farmers. Although agriculture somehow improved, average efficiency decreased and price-support system led to increased expenditures. Turkey became major wheat importer after it was a major exporter. By 1954, cereal output declined, agricultural production declined by 14 percent, and GNP declined by 3 percent (Singer, 1977:196; Maxfield and Nolt, 1990:60-62; Karasapan, 1986:31).

Price support programs and subsidies increased inflation. Exports were of high cost (Singer, 1977: 222). In 1956, stabilization program prevented financing from Central Banks to SEEs, allowed financing through own funds or normal banks (Maxfield and Nolt, 1990:60-62), devaluation, liberalization of imports, raising SEEs' prices, and limiting expenditures (Bayar, 1996:777; Okyar, 1965:104-105). The program was based on standby agreement with IMF to lower inflation and increase exports. (Pamuk, 2008:281-282; Naş, 2008:20). Prices of SEEs goods increased in 1958. Therefore, one-and-for all price increase occurred, credit by central bank declined and inflation dropped from 25 percent in 1958 to less than 5 percent in 1959 (Metin, 1998:413).

Economic assistance fostered Anti-Americanism⁸⁰. It was believed that Democrats would keep power, help new middle class be powerful, and harm former bureaucratic-intellectuals. The Cold War enhanced position of the army and its supremacy. Others believed that strategic importance of Turkey would diminish gradually because of development of new weapons, as Turkey hoped for continuous war. The exploitation of West-East conflicts for serving Turkey's economic interests would hurt its world position, and eradicate its influence among newly rising nations. There was close attention from Soviets to social and economic developments in Turkey, on the hopes that public attitudes would be changed towards socialism (Karpas, 1964:71-72).

Criticism of DP was related to absent long-term perspective in economy management (Pamuk, 2008:281-282; Naş, 2008:20). Although services and manufactures increased during 1950s, it was insufficient to provide employment for urban migrants. Mechanization displaced workers (Singer, 1977: 208).

⁸⁰Anti-Americanism increased in 1960s due to Vietnam War and intervention in Middle East (Ahmad, 2008:246).

DP managed to mobilize lower social groups. Power was not in elite support, but in masses. DP followed incentives as welfare projects, credits, and cancelled agricultural taxes. Some criticized unplanned economic policy, imbalanced income distribution, inadequate tax policy, and reward system favoring their followers. However, it cannot be denied that DP's economic policy created more dynamic economy; million jobs were created in transportation, machine maintenance and small industries, value of land increased, facilitated credit, and new opportunities were discovered (Karpas, 1964:67).

DP lacked elements of autonomous political institutionalization. This was translated into public policies lacking rationality. Moreover, coalitions were based on short-term considerations. Parliamentarians attempted to keep spoiled operations through benefit networks building. This means personal relations were more important than expertise (Heper and Keyman, 1998:263). DP did not allow labor much freedom. Unions were dependent on the party, politicizing unions, making state money disbursements a right for close unions and brutal reactions to any strikes for 10 years. They controlled large portion of economic activity and granted special patronage to their supporters. The system of protective tariffs favored certain groups (Owen, 1992:86; Blind, 2009:42; Sakallioğlu, 1992:714; Zurcher, 2004: 177).

3.4. ECONOMIC PERFORMANCE IN 1960s AND 1970s

There was social unrest, but relative political stability. DP's government was overthrown by military coup in 1960⁸¹. It was a revolution of intellectuals, involved in writing constitution. CHP was trusted by the military government because of linkages to the army, and opposition to DP. In 1963, Justice Party (AP) won elections. There were calls for institutional and constitutional reforms. A new state was recommended in terms of social institutions (Ahmad, 2008:239-240; Karpas, 1964: 50-51).

⁸¹ The Committee of National Unity (CNU) was formed, and six months later control of government was guaranteed to council, consisting of 67 army commanders and then included civilian government (Ahmad, 2008:239-240; Karpas, 1964: 50-51).

The Constitution⁸² in 1961 emphasized planning to achieve economic goals. Political elite was not expected to intervene in socio-economic planning, and promised social and economic individual rights (Heper and Keyman, 1998:264). During 1962 and 1963, Turkey had basic conditions for sound economic development. However, impediments were lack of objectives and social causes (Karpas, 1964:50-51). The state had large role compared to other countries undertaking ISI, dominant state in strategic sectors such as manufacturing industry and investment, with share of 40 percent and 50 percent during 1960s and 1970s (Boratav, 1986, 125).

In 1960s, planning was a mix of social alliance among reformist wing of bureaucracy, civilian, and military. CHP shifted to left after 1960 because of bureaucracy. Planning was opposed by some social groups for political reasons. Non-industrialist business groups and ministries feared changes to their operational scope. By 1960s, working class was still not a political actor (Milor, 1990:5-6; Karpas, 1964:56-58).

In 1961, a “Declaration” signed by 160 intellectuals and published in *Direction* (Yön) magazine proposed a brand of socialism, advocating state ownership and economic planning. The program was not known as socialism, but rather as new concept of etatism. This group attacked etatism as form of capitalism, which oppressed working class and served industrial bourgeoisie, and that nationalism and populism were used to mobilize masses and hide nature of capitalism. The state was part of struggle among classes, rural local notables such as landowners, and mercantile bourgeoisie. The state did not escape conflict with landowners about land reform, so land redistribution plans were quitted until 1945 when abortive land reform law was issued. Meanwhile, bourgeoisie was important partner in industrialization process, which normally ignored agriculture (Hale, 1980:112).

⁸²In 1961 Constitution, there were attempts to re-institutionalize politics and state through the National Security Council, the Constitutional Court, the State Planning Organization, and the Council of State (Heper and Keyman, 1998:264).

A consistent program for ISI was set up by military government. There were five-year development plans drawn with help of USA and Europe. It was expected to eliminate agricultural subsidies, impose more taxes on land, and devalue TL. However, USA did not have the major power in shaping Turkish experience of ISI due to its small role of trade and investment in Turkey (Maxfield and Nolt, 1990: 60-62).

The military government built State Planning Organization (SPO) to centralize economic interventions, implement ISI, manage central economic planning⁸³, and allocate foreign exchange. SPO had to approve all investments to benefit from subsidized credits and tax exemptions, cooperate with Undersecretaries of Foreign Trade and Treasury (UTFT) in controlling and managing trade policy. Exchange rates devaluation aimed at accelerating exports, gradual management of liberalized trade. Tax holidays, credit provisions, custom exemptions, and investment incentives were provided by the state (Pamuk, 2008:283; Owen, 1992:86).

SPO was a planning agency to create a market free of exploitive agrarian and merchant interests, and support the market if failed to allocate capital in high-value added fields. It was to imitate autonomous technocratic Western institutions (Pamuk, 2008:283; Owen, 1992:86; Milor, 1990:2-3; Adly, 2013:30-31). The focus was maintained on ISI and inward-looking strategies. SPO was responsible for planning under the High Planning Council. Both long-term programs and medium-term five-year plans were drawn. The five-year plans were 1963/67, 1968/72, and 1973/77. A fourth plan in 1977/79 was delayed because of foreign exchange crisis. The SPO after elections of 1965 employed technological planning, which relied on engineers with little concern for economic efficiency (Hansen, 1991: 352-361).

⁸³ SPO used "planning by stages" technique. A macroeconomic stage was set, followed by a sectorial/regional stage, and then a project appraisal stage, in which concrete investment projects filled sectorial investment targets. Based on Keynesian model, macro stage was drawn. Sectorial stage used Leontief's input-output model. Finally, project appraisal phase used ad hoc evaluation method, which was committed to shadow prices, but had no real conception on how to realize them (Hansen, 1991: 360-361).

SPO drew up a fifteen-year development plan in (1963-1977) to address long-term economic problems systematically. Investments were inefficient and productive capacity of the economy did not increase. There were goals related to agriculture: increase output to meet industrial demand for raw materials, end stranglehold of agriculture, and expand agricultural sector. The plan was expected to achieve this 7 percent growth (Karataş, 1977:4). SPO stipulated investment shares for private sector, while public sector failed to accumulate adequate capital. Agriculture sector was under-taxed, so taxes were increased (Karpaz, 1964:69). Political pressures prevented SPO autonomy; it could have made centralized economic decisions to reduce intra-bureaucratic conflicts (Milor, 1990:2-3).

Between 1963 and 1967, Turkish external debt was \$ 1 billion. The Plan in 1962 was approved by Parliament. The plan was not only product-oriented, it aimed at long-term goals such as balance in external payments, increased number of technical personnel, social equality in income and welfare. It was proposed to reach 7 percent of annual growth rate in GNI, from 52.7 billion TL to 145.3 billion TL in 1962 and 1977 respectively. Real savings were expected to increase through limited consumption and reallocation of resources (Karataş, 1977:4).

The state supported private business by offering incentives and enhancing global competitiveness. Clothing and textile industries expanded, as they were labor intensive. In 1959, Turkey applied to European Community access. In 1969, Ankara Association Agreement was signed to offer more eventual membership chance. However, Turkey was not able to win full access to European market, due to custom duties on sensitive commodities in European countries. The existence of quota system on textiles and clothing constituted 2/3 of manufactured Turkish exports. Turkish exports were heading to Middle East rather than Europe, as other developing countries joined European Community. Therefore, the preferential treatment was offered to other countries as well (Adly, 2013:12).

The economic and social change process was fast; industrialization, labor migration, and urbanization increased. It created new social strata of militant workers, and linkage between government and interest groups, in terms of political and electoral terms. AP formed a government of its own order. Planned economic development process was due to multiplication⁸⁴ of conflicting economic interests that cannot be represented by a single party (Owen, 1992:86-87). There was expansion of rights and liberties scope in Constitution to protect state elite. There was increased power of peasants and their bargaining power (Heper and Keyman, 1998:267).

Post 1960s, government and private sector were complementary, SEEs losses were financed by central bank, they operated in traditional areas and areas in which private sector was weak (Arıcanlı and Rodrik, 1990:1345). Industry share was 16.2 percent in 1963-1967 and became 22.6 percent in 1968-1972. Heavy and capital intensive industries increased. However, high salaries to get political support led to deficits in SEEs, so external debt increased, and money supply increased. In 1977, 66 percent devaluation in TL occurred, remittances of immigrants created a current account surplus, and foreign exchange inflows were high. In 1973-1977, the third five-year plan was made to create growth of 14.2 percent in industrial sector, investment 13.8 percent and GDP growth of 7 percent. The growth rates declined after 1973 due to global slowdown economy (Bayar, 1996:777).

Easy stage of ISI was from 1963 until 1977. Domestic market provided some opportunities, but ISI did not move to stage of complex technology. Although there was income inequality, many population segments like civil servants and workers were incorporated in consumer durables market. Real wages doubled due to political and institutional changes. Labor worked in Europe; they had constitutional right, and their wages were easily increased by large industrial firms, which did not face pressures for export competition. The ignorance of exports of manufactures was a factor behind weak ISI. Export encouragement was expected to increase efficiency and competitiveness of industrial structure, provide foreign exchange, support ISI, and create backward linkages towards more complex industries (Pamuk, 2008:283-284).

⁸⁴During 1960s and until 1973, polarization of party system was clear; both leftist CHP and rightist JP, NSP were forced to form a coalition with smaller parties. The National Action Party and Islamist National order party were established (Owen, 1992: 86-87).

In 1960s, 76 percent of employment was in agriculture, but low productivity and stagnation. ISI was biased against agriculture along with overvalued exchange rates. During 1960s the economic system was near *laissez faire*; between 1963-1967, GNI growth was 6.4 percent, 6.7 percent between 1968 -1972, 7.2 percent between 1973-1977 during three consequent five plans. Turkey achieved higher than average 6 percent GNI growth rates for countries in same low middle-income category (Çeçen *et al*, 1994:38; İmrohoroglu and Üngör, 2013:3).

