

Free Markets and Economic Performance: Turkish Experience

Mustafa ACAR¹ 

¹Prof. Dr., Necmettin Erbakan Üniversitesi, Siyasal Bilgiler Fakültesi, İktisat Bölümü, Konya, Türkiye acar70@gmail.com

Article Info	ABSTRACT
Article History Received: 03/10/2024 Accepted: 22/12/2024 Published: 31/12/2024 Keywords: Türkiye, free markets, free market economy, economic performance, Turkish economy, macroeconomics JEL Codes: E0, E2, E6	<p>There are basically two alternative models to organize economic activities and answer such fundamental questions as what, how, and for whom to produce: free market system based on individual decision making, and command system based on central planning. There has always been a friction and controversy between two types of mentalities in this regard: collectivist, statist, socialist mentality supported central planning, collectivist decision making, and government-controlled command economy. On the contrary, the individualist, capitalist, liberal mentality argued for free markets based on individual decision making where prices are determined by free interaction of market forces, i.e. supply and demand and the price mechanism. Even though the collapse of the socialist model showed the superiority of the free market system at a global level, many countries have difficulty to establish a truly free market system yet. In this context, this paper investigates Türkiye's journey towards free market economy and performance of the Turkish economy in recent decades. The country has been struggling to switch from a centrally planned to a free market economy since the early 1980s. It was not a smooth process though: there have been ups and downs, U-turns, and fluctuations. Turkish experience shows that economic performance goes up when pro-free market policies are implemented whereas it goes down when statist, collectivist, anti-free market type of economic policies are adopted.</p>

Serbest Piyasalar ve Ekonomik Performans: Türkiye Deneyimi

Makale Bilgileri	Öz
Makale Geçmişi Geliş: 03/10/2024 Kabul: 22/12/2024 Yayın: 31/12/2024 Anahtar Kelimeler: Türkiye, serbest piyasalar, ekonomik performans, Türkiye ekonomisi, makroekonomi JEL Kodları: E0, E2, E6	<p>İktisadi faaliyetleri organize etmek ve ne üretilmeli, nasıl ve kimin için üretilmeli gibi temel soruları cevaplamak üzere esas itibarıyla iki alternatif model vardır: bireysel kararlara dayalı serbest piyasa sistemi, merkezi planlamaya dayalı kumanda sistemi. İki zihniyet arasında bu bağlamda her zaman bir ihtilaf ve sürtüşme olagelmıştır: kolektivist, devletçi, sosyalist zihniyet merkezi planlama, kolektivist karar mekanizması ve devletin kontrol ettiği kumanda ekonomisini desteklemiştir. Bunun aksine, bireyci, kapitalist, liberal zihniyetse bireysel kararlara dayalı, fiyatların –arz, talep ve fiyat mekanizması gibi piyasa güçlerince belirlendiği- serbest piyasaları savunmuştur. Her ne kadar sosyalist modelin çökmesi serbest piyasa sisteminin küresel düzeyde üstünlüğünü göstermiş olsa da pek çok ülke gerçek anlamda bir serbest piyasa sistemi tesis etme konusunda zorluklar yaşamaktadır. Bu çerçevede, bu çalışma Türkiye'nin serbest piyasa sistemine geçme serüveni ve son on yıllarda Türk ekonomisinin performansını incelemektedir. Ülke 1980'lerin başından beri merkezi planlamadan serbest piyasa ekonomisine geçmeye çabalamaktadır. Ancak bu kolay bir süreç olmamış; inişli-çıkışlı, U-dönüşlerinin yaşandığı çalkantılı bir süreç olmuştur. Türkiye deneyimi göstermektedir ki, serbest piyasacı politikalar uygulandığında ekonomik performans yükselmekte, devletçi, kolektivist, anti-serbest piyasacı ekonomik politikalar uygulandığında düşmektedir.</p>

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INTRODUCTION

Economic activities such as production, consumption, distribution, saving and investment are necessary for human beings to survive and enjoy the bounties of life. Based on the historical experience, one can argue that there are basically two major alternatives on how to organize economic activities and answer such fundamental questions as what to produce and how much, how to produce, and for whom to produce. In other words, economic systems can be differentiated from each other depending on how they answer these fundamental economic questions.