Between 1963 and 1970, ISI had positive performance, which turned negative between 1971 and 1977. Whereas one third of output growth rate was caused by technological change, the share of labor in agricultural sector declined from 77 percent in 1962 to 61.8 percent in 1977, and in manufacturing sector increased from 7.2 percent to 11 percent and from 15.1 percent to 25.6 percent. Persistent unemployment was caused by relatively slow growing manufacturing sector. Moreover, exchange rates and interest rate policies along with high tariffs and quotas diminished optimal capital intensiveness (Çeçen *et al*, 1994:40-41).

Between 1963 and 1978, SEEs subsidized private sector's inputs through price deregulation and capital accumulation. However, there were no autonomy and managerial incentives in SEEs, politicians and bureaucrats intervened, managerial elite was not encouraged to produce efficiently, monopolistic and oligopolistic market structure existed. In 1977, about 44 percent of public sector investment was done by SEEs, but their contribution to GDP was 7 percent, same percentage since 1967 (Mehmet, 1983:56; Öniş, 1991: 164).

During First Plan, there was virtual ban on imports of consumer goods, so substitution was for intermediate goods. Industry improved in intermediate and capital goods, although growth was slow. In 1975, unemployment rates were high because of slow growth in construction and manufacturing, decline of investments and exportable goods. The structure of imports did not change or decrease dependency on imported capital goods. In 1968, exports exceeded set targets by 10 percent in First Plan period; this was because of world price increases, good quality crops, tax rebate system, and exports of processed goods (Karataş, 1977:7-8).

The Third Industrial Plan was drawn in 1973 until 1977; based on heavy foreign debt, and lack of foreign reserves. The country did not realize balance of payment surplus through internal adjustments. ISI in energy and manufactures was negatively performing (Richards and Waterbury, 1990:322). In the fourth Five-Year Plan in (1979-1983), there was proposal to reorganize SEEs into sector-holding companies, change organizational structures and pricing decisions, Turkey had strong bureaucracy and state tradition, which influenced pace of public-sector reform (Öniş, 1991:164-165).

The dependent nature of ISI was evident when it moved towards intermediate goods industries, through importing technology and plants. Foreign exchange reserves decreased and right government coalitions needed short-term loans, under unfavorable terms. ISI in Turkey generated profits due to large domestic market, high tariff protection, and state intervention (Pamuk, 1981:29). However, ISI did not generate enough foreign exchange, because of slow growing exports, increased imports of intermediate goods, high food consumption, gap between investments and savings, inequality between rural and urban areas, and high unemployment (Richards and Waterbury, 1990:248).

The unequal allocation of investment resources to sectors was a problem; most of investment targeted manufacturing, construction, transportation, and communication sectors. Technological changes due to new production technologies improved labor quality (Çeçen *et al*, 1994:41-42). The bureaucratic state was providing subsidies to entrepreneurs: rent-seeking behavior in business was common; incentives for business makers were to access cheap credit and foreign exchange, and import final and intermediate goods. Therefore, a form of distributional coalition emerged between state and business makers (Demir, 2005:669-670).

ISI helped in accumulation of industrial capacity and it led later to success of free market policy: active exchange policy, austerity at home, and subsidization. Liberalization came later, so its effects were minor on exports. Export subsidies were main factor of success. Investments were negatively affected due to high interest rates and fragile financial sector, distortions in social and political context caused by price adjustments (Arıcanlı and Rodrik, 1990:1349).

The complex stage of ISI required highly trained labor and advanced technologies for efficient production. Absence of these factors negatively affected growth rates; oil crisis and high dependency on capital imports and intermediate goods were factors to consider. The government kept its expansionary policies despite first oil crisis in 1974 and deteriorating terms of trade (Çeçen *et al*, 1994:37).

ISI failed after 1973. Internal domestic political conditions: high inflation, Cyprus invasion, increased real wages (Hansen, 1991: 353-367), foreign debts, balance of payment deficits, decline in worker remittances, stagnant exports, exhausted foreign reserves, high interests on debts and import bills created a crisis in 1970s (Çeçen *et al*, 1994:37). After 1975, increased political instability and terrorism were about creating a civil war. The experience of Turkish industry to compete internationally was mature. There was needed a shift in policy, to remove overvalued currency and bias against exports. There was internal opposition from workers fearing downward pressures on wages and industrialists opposed as well (Pamuk, 2008:284-285; Mehmet, 1983:55).

Table 4 shows the structure of manufacturing sector in Turkey. It reflects a declining share of consumer nondurables from 66.7 percent in 1963 to 39.8 percent in 1980, and consumer durables increased from 4.4 percent to 10.1 percent. Intermediary goods increased from 20.5 percent in 1963 to 42.6 percent in 1980, while capital goods declined from 8.4 percent to 7.5 percent. The table shows a declining share of employment in all sectors between 1963 and 1980. Employment share declined from 65.4 percent to 54.2 percent in consumer non-durables, 3.7 percent to 11.1 percent in consumer durables, 28.7 percent to 24.8 percent in intermediary goods, and 12.2 percent to 9.9 percent in capital goods. This reflects the fact that ISI between 1963 and 1980 increased output of intermediary goods and consumer durables, while consumer nondurables and capital goods declined. Moreover, employment declined due to capital-intensive ISI process (Boratav, 2003:133).

Table 4. Structure of Manufacturing Sector in Turkey, 1963, 1980

Shares of value of Production %					
Years	Consumer Non-durables	Consumer Durables	Intermediary Goods	Capital Goods	Total
1963	66.7	4.4	20.5	8.4	100
1980	39.8	10.1	42.6	7.5	100
Share of Employment %					
1963	65,4	3,7	28,7	12,2	100
1980	54,2	11,1	24,8	9,9	100

Source: Boratav, (2003:133).

Table 4 shows the structure of public industry for years 1963 and 1980. Share of public investments in consumer nondurables declined from 53.3 percent to 29.2 percent, capital goods from 9.8 percent to 6.2 percent, and consumer durables from 0.4 percent to 0.1 percent. Only intermediary goods share increased from 36.5 percent to 64.5 percent. Shares of employment in capital goods declined from 18.7 percent to 10.5 percent, in consumer nondurables from 57.0 percent to 53.9 percent. Employment share in consumer durables increased from 0.2 percent to 2.3 percent, and in intermediary goods from 24.1 percent to 33.3 percent. This shows increased role for SEEs in production of intermediary goods, and increased share of employment (Boratav, 2003: 133).

High inflation and unemployment, labor unrest and political violence were factors postponing SAPs by the government to preserve economic growth, but this took place through foreign borrowing. Devaluation, import restrictions, and austerity programs meant a need for real reform (Beysan and Blitzer, 1990:9). Pressures by IMF aimed to reduce inflation and unemployment. There was difficulty in importing necessary goods for industry, which operated under full capacity. The inflation reached 100 percent in 1980, oil shocks, real wages declined, income inequality increased, increased labor supply and less demand, unemployment grew at 5.4 percent annually between 1977-1980, stagflation occurred (Bayar, 1996:778).

Table 5. Structure of Public Industry in Turkey, 1963, 1980

Shares of value of Production %					
Years	Consumer Non-durables	Consumer Durables	Intermediary Goods	Capital Goods	Total
1963	53.3	0.4	36.5	9.8	100
1980	29.2	0.1	64.5	6.2	100
Share of Employment %					
Years	Consumer Non-durables	Consumer Durables	Intermediary Goods	Capital Goods	Total
1963	57.0	0.2	24.1	18.7	100
1980	53.9	2.3	33.3	10.5	100

Source: Boratav, (2003: 133).

The share of agriculture in total output declined to 23.3 percent in 1977 after it was 38.4 percent in 1962. On the other hand, manufacturing sector had an increased share from 22.3 percent in 1962 to 31.5 percent in 1977. However, absence of expected outcomes was owing to inability of expanding manufacturing sector to create employment opportunities (Çeçen *et al*, 1994:38). Protection rates were high: 68 percent in 1979, 80 percent of imports had quantitative restrictions, unemployment rate in 1979 was 1.5 million out of 16 million (Richards and Waterbury, 1990: 248).

In late 1970s, Turkey faced a debt crisis when it suffered from increasing rates of imports and declining exports revenues. The state policies supported imports through over valuated exchange rates, increased industrial imports, and terms of trade declined (Richards and Waterbury, 1990:247). Negative GNI growth, three digit inflation, and high unemployment created social unrest and political instability, which ended by military coup in 1980 (Çeçen *et al*, 1994:44). Worsened economic conditions created need for 1980 coup (Pamuk, 1981:27).

The debt crisis was high in political emergency and economic magnitude; there was a threat of bankruptcy, so the government attempted to reschedule its debts with creditors and demanded relief from OECD countries. Turkey kept expansionary policy and was detached from European economies. Budget deficits were financed by short-term debts from European banks under guarantee of exchange rate by government (Arıcanlı and Rodrik, 1990:1344; Mehmet, 1983:55).

Table 6 summarizes GDP in constant prices by economic activity in the period between 1968 and 1980. It shows a steady decline in agriculture share from 33.5 percent in 1968 to 24.8 percent in 1980, and growth share was 1.1 percent in 1980, with negative growth rate of -1.2 percent in 1969. Moving to industry, it had an increasing sector share from 17.8 percent in 1968 to 22.0 percent in 1980, and growth share of 12.1 percent in 1969, turning to negative share of -3.3 percent in 1980. Finally, the manufacturing industry shows an increasing sector share from 15.1 percent in 1968 to 16.1 percent in 1969, and decline until 1972, after which it slowly the sector share was 17.4 percent in 1973, and reached 18.3 percent in 1980. Annual growth in manufacturing sector was 11.7 percent in 1969 and -3.9 percent in 1980. As shown, agriculture share declined due to state policies and focus on ISI. However, industry annual growth was declining, and same holds for manufacturing industry (TÜİK).

This crisis was an uncontrollable shock to Turkish economy, because it had trade relations with EU. Therefore, Turkish exporters suffered from low demand from European market with which it has a customs union. Turkish trade policies had high change rates. Therefore, high degree of uncertainty existed about access to Turkish market by foreign investors. Turkey had a duty free two-way trade with EU except in agricultural products (Bown, 2014:193). By late 1970s, policy shift was to export-oriented policy.

Table 6. Turkish GDP in Constant Prices by Economic Activity at 1987 Basic Prices

Agriculture			Industry		Manufacturing Industry	
	Sector Share %	Growth Share % of agricultural output	Sector Share %	Growth Share % of industrial output	Sector Share %	Growth Share % of manufactures output
Year						
1968	33.5	-	17.8	-	15.1	-
1969	31.7	-1.2	19.1	12.1	16.1	11.7
1970	31.2	2.8	18.5	1.3	15.7	1.6
1971	30.7	5.2	18.9	9.0	15.9	8.7
1972	28.4	1.1	19.1	10.4	16.2	10.9
1973	25.0	-7.8	20.3	11.9	17.4	12.9
1974	25.7	6.3	21.1	7.3	18.1	7.3
1975	25.0	3.1	21.7	9.1	18.5	8.7
1976	24.6	7.0	21.7	9.0	18.5	9.0
1977	23.4	-1.9	22.6	6.9	19.2	6.6
1978	23.8	2.8	23.0	3.4	19.6	3.2
1979	23.9	0.0	22.1	-4.4	18.5	-6.1
1980	24.8	1.1	22.0	-3.3	18.3	-3.9

Source: TÜİK

3.5. MOVEMENT TO FREE MARKET ECONOMY (1980s)

Turkey had lax fiscal-monetary demand management and problems remaining from ISI. This made radical turnout in development strategy inevitable (Hansen, 1991:258). Turkey had a developmental state, where state owned major means of production, and some tolerance for small and medium private enterprise (Waterbury, 1999:333-334). Turkey adopted set of economic restructuring policies, shrinking role of government in economy and democratizing the political system. The economic reform was based on neo-liberalism and rationality assumptions. Whereas, the political reform was based on irrationality assumption, people were assumed unable to determine their fate and still not ready for democratic elections (Demir, 2005:669-670).

Other factors were clashes between industrial, commercial, and agricultural interests, threat of giant business owners (Karasapan, 1986:31). However, political competition for party votes among coalition governments might have benefited the economy, as each party has attempted to preserve social base through higher expenditures. Although the norm was austerity programs, high expenditures were a means to keep power (Arıcanlı, 1990: 235-236).

Party competition initiated distributional pressures, which could not be contained by the government. Moreover, fiscal deficits and high inflation, the government ignored structural economic deficiencies. The focus was on capital infusion as engine for growth (Öniş and Rubin, 2003:6-7). Coalition governments created instable regulatory policy, caused by political bargaining and problem of principal agent. Rents were extracted by interest groups. There was high transaction cost. Coalitions were short-lived. Policies toward industries were in conflict. Government could not control these conflicting views on state role (Çetin, 2010:40).

In 1980, the military government pursued a stabilization program by IMF. Exports reached \$ 8 billion in 1985, after \$ 2.9 billion in 1980. Inflation became 40 percent, real wages declined and small companies went bankrupt (Karasapan, 1986:31). SAPs focused on contractionary macroeconomic policies (Metin, 1998:420). It was the start of neoliberal reforms, aiming at short-run stabilization and long-run structural adjustments, through collaborative efforts between World Bank and IMF (Öniş and Rubin, 2003: 4-5). Between 1980 and 1984, World Bank guaranteed five loans. After 1980, budget financing for SEEs decreased. Organization and implementation of privatization became major responsibilities of SPO (Öniş, 1991:166).

ISI was hard to remove due to many groups with different interests. In a country with large domestic market, a shift in economic policy requires strong government with autonomy and long-term horizon. However, this was not the case in Turkey. The new government implemented the new program package to establish market-based economy. Economic changes were uncertain due to arbitrary matter and services provided for groups close to the government (Pamuk, 2008:285).

When the government began to focus on producing intermediate and capital goods, import tariffs and foreign exchange overvaluation increased imports of raw materials and machines (Richards and Waterbury, 1990: 247). Initial devaluation in 1980 was kept by downward trend to face inflation and create depreciation over time in real terms (Arıcanlı and Rodrik, 1990:1343-1344). In 1982, a new constitution was adopted. The reform in 1983 promised to address social problems that have been neglected so far. It signaled first time to define set of policies that would transform the economy and government relations. The plan included these elements: realistic flexible exchange rates, effective export promotion, sequential import liberalization, through rational tariffs and removing quantitative restrictions, better management for external debt and information system, lowering inflation through tight monetary controls, higher private savings through deregulated interest rates and privatization efforts (Baysan and Blitzler, 1990: 10-11; Hansen, 1991:383-385). In 1983, Motherland Party under Turgut Özal came to power. The political system was isolated from military that had to look after domestic security. The party came with coalition of politicians, religious, and nationalist groups, so it was highly appealing (Owen, 1992:88).

The devaluated Turkish Lira in period between 1979 and 1986 through a crawling peg system fell by 2000 percent against US dollars. Exports to MENA were 22 percent in 1980 (Richards and Waterbury, 1990:248). Economic decisions were rational and according to market signals. The government exerted less control over private sector, and efficiency and entrepreneurship were encouraged. Percentage of exports/GDP increased from 4.9 percent to 20.9 percent in 1979 and 1985 respectively. Annual economic growth was 5.3 between 1981 and 1985. In 1986, inflation reached 29.6 after it was 108 percent in 1980 (Heper and Keyman, 1998:266).

SEEs began price adjustments to reflect real costs. Basic goods such as bread and sugar were subsidized. Agricultural prices followed world prices through market-oriented approach (Hansen, 1991: 388-390). Export subsidies were announced, tax rebates, export credits, retention of foreign currency, banned layoffs, along with foreign capital inflows increased imports, so manufactures were in excess condition (Arıcanlı and Rodrik, 1990:1345).

Turkey changed its economic policies to join the European Common Market (Richards and Waterbury, 1990:322). Focus on exports was to achieve surplus in balance of trade, encourage private investments, and remove government control over agricultural goods. Exports increased due to Iran/Iraq War (Owen, 1992:88).

Active exchange rate policy and import liberalization were to promote exports, rather than pure export subsidies. Import liberalization was gradual, as rapid liberalization would increase balance of payment problems and unemployment. Therefore, import procedures were simplified, and explicit import quota was abolished (Baysan and Blitzer, 1990:13-14). Industry was restructured, with high protection rates in exporting and sensitive sectors. Raw material exports converted to manufactured exports, expanding economic institutional capacities, changes in state-business trade coordination modes, and filling state agents with highly skilled technocrats. Incentives for exporters were provided to reorient manufacturing sector outwardly. Highest effective protection rates were devoted for exporting industries rather than import/ non-import competing industry (Adly, 2013:30-31).

Fiscal discipline increased political competitiveness after 1983. Inflation fell to achieve trade equilibrium, cancelled quota list, reduced advanced deposit requirements on industrial imports, granted tariff exemptions on intermediate goods imports, and foreign exchange market was established in 1988 (Çeçen *et al*, 1994:46; Bayar, 1996:780). In 1984, there was a law on goods not be imported, being under license, versus all goods without specification are prohibited. The positive list turned into a negative list, which reduced quantitative restrictions (Arıcanlı and Rodrik, 1990:1345-1346).

During 1980s, Turkey was first among countries in export growth, with manufactures accounting for 80 percent. Dominant exports were textiles, exports, iron, and steel (Pamuk, 2008:286). Turkey was highlighted as success model by IFIs. It increased exports of manufactures (Öniş and Rubin, 2003: 4-5). Turkey was a good example for SAPs. That is why debt was rescheduled and new inflows of resources occurred, which lessened inflationary pressures and foreign exchange constraints. Influence was mixed, because private investments did not increase as expected, high political instability and interest rates, absence of new investments, and it was rather expansion of existing industries (Pamuk, 2008:286).

Export-led growth strategy was successful. The transition experience of Turkey can be aspired for by LDCs with similar strategies. Indeed, reform was costly to Turkey because of institutional structure, which limited its success in economic changes. Economic change and its direction in the long term depend on institutions, to analyze economic change; institutions reduce uncertainty in economic, political, and social life, through maintaining commitment and less transaction costs (Çetin, 2010:3). The adopted populism delayed privatization and undermined its objectives (Asutay, 2010:115). Interest groups in regulated economies shape and influence outcomes of public policy. They receive government transfers and wealth (Demirbaş, 2010: 128).

The coup in 1980 and Cyprus invasion in 1973 negatively affected Turkey and Europe relations; in 1980 Turkish exports to Middle East was 17 percent and 40 percent in 1984. Between 1980 and 1985, 45.5 percent of Turkish total exports were due to diversified markets towards Middle East. However, after 1986 oil crisis, Turkish exports targeted European markets, with 46.7 percent of exports and 51.2 percent of imports (Adly, 2013:12).

Bourgeoisie was technologically and financially dependent on foreign capital and state support. Therefore, they were never able to develop hegemony over financial capital. Industrial bourgeoisie was dependent; they left market-oriented industry to rebuild their linkages to international capital. IMF delayed payments and gave credit to import other intermediate goods. When crises occur, new ruling classes emerge and break the old alliances, so new coalitions and linkages to international capital emerge (Pamuk, 1981:30).

Table 7 shows that policy changes in Turkey were based on “top down” approach, rather than social consensus, and they were response to international economic events. The state was reactive, rather than proactive (Öniş, 2003: 3). Crises were based on balance of payment crises owing to deficits in current account. These crises were created by fiscal imbalances, export stagnation, and trade deficit. The crisis in 1958/59 was caused by falling world prices for agricultural products. On the other hand, crisis in 1978/78 was caused by oil shocks and internal imbalances. The IMF and World Bank were active actors post-crisis, through stabilization programs (Öniş, 2003: 4-5).

By the end of 1980s, there were attempts to fulfill demands of major social groups, low tax burden supported industry, wages rose, and high prices for agricultural products existed. The current expenditures took much of funds so that no much was left for public investments. There were restrictions to trade unions and labor's bargaining power. There was high concentration of power, which made it difficult to coordinate between state and business. There was some resistance to privatization and tax reforms. This led to crisis in 1994 (Heper and Keyman, 1998:269).

Regulatory processes started in 1990s. Turkey delayed its transition process, so it was not able to undertake the initiative alone. There was no separation of power among institutions. Therefore, regulatory institutional change was done under external pressures. State's role in the market was not weakened by privatization, which was a means to generate income, while controlling enterprises (Çetin, 2010:34-41).

The political authority assumed low responsibility towards social assistance. Turkey had the military, economic, and legislative powerful institutions. However, it lacked transparency and accountability, leading to democracy gap. Moreover, there was lack of funds, and differences between lending and borrowing interest rates, and strict rationing of credit deferred long-run investments. The transition in 1980s led to capital account liberalization, which created short-term crises in years 1994, 2000, and 2001 (Demir, 2005:672; Şenses, 2003: 92).

Table 7. Characteristics of Economic Crises in Turkey

	1958/1959	1978/1979
Nature of the crisis	Balance of payments crisis originated from the current account, primarily caused by domestic imbalances.	Balance of payments crisis originated mainly from the current account, caused mainly by domestic imbalances.
Origins	Fiscal imbalances; steady appreciation of the real exchange rates; export stagnation and rising trade deficit	Fiscal imbalances; steady appreciation of the real exchange rates; export stagnation and rising trade deficit; distorted production and trade structure caused by ISI
External dimension	Peripheral; falling world demand for agricultural products in the latter half of the decade.	Successive oil shocks have contributed to the crises; oil shocks largely aggravated the problem created primarily by domestic imbalances.
International actors in the post-crisis context	IMF is the dominant actor in the post-crisis period: a typical short-term stabilization program.	Both IMF and World Bank are heavily involved; official assistance through the OECD is also important.
Political consequences	Collapse of the democratic regimes; Restoration of democracy occurs over a relatively short period.	Collapse of the democratic regime; longer military rule. Restoration of full or unrestricted party competition occurs over a longer period.

Source: Öniş (2003: 4-5)

3.6. IMPLICATIONS AND CONCLUSION

As explained, Turkey witnessed some rounds of institutional changes. First, replacing the Caliphate with Republic in 1923 and modernization. Second, capitulations expiry and setting protectionist tariffs in 1929. Third round was in 1946, when multiparty system was introduced. Fourth round was in 1961 Constitution that rebuilt parliamentary democracy, started economic planning, and legalized labor unions.

The fifth round was after 1978 crisis and dismantling of etatism, and adopting export promotion (Hansen, 1991: 421-424).

Turkish political life had some unique characteristics among LDCs. First, except for coups in 1960 and 1971, multiparty democracy was enjoyed since 1946. In 1960, military claimed that DP departed from Kemalism. In 1971, the military mentioned in the “memorandum” that government failed to modernize in ways in accord with Kemalism. Kemalism emphasized civilian government, and Turkish army included lower-middle class that had no ties to large landowners (Kili, 1980:394).