In this context, historical experience shows that there are two main economic systems regarding the organization of the fundamental economic activities: socialist system and capitalist system. The socialist system is based on central planning, collectivist decision-making, state ownership of production factors, government-controlled economic activities on what, how and for whom to produce, and how prices are going to be determined.

On the contrary, the capitalist system is based on private property, individual decision-making, free markets, prices determined by the interaction of demand and supply, producers and consumers decide on what, how, and for whom to produce. We can call the first alternative as the *command system*, and the second one as the *free market system*.

On a still higher level, in a sense, we can argue that there are basically two types of mentalities with regard to looking at things, reading the economic, political and social reality surrounding us, interpreting the sources of knowledge, and shaping our lives: radical, authoritarian, statist, centralist and collectivist mentality on one hand, versus democratic, moderate, individualist, de-centralist, liberal mentality on the other. Actually, the economic systems are nothing but a reflection of these mentalities on economic reality. Democratic-moderate, liberal mentality is pro-freedom, free market and free trade that support economic and political freedoms, and prefers outward-looking policies. On the contrary, the radical, authoritarian, statist mentality is pro-central planning, collectivism, protectionism, and inward looking, focusing on “do nots,” bans, restrictions, and prohibitions.

From this perspective, as mentioned above, the free market system is simply a reflection of moderate-democratic-liberal mentality on economic sphere while the command system is simply a reflection of the authoritarian-statist mentality on economic grounds.

For a long period, in fact for more than half of the 20th century, soviet type of socialist, centrally planned, command system dominated a large part of the world including former USSR, Central and Eastern Europe, and China. Moreover, the idea of central planning was so attractive then that not only officially communist regimes but also some other democratic countries, including Türkiye, adopted central planning system under “5-year development plans” as well. However, the socialist central planning system collapsed at the end of 1980s, hence command system lost its attractiveness and many countries adopted pluralist democracy and free market economy.

As a country being lost for a long time between East and West, democracy and authoritarianism, central planning and free market system, Türkiye has been in search of adopting free market economic system since early 1980s. The process was not an easy and smooth one though; there have been fluctuations, hesitations, U-turns, ups and downs on the road. This paper investigates Türkiye’s journey toward establishing free market system and its economic performance in this period. The rest of the paper is organized as follows.

The next section will discuss the main pillars of a free market economy. Section 2 will give a brief summary of Türkiye’s journey toward establishing a free market economic system. Section 3 will focus on the economic performance of JDP governments in the last two decades.

1. FREE MARKET ECONOMY VS. COMMAND ECONOMY

As underlined above, there are two major conflicting perspectives on how to organize economic activities and who determines what to produce, how to produce and for whom to produce. These alternatives can be described simply as free market vs. command economy; capitalism vs. socialism, individual decision making vs. central planning. These models or systems actually do not come “out of

the blue,” but they are the reflections of two mind-sets: liberal vs. illiberal, democrat versus authoritarian mentality. In this section we will elaborate on the main institutions of a free market economy. Broadly speaking, one can argue that there are five main institutions or pillars of a free market economy, each of which are briefly explained below.¹

1.1. Five Pillars of a Market Economy

As elaborated by Acar (2021), one can argue that there are basically five fundamental institutions that characterize a free market economy: private property, freedom of choice and entrepreneurship, competition, free trade, and limited government. From an Islamic perspective, these institutions are perfectly compatible with basic Islamic tenets and teachings. In other words, Islam is compatible with free market system.

1.1.1. Private Property

Private property refers to the right of the individuals in an economy to own property, purchase and sell them as they wish, accumulate wealth as the fruits of their labor and skills. In a free market economy property is immune from the assault of others, protected by the law. This is such a key institution that without private property it is impossible to talk about economic freedoms and free market economy.

1.1.2. Freedom of Choice and Entrepreneurship

Another key institution of a free market economy is freedom of choice and entrepreneurship. The first part of it refers to freedom of consumers to spend their money wherever they would like to. In other words, in a free market economy consumers are free to choose among alternative goods and services (Friedman & Friedman, 2021). The second part of it refers to producers and entrepreneurs. In a free market economy, the businessmen, entrepreneurs or producers in general are free to invest their resources in the areas they prefer, produce goods and services they like to produce. The only boss over their decision to produce what, how much, or for whom would be consumers' demand. Therefore, in a free market economy the ultimate boss is the consumer. It is the demand by consumers that direct investment and production decisions.