Turkish economic system has some ideological and structural contradictions, which emerged during establishing industrial and economic base. Turkey stayed more than fifty years to reach sustained growth take-off depending on SEEs. It was the oldest developing country that achieved development through planning (Owen and Pamuk, 1998:28; Mehmet, 1983:47-56). State interventionism in Turkey was not successful. It focused on profits in private industry, and how to keep them higher than world market levels, there were no changes in efficiency or competitiveness. Uncompetitive market forces prevented new entrant (Milor, 1990:26-27).

There was conflict between etatism emphasizing role of the state, and its inactive role in achieving social welfare. There was focus on economic and political priorities. Sociopolitical concerns shaped economic expediency until 1980s (Buğra, 2007:35). Kemalism was mixture of collectivism and individualism based legislation and policies. The military officers had low connection to lower classes and they came from modern educational background, they had secular, nationalist, etatism and anti-religious ideology, but weak social orientation. Kemalism was seen by political economists as elitist ideology that Turkish masses never understood (Hansen, 1991: 425-426).

Changes in rural structures were accompanied with increased poverty, caused by capitalist developments (Buğra, 2007:35). In Turkey, policies were imposed from above on indifferent nation, Kemalism did not mobilize people to reach its goals, and even speeches of Atatürk were not before mass rallies. Moreover, there was no ‘leader principle’ based on single powerful leader’s legitimacy. Finally, there was no military rhetoric and expansionist propaganda in Turkey, as leaders had realistic and defensive policies (Zurcher, 2004:189).

The middle class emerged in late 19th century, and included intellectuals, bureaucrats and military. Subordinates were service groups, small entrepreneurs. In 1950s, the lower economic groups were more powerful in party organization and in local provinces, so they were influential on the government, so military and intelligentsia were in secondary position. This was a reason for socialism taste in etatism, and an economic social meaning to class. Economic groups were attacked by social reforms and etatism; they opposed welfare measures and state intervention as means of bureaucratic domination and dictatorship (Karpat, 1964:57-58).

DP policy of de-elitism was blow to Kemalism, as uneducated rural masses came to surface (Hansen, 1991: 426). The government was unable to provide effective governance of the economy, due to high inequality ((Öniş and Rubin, 2003: 2).

In 1973, ratio of income shared by top 20 percent to income shared by bottom 20 percent was 16.6 percent. In order to achieve social justice, deliberate policies should ensure that economic rewards are equally distributed among clusters. In private sector, employment did not grow due to high technology industrialization and overvalued currency. Increased unemployed pool led to revolutionary activities, violence, and terrorism (Mehmet, 1983:53-54).

Turkish elite had anti-rural bias, unlike original ideology of populism embodied in Kemalism. In most LDCs, postwar industrialization was urban-based, ignoring rural development. State apparatus served elite and their interests, rather than modernization and development of the country. Kemalism had egalitarian and populist ends as initial goals. However, there was no consideration if needed political and economic institutions were feasible. The whole burden was on state, which had to distribute benefits of development to whole society in equitable way. However, an authoritarian grants economy was dominated by self-serving elites and monopolistic SEEs. There was ignorance of majority for benefit of privileged minority. The military had close ties with industrialists and direct investments were made (Maxfield and Nolt, 1990:60-62; Karasapan, 1986:31; Mehmet, 1983:54-57).

There were populist cycles and fiscal crises, which described Turkish economy after 1950s, created by DP. Populism referred to usage of state resources and manipulation of economic outcomes in ways beneficial to certain social groups and elites. Populist cycles created wide electoral base, and resulted in fiscal crises and inflation, this ended by coup in 1960 and stabilization program by IMF (Öniş, 2003:2). Political unrest in Turkey had social roots; break down of traditional organization values, pressures to change the society and economics, and social and political units that suit for nation state's requirements. The government has to approach society and integrate society and politics, local communities in turn accept wider political allegiance (Karpat, 1964:51).

There was chronic illness in Turkish economic thinking; economic life was subordinated to social and cultural goals, as viewed by bureaucracy and intelligentsia, while private enterprise supporters ignored social and human dimensions of economic life. There were trials from the government to enhance popular interest in economic development, foreign aid helped industrialization and agriculture development. Mixed economy was traditionalist, conservative and based on elitism. SEEs did not conform to true socialism, nor did private enterprise to modern capitalism. They rather reflected domestic socio-economic conditions (Karpat, 1964:68). High quality exports targeted developed countries, and low quality exports to developing countries. This reflects a classical export growth pattern (Hansen, 1991: 402).

Table 8 provides a summary of development strategies in Turkey since 1923 until 1980s. Between 1923 and 1929, the focus was on private enterprise and free trade. After Great Depression and until 1939, the shift was towards etatism and mixed economy. Between 1939 and 1946, the WWII affected the economy and political life due to mobilization. At the end of 1940s until late 1950s, there was democracy, mixed economy, and focus on agriculture. During the 1960s and 1970s, the military government focused on ISI and planning. Starting in 1980s, the shift was to export-oriented growth (Hansen, 1991:264).

Table 8 Development Strategy in Turkey since 1923

<i>Period</i>	<i>Institutional Setting</i>	<i>Basic development strategy</i>
1923-29	Private enterprise, free trade with low tariffs (Lausanne Treaty)	Westernization, recovery, infrastructure, industrialization, tax reform
1929-39	Etatism, mixed economy with large public enterprise sector, balance of payments controls, primitive five-year planning	Inward-looking import substitution, infrastructure, industrialization
1939-46	Etatism, mixed economy, war economy for neutrality	Military considerations
1946-50	Relaxed etatism, mixed economy, controls	Recovery, increased emphasis on agriculture
1950-53	Democracy, trade liberalization, mixed economy	Agricultural expansion and mechanization
1953-59	Democracy, mixed economy, balance of payments controls	Agricultural expansion, import substitution
1959-62	Democracy replaced by military regime, etatism, mixed economy	Stabilization
1962-78	Democracy, mixed economy, comprehensive planning, labor market liberalization	Import substitution
1978-80	Same as in 1962-78	Stabilization
1980-85	Military regime followed by limited democracy, mixed economy, trade and financial liberalization, labor market repression	Stabilization, export-oriented growth

Source: Hansen, (1991:264)

4. COMPARATIVE ANALYSIS of ISI in EGYPT and TURKEY: STATES and ECONOMIC DEVELOPMENT

The following chapter provides an overview on major points of analogy and difference between Egypt and Turkey, along with their implications for success or failure of economic policies in both. Historical, global, and political contexts were analyzed in this study. External and internal forces that affected both countries were discussed, based on position of each country in the international system. Egypt and Turkey adopted similar policies. However, timing and consequences differed. Colonialism, domestic institutions, governments, human capital, macroeconomic policies, and international system (Adewale, 2012:293; İmrohoroglu and Üngör, 2013:1-2).

Different outcomes despite similar steps in terms of economic policy could be attributed to different growth path of each country (Owen and Pamuk, 1998: xvii). In order to understand future development policy of country, its past development policy should be considered to highlight roadmap. Therefore, initial conditions in each country were analyzed. The structure of one domestic economy can be looked at from an international view. If one allowed comparative studies, one could check whether a country's economic performance has lagged behind other countries with similar conditions. International context is important and determinant in crises (Waterbury, 1993: 24; Mehmet, 1983:49).

If a nation's growth is to be understood, politics of economic restructuring should be considered within some contexts: political, historical, and global. Political context refers to role of state in harmonizing conflicts and allocating resources. Historical context refers to history of landownership, relocation of population, and transportation systems' changes. Global context refers to the impact of external forces on national economic performance; world recession, international indebtedness, foreign exchange, crises, and structural adjustment programs (SAPs). Exogenous political factors limit government's sovereignty and shape its economic policies (Hansen, 1991:242; Todaro and Smith, 2006: 14-15; Owen, 1992:71; Owen and Pamuk, 1998: xvii).

Domestic and international factors constrain growth paths. Domestic ones are economic like resource endowments, population, and physical size, or institutional such as governmental policies, relative gains and losses achieved by local classes, regional and international allies, and finally strengths and weaknesses of agencies used by the country to implement its desired policy. International constraints are access to capital and technology, foreign trade, international markets and financial flows, powerful external agencies such as IMF, UN, World Bank. International constraints determine the transition of LDCs, due to offered capital and technology by the international system (Todaro and Smith, 2006: 113; Richards and Waterbury, 1990: 33; Boratav, 1986: 138).

Physical size and population shape national income levels, economic potential, resources endowment, and domestic markets. Colonial history shaped educational and social institutions in LDCs, which after independence became concerned less with economic development. The focus was on building economic and political structure. Moreover, physical resources such as land, capital, and human resources are in terms of skilled people (Todaro and Smith, 2006: 46). Noneconomic factors such as political, cultural, and strategic systems affect economic policy (Okyar, 1979: 326). Economic and non-economic factors are interdependent. Non-economic factors led to failure of development policies, for example, property rights, income distribution, and domestic attitudes towards modernization (Todaro and Smith, 2006: 14-15; Owen, 1992:71).

Geography⁸⁵ is another factor affecting economic growth and agricultural productivity, because it determines transportation costs and technology diffusion. International trade consolidates market integration and helps economic convergence between rich and poor countries. Institutions are another factor, in terms of property rights and rule of law. The country is integrated with the world based on its flows of trade and trade barriers (Rodrik *et al*, 2002:1-2). For example, Turkey is endowed with land, fertile coastal plains and forbidding mountains. It has command over Bosphorus and Dardanelles. In Egypt, Suez Canal is a transportation monopoly, so it collects taxes from international maritime. It has fertile soil in Nile Valley and Delta (Hansen, 1991: 395-440).

⁸⁵It is not an easy task to measure geography. There can be measures such as distance from the equator, proportion of land mass in the tropics, and temperature average (Rodrik, Subramanian, & Trebbi, 2002:1-2).

Middle East is an underdeveloped area, due to characteristics it shares with most LDCs. In this chapter, some aspects on Middle East are presented, as being helpful in understanding ISI in Turkey and Egypt. Middle East had low integration into world economy, due to structural problems and economic imbalances such as less private capital inflows, backwards production techniques, low public health, external debt, declining prices of primary products, authoritarian political regimes, underdeveloped domestic markets, lack of advanced technology (Yousef, 2004:91-92; Kamrava, 2012:96; Bonne, 1946:526; Méon and Sekkat, 2004: 1477).

In Middle Eastern countries such as Turkey and Egypt, the public sector emerged as a sign of widely accepted interventionist state. The leader had ultimate power to decide resource allocation, budgets, and investments. Power concentration was derived from two principles. First, state authorities had to maintain law, and provide its citizens with welfare and national defense. Second, balances were a means to help the state reach its goals (Jreisat, 2006:412-413).

Interventionist-redistributive government created set of expectations about state role. Therefore, governments that reduced subsidies or welfare programs witnessed social and political constraints, business elites received economic gains of reforms, for example, violent mass protests followed up in Egypt in 1977 when subsidies were announced to be reduced (Yousef, 2004:100). Hunger revolt was one of governmental fears in Egyptian society (Roussilion, 2008:362-365; Owen, 1992:116).

4.1. Colonial History: A Factor affecting Institutions and Economy

Political and economic shifts influence industrial relation system. Industrial relations in LDCs emerged with colonialism and independence trials. Turkey did not have a colonial history, but it had weak industrial institutions. Except for Republic of Turkey, most Middle East countries were colonies. Institutions were set by DCs to exploit rather than support LDCs (Todaro and Smith, 2006: 79; Çetin, 2010:4). Institutions were influenced by settler mortality. European powers did not build high-quality institutions or enforce rule of law, their interest was to extract resources (Rodrik *et al*, 2002:3).

Colonial powers left damages that needed to be repaired by the state. Therefore, private sector was not the ideal party to plan and mobilize resources. Political structures only preserved imperial interests rather than domestic well-being (Jreisat, 2006:412-413).

The state can be seen as an architect, which designs structural transformation and how positions change in each stage of development. Turkey was never colonized; it did not accumulate capital through developed world. It lacked any modern infrastructure. Therefore, the emerging state had to accumulate the necessary capital. This may reflect the fact that Turkey had no choice other than self-building to accumulate capital and achieve economic growth (Bayar, 1996: 773-774). On the other hand, Egypt has always lacked political autonomy. A country only develops, if it has political and fiscal independence, so tariff protection, tax exemptions, educational policies, and credit facilities should have been implemented simultaneously to achieve economic development (Issawi, 1963:195-196).

Post-colonial Middle East had emergent sense of citizenship and public welfare provided by the state, new forms of rights and duties were established, competition for political power, trade unions, and professional associations. Nationalist struggles turned into political incorporation, which dominated movement rather than elites (Yousef, 2004:94), for example, although Turkey was never a colony, there was no sense of Turkish nationalism due to lack of true nation state, reforms by Ataturk aimed at shifting loyalty from Islam to secular nation, including its territorial limits (Karpat, 1964:53).

Although states are formed out of common feelings of kinship, modern Egyptian state was formed and then feelings of belongingness were established. The state was established in 1805, and forms of identity followed (Marsot, 2007:72). Egypt was a province of the post-Ottoman Middle East, which was divided among colonies that determined national boundaries, local governments, and electoral systems (Yousef, 2004:94).

Liberal economy that exploited Egypt during monarchy was a reason favored state-led growth. Egyptians always believed in duality in economy and society. All development fruits went to foreigners; people had no willingness to learn and change into modern society. After colony ended, the dual society continued, and rich westernized their life style, while traditional rural remained impoverished (Marsot, 2007:128).

For Rostow (1959: 6), nationalism although aimed at political independency, it impeded economic development. Some leaders ignored domestic economic needs, as they stood in face of colonial powers, so familiar game of power and politics gained attention, and domestic modernization was neglected (Rostow, 1959: 6). This can be the case in Nasser's Egypt, where external context shaped economic policies (Roussilion, 2008:352-354). Global context and the war with UK and France meant loss of Western financial sources (Ikram, 2006:3).

Although Turkey did not have linkage to Arab-Israeli conflict, it was engaged in disputes with Greece and Cyprus (Hansen, 1991:255-450; Yousef, 2004: 94). International alignment affected both countries. Turkey gained from NATO and OECD membership. Egypt was penalized for nonalignment by USA, and encouraged by Soviets. Turkey lost internationally for invading Cyprus, and Egypt was rewarded when it signed Camp David Treaty, and was boycotted by Arabs (Hansen, 1991: 441-444). Both countries are middle power states, which had a rank of middle power in global system, but as major power in regional system (Kuntay, 2014:11-20).

4.2. Economic Performance in Egypt and Turkey

ISI was adopted under unique economic structures, social and political institutions. In Egypt, military dictatorships overthrew democratic regimes in 1952. ISI started in parliamentary democracy in Egypt, and continued until 1980 under three autocrats. In Turkey, ISI started under autocracy, continued until 1980 under democracy, and then shifted to export-led growth. Both countries had similar terms of trade from 1920s until 1950s, deterioration during the Great Depression, economic recovery after WWII, and predominant agricultural economies.

Egypt after 1973 became a net oil exporter. Turkey lost on terms of trade in 1973 until 1984 and was a net oil importer. Turkey was neither a pure authoritarian, nor a democratic pluralism; it was semi-democracy. While in Egypt before 1952, there was a pluralistic system, free trade, and parliamentary democracy (Hansen, 1991:521; Silva, 2007:68; Demirbaş, 2010:129).

Political organization and administrative competence of government represent single explanatory variable in different economic performance among countries (Waterbury, 1993:9). WWI challenged democracy in Egypt, autocracy in Turkey. WWII had set background for changes in Egypt and Turkey. In Turkey, early reforms began in 1920s when the population was in decline, due to wars and migration. In Egypt, although Britain did not focus directly on reforms and human capital, education was of high quality compared to Turkey, recovering from Ottoman debt (Hansen, 1991: 190-195).

Egypt was integrated into capitalist world through cotton exports. It had commodity relations based on export production and manufactured consumer goods imports. In 1918, there was balanced development of agriculture and industry. Until 1940s, state was responsible for every aspect beyond irrigation and public utilities (Ayubi, 1992:92). During WWII, industrial development was promoted; domestic market was deepened, manufacturing employment increased. Mechanization was intensified in textile industry and workers were dismissed. British in interwar period had improved variety in cotton, increased input of fertilizers, and enhanced drainage (Hansen, 1991:468; Bein, 2008:332).

In Turkey, in 1924, a national bank (Banque D'affaires) was built, as a domestic financial institution to reduce foreign influence. The bank was mediatory agent between business and government. It had holdings in economic activities (Boratav, 1981: 169). In Egypt, Banque Misr (Misr Bank) was founded, and bank's founders believed economic development was necessary for political independence (Bein, 2008:325).

Both countries had disguised unemployment problem, due to high population growth rates. The growth in Egyptian population was too high through history. Between 1937 and 1960, population density rose by 69 percent while agricultural cultivated output grew only by 10 percent. Therefore, the country suffered from disguised unemployment and low productivity (Roussillon, 2008:337).

Moving to Turkey, in 1920s, in urban areas, less than 25 percent of Turkey's population lived, with more than 5,000 citizens. After WWII, urbanization increased it to 44 percent by 1980 (Pamuk, 2008:268).

In 1962, there was population growth more than growth in agricultural output, which created disguised unemployment of about 1 million in agriculture (Karataş, 1977:4).

In Egypt, the Great Depression intensified the need for ISI through a new economic vision (Beinin, 2008:320). Egypt was unable to set independent tariff until 1930, because of existing capitulations until 1937, and mixed courts until 1929. In the early 1930s, tariffs on manufactures rose. There were technological developments in agriculture, urban migration, which changed crop patterns, market relations, and peasant's communities (Beinin, 2008:329-332; Clawson, 1978:20). In the 1930s, Egypt did not sign bilateral agreements and did not have exchange controls (Hansen, 1991:79).

ISI was assisted in Egypt through tariff reform in 1930s, cheap loans by government, and capital was favored. In 1937, tax reform aimed at taxing urban foreign businesses, and it aimed at equity between Egyptians and foreigners (Hansen, 1991: 451). Tariffs on manufactures rose, and 8 percent excise tax on domestic produced textiles was repealed in 1925. Some industries were existent before tariff protection was set. Landowners were major investors in Misr Bank, and 87 percent of capital in cotton spinning and weaving (Clawson, 1978:20).

In the 1930s, irrigation system in Egypt was improved, manual pest control, chemical fertilizers helped yields and quality to be back to the 1900 level. In 1930, laws of customs duties and taxes were modified. Land-tax was modified in 1939. First income tax was issued and fixed rates on income categories. Tariff reform aimed at higher duties on imports of capital goods, and fewer imports of consumer goods. Government credits expanded to buy fertilizers and seeds. In 1935, interest rates declined. The tariff reform was one major step in industrialization.

Capitulations⁸⁶ and trade treaties with Europe forced Egypt to set low customs duties of 8 percent on imports, and 1 percent on exports. In 1932, import duty was 1 percent, and high flexible tariffs were imposed on wheat and sugar. The reform was supported politically by the Egyptian Federation of Industries, and landowners who aspired at better investment to overcome depressed agriculture (Hansen, 1991:80-95; Beinini, 2008:331; Issawi, 1963:38-41).

Moving to Turkey, in 1929, Lausanne terms expired, capitulations were abolished, and the country regained tariff autonomy. External terms of trade declined by 23 percent in 1929. Mode of accumulation based on full specialization in agriculture, ended by the Great Depression. The Turkish government resorted to bilateral trade agreements and reciprocal quota systems. Germany was the major trade partner during the period of 1937-1939. After 1929, economic growth was based on interventionism, reducing imports between 1928/1929 and 1932/1933 from 14.4 percent to 8.7 percent. Unemployment declined; three fourth of labor force was employed (Owen and Pamuk, 1998:13-21; Okyar, 1979:327). It can be argued that Great Depression was the motive behind revised economic policy. It was realized that foreign trade might not be the best way to obtain necessary industrial goods, and the country had to rely on domestic resources (Okyar, 1965: 98-99).

Turkey had followed ISI since 1929, and trade controls were relaxed in 1950/53 and 1970/73. Lack of capital, managerial incompetence, domestic stagnant production, and subsidies to private sector were reasons behind failure of free market economy (Mehmet, 1983:50; Hansen, 1991: 280-3540).

Turkey tripled its GDP in two decades and economic structure shifted towards industry. In 1924, industry share was 8.5 percent; it reached 15.5 percent in 1939, which was impressive compared to resource constraints (Naş, 2008: 26-27). Turkey achieved high success in the interwar period, because of agricultural growth and expanded cultivation. It had high agricultural growth after 1960, but industrial growth was higher since the Republic foundation (Hansen, 1991: 255-459).

⁸⁶ Capitulations stated that foreigners in Egypt would be taxed after approval from their governments. Moreover, no taxes were on personal income or company profits. Any legal question for foreigners would be discussed by Mixed Courts. Capitulations were abolished in 1937 (Tingor, 1980:104).

In 1950s, Egypt witnessed a change in political and economic spheres. It moved into state-led growth, and became a Republic under military rule. In 1950, in Egypt, about 85.4 percent of commodity exports were cotton, and 81.2 percent of exports were petroleum, with 9 percent of industrial goods (Hinnebusch, 1993:162-165; Mabro, 1967:322). Controls on foreign trade, exchange rates, prices, and rents were introduced. The government relied on subsidies to face inflationary prices of consumer goods. In late 1940s and 1950s, tariffs increased to allow for ISI. Private enterprises operated and benefited from protectionism (Ikram, 2006:2).

In the 1960s, public sector in Egypt dominated all sectors such as housing, retail trade, and small industries. Industrialization was a process for state building, although normality was that state builds national industry (Ayubi, 1992:92). Nasser in 1965 announced that private sector in Egypt was inefficient. Therefore, the movement towards nationalization and state capitalism started through focusing on productivity and discipline (Richards and Waterbury, 1990:195).

In Turkey, during 1950s, less than one-quarter of GDP was generated by agriculture, although the focus was on agricultural expansion, manufacturing constituted one-fifth. In the 1960s, manufacturing share increased in GDP, and agriculture declined. In the interwar period, trade generated 7.5 percent of GDP, and in 1980s, it was almost equal to manufacturing share (Hansen, 1991:267), reflecting a passive and squeezed agricultural sector. In the second half of 1960s, agriculture was recognized as supplier of resources in an active and equal way. It was a co-equal partner with industry. This indicated resources would flow to agricultural sector to increase productivity and output, which in turn facilitates extraction and transfer of resources into industry (Thorbecke, 2006:5-7).

Egypt, in 1970s, depended on petroleum. High inflow revenues shifted the focus towards borrowing and consumption instead of reform and production. *Infitah* was driven by a newly integrated economy into world markets and need for funds. Banking system was liberalized but was unable to attract funds due to low interest rates domestically. Egyptian state was never strong enough to regulate world market's domestic impact to its interest, this was because of dependence on Western aid and loans and oil international prices. In 1980s, prices of oil declined and foreign exchange crisis occurred. Egypt was always important to the West due to its strategic geopolitical position for economic concessions; it also was a major factor in resolving efforts of the Arab-Israeli conflict. Reforms cannot be imposed unless there is internal support (Hinnebusch, 1993:162-165; Mabro, 1967:322; Hinnebusch, 1993:162-165).