1.1.3. Competition (Free Entry and Exit)

Competition is also a must, a necessary condition for a free market economy. In a sense, “free markets” mean free entry and exit. Those businessmen and entrepreneurs who would like to enter a market, industry, or sector are free to do so; no government permission is needed. If there is no competition, if entrepreneurs are not free to enter into and exit from the markets when they deem fit, we cannot talk about the existence of a free market economy. Competition stimulates better quality, lower production costs and efficient use of factors of production. Without competition we can expect lower product quality, higher prices, and hence lower level of welfare.

1.1.4. Free Trade

As its name implies, free trade means that individuals have the right to choose with whom to trade, at what price and how much they are going to buy or sell. Free market economy is an open-border economy where goods and services move across the borders freely. Without free trade where goods and services are exported and imported across borders in a competitive environment, one cannot talk about the existence of a free market economy. On the contrary, the statist, command economy's alternative to free trade is protectionism where government favors domestic industries, firms and producers. In other words, in a command or closed economy domestic firms are protected against foreign competition through trade restrictions in the form of tariffs, quotas, import bans, etc.

The debate over free trade versus protectionism has a long history that goes back to the mercantilist era (16th and 17th centuries). Since then there have been supporters of free trade and supporters of protectionism in every period and every country. Interestingly enough, both supporters of

¹ For more discussion and detailed information on free market vs. command economy, see, for example, Mises (2006); Smith (2020); Friedman & Friedman (2021).

free trade and supporters of protectionism developed several arguments for and against free trade and protectionism.

Among the arguments for protectionism are national security, self-sufficiency, infant industries, reducing unemployment, fair trade (“level playing field”), anti-dumping, preventing child labor, and environmental protection. Each one of these arguments sound good at a first glance, but as the proverb goes, “the devil is hidden behind the details.” When scrutinized closely through a critical evaluation, every single argument for protectionism collapses. For example, it is free trade, not protectionism, that links economies and allow them to develop friendly relations thereby reducing the possibility go into war by increasing the cost of war. Therefore, national security is better guaranteed by free trade and not protectionism. In short, it can be shown that free trade policies are superior to protectionism on both fronts: materially (lower prices, higher quality, larger supply and more variability, efficient use of resources, better technology and competitive power, hence higher welfare), and morally (in the form of peace, solidarity, friendly relations, individual dignity, more choices before individuals in every sense to live a more meaningful life).

1.1.5. Limited Government

Last, but not least, limited government is a must for a free market economy. A government dictating almost everything to the individuals on their production, investment-saving decisions and organizing their daily life is incompatible with free markets. From a classical liberal perspective, as underlined by Adam Smith (2020 [1776]) long time ago, the best government is the least government; that is, government is expected to be a night watchman, providing basic public services like internal and external security (“national defense”), justice and big infrastructure investments (health, education, and transportation). A limited government that provide basic public services in an efficient way and leave all the decisions on what to produce, how to produce, and for whom to produce can better serve the peace, tranquility and welfare of the citizens. By our very nature, as the mature and adult human beings we are not fond of being treated as immature, little children. We don’t need a government to command on what to do and what not, but we need a government to provide security and justice. The number of alternatives citizens would have are much larger when markets are allowed to function freely under a limited government focusing only on security, justice, and guaranteeing basic rights and liberties.

2. TÜRKİYE’S JOURNEY TOWARDS FREE MARKETS SINCE EARLY 1980s

Turkish Republic has been founded in 1923 on the ashes of Ottoman Empire (1299-1922), one of the largest, long-lasting, and powerful empires in history which collapsed at the end of the First World War (1914-1918). The Asia Minor or Anatolia where Turkish tribes started to settle down in 11th century (especially after 1071 A.D. when Turks defeated Byzantium army in Malazgirt, Eastern Anatolia) has been a point of attraction and hence both a battle field and a cradle for many civilizations since the ancient times. Phrygians, Assyrians, Urartu’s, Hittites, Roman Empire, Byzantium Empire, Kurds, Arabs, Ottomans, and Republic of Turkey are among the inhabitants of Anatolia where followers of all major beliefs, i.e. Christianity, Judaism and Islam, lived together for centuries.