In 1976, IMF and Egypt signed a standby agreement to decrease subsidies for consumer goods (Roussilion, 2008:362-365; Owen, 1992:116). The absent consensus on economic reform erected rent-seeking behaviors through monopolies. ISI was totally an exhausted strategy, while outward-oriented strategy was preferred to help Egypt integration into world economy (Hinnebusch, 1993:159-160). In Turkey, in 1970s, the government announced the departure to an outer-oriented economy; Turkish Lira was devaluated by 49 percent, a move to crawling peg nominal exchange rates, according to IMF conditions, export incentives, liberalized imports, free interest rates, and higher prices of SEEs products. This tight monetary policy led to losses for private sector that kept exporting (Bayar, 1996:780).

The facts discussed above draw attention to supremacy of public sector in both countries, and their dependency on SEEs as major growth engine. This will be discussed below:

4.3. Public and Private Sector in Egypt and Turkey

Mixed economic systems include public and private ownership of resources. In many LDCs, public sector was larger due to lack of skilled labor, which has to be coordinated (Todaro and Smith, 2006: 46). Private business did not invest in favor of the people. SEEs were better servants to society's needs (Hinnebusch, 1993:161).

SEEs were major instrument in growth planning. There was less monitoring, and would have less transaction costs. They also had social purposes such as providing low-cost commodities, jobs, and development. However, to realize this, selfless public officials would not exploit their power and assets they control, as monopolist SEEs were for public interest. On the other hand, private monopolies would exploit assets. There were three illusions on public sector. First, bureaucratic control would work as intended and handle distortions and gross inefficiencies. Second, sustainable devoted management. Finally, planners would design rational strategies and self-financing growth in publicly owned assets would result. SEEs have been making loss in both countries, and contributed to budget deficits, low export revenues, dependency on imports, and borrowing, in order not to alter distributional arrangements (Waterbury, 1993: 6-15).

One of major differences between two countries was public sector, narrowed in Turkey, where private sector expanded. Egypt, on the other hand, kept public sector and SEEs, despite structural adjustments and reform promises. Public sector size can be measured by its expenditure and revenue as percentage of GNP (Hansen, 1991: 448).

In Egypt and Turkey, although private sectors differed in strength, there was some analogy. Private sector was weak for some period, owing to profiteering and speculation, and selling out national good through coalitions with foreign investments. The state attempted to protect marginalized groups from private greed, and undertake projects that shortsighted private sector would not afford. Moreover, each of spread ideologies believed in emergence of nationalist entrepreneurial bourgeoisie that would support policies set by the state (Waterbury, 1993: 5-15).

In 1952, Turkey had larger public share in GDP more than Egypt. It was 20 percent against 18 percent. In 1982, both countries had larger public sector, but proportions reversed. In Egypt, it became 45 percent. In Turkey, it was 22 percent. As a result, public consumption in Egypt increased by 50 percent, and declined in Turkey. Turkey preserved the fifty-fifty ratio between two sectors in industry. (Hansen, 1991: 457-458). In Egypt, Law 97 of 1983 stated that SEEs could not be declared bankrupt. Indeed, private firms with accumulated debt of 50 percent of their capital could be. The absence of liquidation process in SEEs was common in both countries (Waterbury, 1993:16).

In Turkey, promises were that state would cede its place to private sector. However, by assets concentrated in public sector, interested managers and politicians started to protect and extend resources owned by the state. The weight of public sector was always big in Turkish economy. In 1950s, eleven SEEs were established in Turkey. In 1959, public sector share in public total investments was 62 percent. In 1979, public share in fixed capital investments was 50 percent. The business sector was big; it was responsible for the export activity and represented a high pressure on the public budget. Business enterprises in Turkey were always controlled; they had to keep operational levels near full capacity and to make timely debt payments (Mehmet, 1983:54; Buğra, 2007:40; Waterbury, 1992:127; Waterbury, 1993:11-12).

In Turkey, the focus was on profitability rather than redistribution. The focus was on stimulating private sector through devoting more resources to private sector. However, in both scenarios, a state intervening in economic reforms prevented a whole privatization process; it rather created bureaucracy and political conflicts among social groups (Richards and Waterbury, 1990:195).

In 1950s, Egypt had a mixed economy with private and public sectors. One operates on prices and the other on targets. The private sector was assumed to lack social responsibility and to hinder industrial development, so it was liquidated and the vision was an industrial economy. In Egypt, the large public sector harmed the economy, because of low civilian investments after 1966. This was caused by overvalued currency, and that investments were not based on profit maximization (Hansen, 1991: 17; Kenawy, 2009:589).

In Egypt, public inefficiency and bureaucracy replaced private entrepreneurship. Although the economy shifted in 1970s into *Infitah*, the country was drowning in large inefficient public sector. In Egypt, the public sector has always been prolonged due to ideological commitment to state control. The government created terrible situation by intervening in price system prevailing before nationalization. Efficiency of bureaucracy is an important factor in any country adopting socialism (Hansen, 1991: 17; Kenawy, 2009:589).

4.4. Land Reform and Distribution in Egypt and Turkey

In May 1945, The Land Distribution Law was presented in the assembly, as an attempt to support farmers. About 99.75 percent of landownership was concentrated in farms with less than 125 acres (500 dönüm), and small farmers were marginalized. It aimed at providing unused state land, lands without owners for landless peasants, land of those with more than 500 dönüm was expropriated, article 17 stated that three-quarters of land from those owning more than (50 acre) 200 dönüm is expropriated in populated areas. Some 20-year interest-free loans were to be given to peasants. However, opposition stated that this law was threat to security of property, impediment to investment and efficient farming, and protests were done to oppose absent democracy, Menderes was one of opposing parties (Zurcher, 2004; 210).

In Turkey, there was no literal land reform; it was change in ownership of land owned by Greeks and Armenians. The government distributed public uncultivated land to landless laborers through grants. In 1946, the Land Distribution Law declared redistribution of land to small owners, but it was distribution of public land and communal pastures to landless farmers. Nation state building was done through power transfer from bureaucratic intelligentsia to economic groups and involvement of lower social groups in political scene. There was no more semi-feudalistic view of local communities, which were integrated into civic responsibility and identity with larger social and political groups. Landowners were threatened by intended land reform in 1945 (Karpas, 1964:51-53; Mehmet, 1983:50-54; Hansen, 1991: 280-340).

On the other hand, in Egypt, in 1950s, the land reform redistributed excess feddans among landless peasants and limit power of ruling class. The reform limited land holdings to 200 feddans, and extra 100 feddans if there were children. The goal was to achieve social justice, divert investment into industry, increase growth, and obtain hard currency. Although land reform aimed at better life for rural population, landless rural laborers did not witness any improvements, due to higher prices and lower labor demand. By contrast, tenants' income increased due to rent-reductions. Beneficiaries paid installments to the government, but it was less far than previous payments, so their incomes increased (Issawi, 1963:52-54; (Abdel-Malek, 1964:40; Harik, 1984:45; Ikram, 2006:3).

4.5. Economic Reform and SAPs in Egypt and Turkey

Economic reform depends on factors such as degree of the crisis seriousness, pressure by IFIs, strategic importance of the country to USA, powerful interest groups controlling local resources, size of domestic economy, the degree to which it can be dominated by domestic monopoly, and the degree to which it could be liberalized (Yousef, 2004:107; Owen, 1992:114). Reforms should be about timing, pace, kind of economic and political factors, external pressures, and IFIs. It was hard for governments to manage link between economic and political reform. There was acceptance of instrumental connection between two reforms, and that social contract limited the government's ability to intervene less and manage state-labor relations (Yousef, 2004:107; Owen, 1992:114).

Both countries differ in factors such as institutions quality, human capital, and consensus in society on meaning and need for structural change (Adly, 2013: 217). Both started with market-based industrialization, but external economic crises in 1930s, or 1955-1956 changed the policy to etatism. In early 1980s, both countries had a foreign exchange and debt crisis. Turkey undertook a policy radical change to export led growth. However, Egypt depreciated its currency, and rejected strategy change, it benefited somehow from oil price increases in 1979 and Camp David, but after 1984, again a crisis occurred and IMF pressures (Hansen, 1991: 255-459).

In general, leaders were reluctant to reform because of delayed benefits and immediate costs. Social, economic, and political costs accompanied slow incredible reforms (Yousef, 2004:107). Governments should have provided incentives and inputs. Ineffective reforms were caused by lack of changes in rural institutions and production control (Todaro and Smith, 2006: 456). Structural limitations and lack of consensus over true meaning of reform prevented adequate reform implementation (Beinin, 2008:310).

Economic reform by “top-down decree” is about changing bureaucracy, regulations, and state economic policies. However, it may not consider social groups threatened in terms of welfare. It reproduces state-centered approaches to social, economic policy management, keeps paternalistic, and interventionist form of state-society relations (Yousef, 2004: 111).

In Turkey and Egypt, “change from above” strategy was followed. However, Atatürk managed to unite social groups, through conviction or force, that change was needed. On the other hand, Nasser focused on external⁸⁷ causes, and he divided the society based on religion and ideologies. Therefore, he could not gain expected changes in economic terms. Whether in Egypt or Turkey, fundamental institutional changes against corruption and for transition from command economy to market economy were a precondition for successful adjustment (Thorbecke, 2006:19). Atatürk adopted "development from above" strategy to substitute capitalist incentive and maintaining financial resources without loss of autonomy or independence (Bonne, 1946:526).

For countries in crisis, reconstruction policies were advised to focus on certain points: extension of cultivated areas to raise productivity through large-scale developments in irrigation, industrialization as main development policy, better income distribution through reducing rent, reforming land tenure, and increasing service sector in terms of health and education (Bonne, 1946:526). However, political and economic reforms were a threat to political order, if simultaneously implemented (Yousef, 2004: 111).

The difference lies in response to crisis. Soft budget constraints made it unnecessary to reform comprehensively in Egypt in 1970s. Sufficient amount of fund inflows making reforms and difficult decisions delayed (Yousef, 2004:107). Egypt rejected structural adjustments, and relied on strategic rents. Turkey dealt with the crisis through military government, SAPs, and policy shift. Egypt maintained its system and SEEs were strengthened, ISI was not removed. Turkey had system transformation though opening to global markets (Waterbury, 1993: 6).

⁸⁷ Nasser received recognition from Third World's leaders supporting his leadership and ousting of monarchy and British troops' evacuation. The Third World began searching for its independence and this brought anger of U.S. accusing them of hypocrisy. These countries were got aids from both sides. Nasser was recognized as leader outside, but inside he had a country with weak economy and army (Marsot, 2007:132).

Structural adjustments were implemented in unannounced ways through rejecting reforms by Al Sadat and Mubarak. On the other hand, Turkey in 1950s and 1960s apparently rejected to tighten the belt. However, after 1980, it announced reforms to be caused by domestic concerns (Richards and Waterbury, 1990:231).

Egypt never managed to develop a capitalist system with free market, because of crony capitalism, power and wealth interaction, absence of sound regulatory capacity, monopoly, and unequal income distribution. It was contingent on traditional sectors such as gas exports, tourism, and Suez Canal revenues. Turkey suffered from income inequality problems, regional and ethnic problems, authoritarian legacy, military domination, marginalized labor unions, and labor rights violations. Turkish economy had market distortions and deformations deepened by government intervention (Boratav, 1986: 123; Hansen, 1991:458; Adly, 2013:2).

Stagnant economic institutions and exports dependency on raw materials signaled industrialization. Industrial expansion was inward oriented; uncoordinated trade policy was due to conflicts between industry and trade ministries. Incentives system did not highlight the favoritism of exports, lack of communication channels among private sector, state, and exporters created hardships of information access and plan setting (Adly, 2013:217).

4.6. Populism and Etatism in Egypt and Turkey

In some Middle Eastern countries, there was tendency to refer regimes to a single person. Personalizing a regime, however, was not a logical trend, as leadership changes could not be linked to a regime change. Regimes were thought of according to behaviors and actions. Therefore, regimes change resulted from social and economic changes (Richards and Waterbury, 1990: 197-300).

The global trend favored socialism and planning, but Atatürk attempted to keep neutral. Unlike Atatürk, Nasser had global impact in many third world countries, which gained their independence (Çoban, 2007:46-53). Nasser was like Atatürk, they both had to suppress other opposition groups to consolidate power into his hands, Muslim Brotherhood, and communists were jailed (Owen, 1992:28).

Atatürk was seen as owner of leadership style based on modernization and break with tradition. Nasser tried to turn Egypt into modern society through analyzing economic conditions, political mobilization, institutions, and legitimacy to build modern political society (Podeh and Winckler, 2004:2-3).

Kemalism etatism was mono-centric. Urban civilian-bureaucratic elite was controlling the reform and biasing the results. However, this long-term view reflects a mistrust of elite to peasants and minorities (Mehmet, 1983:59-60). Etatism was attached to Egypt since Nasser. It was a mixed economy, with large public sector, the term as described by Atatürk. It was a sequence of autocrats, passing by Nasser, Sadat, and Mubarak. Economic system did not change although government style changed. Egyptians were not involved in decision-making, and that it was the elite receiving benefits and privileges, in return for sacrificing political freedom (Hansen, 1991:110-111).

During Sadat's time, growth was supported by private and public investments, consumer goods subsidies, and low prices for agriculture output. Self-serving administration and discrimination against agriculture was evident. Mubarak did a little in terms of policy change, but private sector expanded, agriculture was not exploited, military was back to contact with private sector (Hansen, 1991: 454).

Nasser and Atatürk preferred that industrialization start with private entrepreneurship and the government protection and subsidies. However, crises changed the ideology towards etatism. Atatürk faced the Great Depression and collapse of international economy. He depended on SEEs, but did not replace private sector. It was not socialism, and private equity was not redistributed to achieve equity. Only public land was distributed to smallholders in order to extend agricultural output and equity in rural population, land reform was a secondary elite issue (Hansen, 1991: 424-453).

Ataturk had set the basis for preconditions to take-off stage (Rostow, 1959: 6). By death of Ataturk, the country has been following the dynamic path of self-dependent growth through "pre-conditioning" (Boratav, 1981:166; Singer, 1977: 5). Nasser expanded the public sector, which became responsible for every aspect in economic life. Nationalization waves harmed private sector (Hansen, 1991: 424-453).

Egypt's economic policy was dogmatic and affected by external factors. In first years, it was conservative. After 1954, it was necessary to increase investment to keep output at

3 percent, which is the population growth rate (Mansfield, 1973:671-672). The position of development in priorities of policy makers shapes economic growth. Nasser aimed at being Arab nation's leader; Sadat aimed at national security. That is why policy routes and results differed. Egypt had an inward-looking economic policy but outside-looking political objectives (Ikram, 2006:76). The government in Egypt did not give priority to growth. The subsidy system aimed to reduce burdens on population. The subsistence level of consumption was enough to keep Nasser or Sadat in power. The economy was mixed but capitalist. Socialism occurs when political and economic life of the country is directed by popular forces' delegates (Abdel-Malek, 1964:45; Hansen, 1991:313).

Nasser and Atatürk had a bond to masses of educated middle class, peasants, and urban workers. They modernized communication through press or radio. Through this colloquial language, masses were successfully mobilized, and power was consolidated. The goal was national integration and supported regime. The term populism appears in a society witnessing two processes of urbanization and industrialization. It is usually a rapid modernization accompanied with transition from a traditional to a modern society (Podeh and Winckler, 2004:4).

Populism means mobilizing masses of low classes into political sphere for first time through economic development policies. Therefore, it is about more activism of lower classes, towards goal of national industry building. That is why social welfare policies were used to win these classes. When ISI is accompanied with nationalization and foreign aid, it would face technical problems, which occur due to need for intermediate capital imports. This leads to balance of payment problems and lack of foreign exchange reserves. These hardships force governments to restrict its welfare policies and social benefits, creating in turn social conflicts and new divisions appear. Lower classes now powerful, express their demands that are believed to be excessive by economic reformers, so the state is weakened (Ayubi, 1992:97).

Reformist policies promote development without class conflict. The policy follows sort of socialist attitude towards welfare, supporting urban working class, peasants, and middle class. This means etatism. The regime aims at national independence from world economy and previous colonies. Socialist policies attempt to create social egalitarianism to widen regime legitimacy (Podeh and Winckler, 2004:56-57).

Popular classes affect political decision-making, which protect their short-term economic interests, but they are not organized in the way allowing them to be an alternative to small partners in political power. Example, government responded to demands of peasantry because they are electorally important, but organizationally passive. Effectiveness and scope of market processes are shaped by economic functions of the state (Boratav, 1986, 135-136).

If strong group of entrepreneurs were willing for industrialization under incomplete competitive markets and class radicalism, there would be a fascist. On the other hands, if there were no strong entrepreneurial group or working class, a populist character would appear (Ayubi, 1992:100). It means that forces existing during development process created populism. Populism creation depends on three variables shaped by degree of tension: the shape of political association between the state and European colony, level of economic dependency on the colony; and degree of cultural similarity between the colonial power and the local society. In Latin America, the association with colonial masters kept on, while their economic and political links were to USA, and culturally they were linked to Europe (Podeh and Winckler, 2004: 9).

Regime failure took place in both countries, because it was no more capable of keeping welfare policies. This was caused by both international sphere and domestic policies. Turkey and Egypt were most evident cases of state-centered corporatism in Middle East, which views corporations as neither mediator between citizens and state not as presenter of private sector interests, but rather as state agents (Ayubi, 1992:98). However, one should consider other factors related to macroeconomic items and their microeconomics basics, especially institutions that should regulate savings and financial markets. Outcomes of a policy are not only shaped by international factors, domestic political, economic, and social conditions have a role. State institutions and social forces shape politics of economic policy change. State policy makers do not have absolute, but rather relative autonomy from social forces (Silva, 2007:70).

Interest groups were powerful, and operated through chamber of industry, commerce, or political parties, unions increased in importance since 1961 until 1980. After 1950, rural population became powerful and support prices for agriculture existed in 1950s (Hansen, 1991:452). In Turkey, power coalition was between two groups: one group controlled the government at national level and had physical power. The other group lacked physical power means but had control over economic and social life in local provinces. First modern group included civilianized military officers, professors, and intellectuals close to the government. They supported supreme state because of modern ideas it was embodying and spreading through reforms. The other group included landowners, craft group, and some individuals with cultural or religious position in traditionalist period (Karpas, 1964:51-53).

4.7. Implications

Based on aspects discussed above, it is clear that main problem in both countries lied in political organization and institutions. Both were major players in economic sphere whether under ISI or ELG. Although the focus of the study was on ISI in both countries, it was clear how institutions were inflexible to change when economic policy was shifted towards market economy, as in Turkey, or to *Infitah*, as in Egypt. However, Turkey was successful in relative to Egypt. Turkey managed to reform its economy through SAPs and internal structural changes. Unlike Egypt that rejected reform, and kept SEEs and inefficient public sector. Egyptian government always offered subsidies to win support, despite budget constraints it might face. These facts pose some implications on both countries.

State-led growth was adopted in different times. Two leaders who initiated the ISI strategy were both nationalists, aiming at industrial basis and manufactures sector. However, Nasser focused purely on external causes, and ignored internal infrastructure. This exogenous focus assumed responsibilities that were beyond economic and political capacity of Egypt. Ataturk, however, had an internal focus on national issues, and started the industrialization program gradually, and based on resources and constraints existing by that time (Mansfield, 1973:677-678).

A factor that should be considered is colonialism. Egypt was a colony for ages. This trend emphasized its dependent nature on external world. The country did not manage to accumulate adequate capital to industrialize. Moreover, Egypt was always involved in regional disputes such as Yemen War, Arab-Israeli disputes, which had cost in terms of economic and political stability. Colonial history of Egypt has shaped its economic route. Colonial power created damages and backwardness, which needed to be repaired by the state (Richards and Waterbury, 1990:186). Egypt doubted benevolence and advocacy of freedom claims made by the West (Jreisat, 2006:412-413).

In Turkey, Institutions, political and social environment contributed to economic change (Pamuk, 2008:273); pure economic and noneconomic motives shaped decreed economic policies (Okyar, 1979: 326). Turkey undertook economic restructuring to comply with economic institutions of capitalism, although institutional environment was reshaped, political and legal environment were not ready because of absent internal forces, no alignment was made between institutional structure and international organizations (Çetin, 2010:5). Turkey was in need for right direction in economic development and political freedom: two conditions that could only bring a country out of any crisis. Balance among social groups is a way to live political freedom. Turkey still faces challenges such as income inequality, gender inequality, and unemployment. However, internationally (Karpas, 1964:68).

Figure 2 shows that in 1950s, Turkey was on top of countries in Middle East in terms of GDP per capita, while Egypt was 40 percent lower. In 1973, Egypt and Turkey were both below the average, relative to oil producing countries. Per capita income in Egypt increased between 1950 and 1973 at 0.9 percent annually, while average at Middle East averaged 4.2 percent. In Egypt, GDP per capita was USD 487 in 1970 and was USD 1654 in Turkey (Kuntay, 2014:15-16; Abdel-Baki, 2013:39). Common features in Egypt were corruption and alliances, which were means of getting support and winning opponents, which in turn inhibited continuity in government system (Marsot, 2007:153; Issawi, 1963:5).

Egypt faced market failures, although it planned for economy. Economic signals and incentives poorly reflect costs of produced goods or services. Government should have coordinated markets, modified prices, correctly set price of factors of production, and avoid misallocation of resources. However, failure was mainly caused by deficiencies in implementation of over-ambitious plans, which set many objectives with no consideration to their feasibility or comparability, vague policies: lack of reliable data, low quality of statistical data. This inconsistency in data abolished accuracy and internal consistency of the whole plan, and lack of skilled statisticians or economists. One should not ignore unanticipated external or internal economic disturbances. The dependency on foreign aid, international trade prevents LDCs from short-term forecasting or long-term planning (Todaro and Smith, 2006: 530).

Figure 2 draws attention that both countries were nearly in same category and conditions by WWI. In 1920s, Egypt was in relatively better situation than Turkey. It had relatively adequate transport facilities, state owned railways, which were better than river and road transportation. WWI harmed the Ottomans, and it lost the war, Balkan wars of 1911/13 and had high debt. Egypt was neutral and had no foreign debt; it had large exchange reserves. Turkey was exhausted by wars and population exchange, but Egypt was in economically good condition. The difference in GDP became evident by 1950s. According to aspects discussed above, this can be attributed to the fact that by WWI, both countries were unstable. Turkey was busy with wars, and Egypt was under British control, with all economic resources devoted to British interests (Kuntay, 2014: 16; Hansen, 1991: 438).

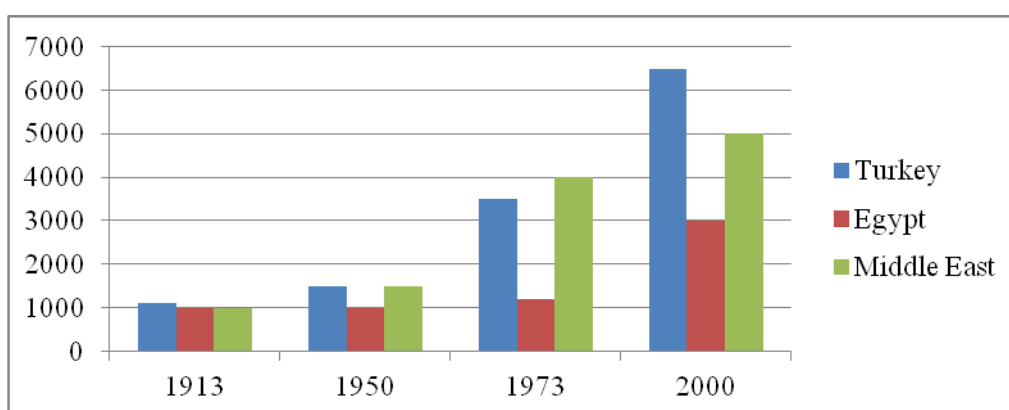
By 1950s, Turkey was already implementing ISI, under clear economic path set by Ataturk. On the other hand, Egypt was undertaking initial steps economically and politically, due to 1952 Coup. During 1950s, Turkey expanded its exports and agricultural output, with SEEs undertaking projects. Egypt was struggling with USA and Britain, High Dam, nationalization waves, and Suez War in 1956 (Hansen, 1991: 438).

By 1960s, the difference in GDP between both countries became wider, and this can be attributed to instable internal conditions in Egypt, which was engaged in wars such as Six Day War and Yemen War. During 1960s, military government in Turkey maintained economic stability through ISI and planning. By 1970s, the difference was still large, which can be attributed to war in 1973, and policy shift to Infitah in Egypt. Moreover, the reluctance to reforms by Sadat and then Mubarak, who kept public sector and subsidies. On the other hand, Turkey undertook reforms and restructured the economy to free market, and implemented SAPs (Hansen, 1991: 438).

During the 20th century, Egypt was most populous and second largest country in MENA. In 1993, the World Bank ranked Egypt as one of low-income countries. It had annual per capita income of \$ 635. While in 1998, the per capita income increased to \$790. Therefore, Egypt moved to the category of middle-income countries (Zohny, 2001:123-124).

In 2000, Turkish GDP was \$6,600, and Egyptian GDP was \$2900, while Middle East had average of \$5000. In 2012, after Turkey, Iran, and Saudi Arabia, Egypt had the largest GDP in the Middle East. Egypt had population growth higher than Turkey and Iran (Kuntay, 2014:15). Egypt and Turkey were among the "Next-11" emerging economies expected to catch up with macroeconomic growth of newly industrialized countries (NICs). In 2013, both Turkey and Egypt were lower middle-income countries (Todaro and Smith, 2006: 39; Abdel-Baki, 2013: 38-39).

Figure 2 Comparison of Turkish and Egyptian GDPs with the Middle East



Source: Kuntay, (2014: 16)

CONCLUSION

The following thesis examined the political economy of import substitution industrialization (ISI) in Egypt and Turkey. It started with introduction, which provided an overview on developing world, changes in world systems in terms of Great Depression and World Wars. It provided an overview on rationale and structure of the study. It explained motives behind nominating Egypt and Turkey for the current study, in terms of historical, economic, and political analogies.

The first chapter discussed emergence of development economics, and provided an overview on many development strategies such as agro export-led growth, mineral export-led growth, manufactured export-led growth, agricultural development led growth. ISI was explained in terms of emergence, rationale, principles, and failure of implementation. It discussed how principles behind ISI were necessity to replicate the North, capital formation as key for growth, and rejection of market solution. The rationales of ISI were export pessimism, price distortions and surplus labor, and infant industry protection, and externalities. Afterwards, export-led growth policy succeeded ISI in some countries. It was explained how both were development strategies, which developing countries adopted to get over backwardness.

The second chapter titled as political economy of ISI in Egypt. It provided a background on Egyptian economy, and how colonial history affected institutional quality. The economy was integrated into global world as mono-crop economy. Later on, when Nasser attempted to restructure the economy, he faced internal and external constraints. Sadat changed the direction of economy and politics. Therefore, there was no clear identity describing the economy. Mubarak seized power when the country was trapped in debts. IMF followed a structural program in Egypt. However, it did not achieve expected results, due to internal constraints such as poverty and resistance of social strata. It showed how British colony shaped the Egyptian economy as mono-crop exporter of cotton.

The lack of exports diversity remained until 1980s; Egypt changed the crop it exported from cotton to oil in 1970s. It was shown how presidents had different focus after the military coup in 1952. Nasser had an external focus on leadership and unity in less developed countries and Arab world, and he cooperated closely with Eastern Bloc. Al Sadat reversed the strategy and followed USA, but it had cost the boycott by Arab nations to Egypt. Inconsistency in policy harmed the Egyptian economy, which entered 1980s with an economy lost between socialism and capitalism, and drown into international debt.

In third chapter, it was discussed how collapsing of Ottoman Empire left behind a destroyed economy. However, Atatürk built the economy through etatism, which had some failures, but generally succeeded in transforming the economy within few years. However, Turkey had a history full of political instability and changing political parties. Each party was changing economic policy, and this harmed the economy in terms of consistency. Turkey adopted ISI and was relatively success. The changing of political policies and interests of social groups led to shift into export promotion, which was again relatively success. However, results were not up to expectations. Turkey had frequent coups, whenever Kemalism and democracy were compromised. In 1960, the military government outset Democrat Party. In 1950s, the focus was on agriculture and mechanization, programs with IMF and World Bank, and rural population started to gain their rights. ISI was kept during 1960s, but the country entered into crisis that ended by a shift in policy towards export-led growth and free market. Turkey was relatively successful, due to support it gained from USA, Marshal Plan, and high agricultural exports.

Afterwards, fourth chapter represented a comparative view on both countries. It showed many points of analogy between Egypt and Turkey, along with points of uniqueness. Both countries were able to industrialize using ISI, but failure occurred due to different reasons. In Turkey, political instability and party conflict harmed the economy, which was changing by every new party. However, Turkey reached the complex stage of ISI, and it could have completed it successfully.

Moving to Egypt, the colonial history shaped its economic structure, political system, and institutions. Moreover, lack of adequate internal resources, unlike Turkey that had strong agriculture, harmed the economy. Egypt was a more fragile prey to foreign domination, unlike Turkey. This in turn prevented the country from capital accumulation.

Both countries had similar leadership paradigms, whether Atatürk or Nasser. They were more than leaders or presidents. They both aspired at strong industrialization and economic independence. However, Nasser never focused on internal matters. Unlike Atatürk, who gave priority to internal issues such as security and built institutions. Efforts of Atatürk were compromised by followers. The same happened when Sadat cancelled any footstep taken by Nasser. It can be concluded that weak internal economy, division among social groups, weak institutions, and high illiteracy were reasons behind Egypt being backward economy. The country should consider its labor force, and improve human capital quality and education systems. Moreover, there should be recognition for a needed reform. The reform should be internally recognized, not externally imposed, to avoid any resentment. Moving to Turkey, the country has already achieved some success on economic performance. However, there should be consideration for political freedom and democracy. Frequent coups harmed the economy. Finally, general conclusion, and bibliography were provided.

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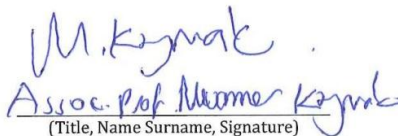
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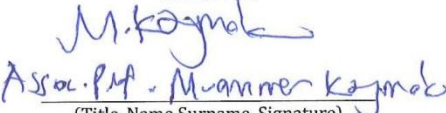
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6. APPENDIXES

6.1. Appendix 1: Ethic Board Waiver Form

 HACETTEPE UNIVERSITY GRADUATE SCHOOL OF SOCIAL SCIENCES ETHICS BOARD WAIVER FORM FOR THESIS WORK										
HACETTEPE UNIVERSITY GRADUATE SCHOOL OF SOCIAL SCIENCES TO THE PRESIDENCY OF ECONOMICS DEPARTMENT										
Date: 29/06/2016										
Thesis Title / Topic: "A Comparative Analysis Of Import Substitution Industrialization In Egypt And Turkey "										
My thesis work related to the title/topic above: 1. Does not perform experimentation on animals or people. 2. Does not necessitate the use of biological material (blood, urine, biological fluids and samples, etc.). 3. Does not involve any interference of the body's integrity. 4. Is not based on observational and descriptive research (survey, measures/scales, data scanning, system-model development).										
I declare, I have carefully read Hacettepe University's Ethics Regulations and the Commission's Guidelines, and in order to proceed with my thesis according to these regulations I do not have to get permission from the Ethics Board for anything; in any infringement of the regulations I accept all legal responsibility and I declare that all the information I have provided is true.										
I respectfully submit this for approval.										
Date and Signature 29.06.2016										
<table style="width: 100%;"> <tr> <td style="width: 30%;">Name Surname:</td> <td>Deena Saleh Hashad</td> </tr> <tr> <td>Student No:</td> <td>N12129429</td> </tr> <tr> <td>Department:</td> <td>Department of Economics</td> </tr> <tr> <td>Program:</td> <td>Master of Economics</td> </tr> <tr> <td>Status:</td> <td> ☒ Masters ☐ Ph.D. ☐ Integrated Ph.D. </td> </tr> </table>	Name Surname:	Deena Saleh Hashad	Student No:	N12129429	Department:	Department of Economics	Program:	Master of Economics	Status:	☒ Masters ☐ Ph.D. ☐ Integrated Ph.D.
Name Surname:	Deena Saleh Hashad									
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Status:	☒ Masters ☐ Ph.D. ☐ Integrated Ph.D.									
ADVISER COMMENTS AND APPROVAL Approve &  Assoc. Prof. M. Kyzmak (Title, Name Surname, Signature)										

6.2. Appendix 2: Originality Report

 HACETTEPE UNIVERSITY GRADUATE SCHOOL OF SOCIAL SCIENCES THESIS/DISSERTATION ORIGINALITY REPORT
HACETTEPE UNIVERSITY GRADUATE SCHOOL OF SOCIAL SCIENCES TO THE PRESIDENCY OF ECONOMICS DEPARTMENT
Date: 29/06/2016
Thesis Title / Topic : "A Comparative Analysis Of Import Substitution Industrialization In Egypt And Turkey " According to the originality report obtained by myself/my thesis advisor by using the Turnitin plagiarism detection software and by applying the filtering options stated below on 24/06/2016 for the total of 194 pages including the a) Title Page, b) Introduction, c) Main Chapters, and d) Conclusion sections of my thesis entitled as above, the similarity index of my thesis is 4 %. Filtering options applied: 1. Approval and Declaration sections excluded 2. Bibliography/Works Cited excluded 3. Quotes excluded 4. Match size up to 5 words excluded I declare that I have carefully read Hacettepe University Graduate School of Social Sciences Guidelines for Obtaining and Using Thesis Originality Reports; that according to the maximum similarity index values specified in the Guidelines, my thesis does not include any form of plagiarism; that in any future detection of possible infringement of the regulations I accept all legal responsibility; and that all the information I have provided is correct to the best of my knowledge. I respectfully submit this for approval.
Date and Signature 29.06.2016
Name Surname: Deena Saleh Hashad Student No: N12129429 Department: Department of Economics Program: Master of Economics Status: ☒ Masters ☐ Ph.D. ☐ Integrated Ph.D.
<u>ADVISOR APPROVAL</u> APPROVED.  Assoc. Prof. Muammer Kaymak (Title, Name Surname, Signature)