In terms of economic policies implemented and the perspective on free market versus central planning or statism, modern history of Turkish Republic can be divided into six parts: single party regime (1923-50), Menderes period (1950-60), planned period (1960-80), Ozal period (1980-93), 28 February period (1993-2002), and Erdogan/JDP period (2002-24). Below, each one of these periods are described briefly.

2.1. Single Party Regime (1923-1950): Nationalism, Statism, Protectionism

Founders of the Turkish Republic were mostly motivated by nationalistic feelings hence they preferred statist, inward-looking development strategies based on protectionism and government control. Since most of the non-Muslim industrialists and bourgeoisie of the Ottoman times were lost due to wars and population exchange afterwards, they wanted to create “domestic bourgeoisie” by implementing protectionist, closed-border policies where foreign competition was prevented through import bans and high tariffs. After relatively liberal policies in the aftermath of the Lausanne Treaty (the founding legal document for the emergence of Turkish Republic signed in 1923 with the major global

players of the time and the winners of WWI), Türkiye adopted statist, inward-looking, protectionist policies as soon as the Great Depression of 1929 erupted. These protectionist policies aiming at self-sufficiency were implemented until 1950 when Türkiye switched from a single party to multi-party democracy under the pressure of the Western powers as part of the conditions for admitting Türkiye's demand for joining Nato and the Western Club.

2.2. Menderes Period (1950-1960): Struggling to Open up

Adnan Menderes, president of Democratic Party who won elections in the early 1950 and came to power and served as the Prime Minister of the country until the military coup of 1960, was a liberal-minded person who believed the merits of free markets and openness. He tried to change the political structure and economic policies towards opening up the economy to external world, allowing imports and foreign capital, etc.

However, his power and the infrastructure for a full-fledged free market policies were rather limited, political atmosphere was not suitable, hence he did not manage to change many things in the direction he hoped for. Especially in the 2nd half of the 1950s the political climate became very unfavorable, military commanders started to show unrest, street demonstrations erupted against non-Muslim minorities, and this period came to an end with the May 27 military coup in 1960. With this military coup Türkiye entered a period of "military guardianship" regime where the army intervened in the political affairs either directly or indirectly and frequently.

The cost of military interventions between 1960 and 2016 cannot be exaggerated: it cost thousands of lives, loss of human resources, innocent people put in jail, democratic institutions were shut down, suspended or abolished, the rule of law was set aside, political environment became unfree, oppressive, suffocating. Accordingly, market forces, private industries and entrepreneurs did not find a suitable atmosphere to flourish.

2.3. Planned Period (1960-1980): Statism and Central Planning

The period between 1960 and 1980 can best be described as the "planned period," because right after the military coup of 1960, a set of soviet-type of central planning and statist policies were started to be implemented. State Planning Organization (SPO) has been founded (1961) and "five-year development plans" were initiated. Contrary to a free market system, the government bureaucrats decided in this period on the place and the amount of investments instead of entrepreneurs and market forces. In other words, Türkiye, even though described as a capitalist, democratic country on the paper, has been implementing Soviet-type central planning since the early 1960s. Therefore, she was quite right when the former Prime Minister Tansu Ciller said in the mid-1990s that the communist system collapsed in the USSR, but still continues in Türkiye!

But central planning and protectionism was not remedy to economic problems faced by the country. In the second half of the 1970s economic outlook was characterized by scarcity of goods and services, queues in front of the stores, high inflation, and lack of foreign exchange reserves to finance imports. In former Prime Minister S. Demirel's words, "the Treasury was in need of even 70 cents!" In other words, the economy was in a deadlock, and the statism and protectionism was not a remedy. Mr. Ozal, Undersecretary of SPO in the early 1980s, Prime Minister and President later on, offered an alternative way: free market economy.

2.4. Ozal Period (1980-1993): Market-oriented Reforms

The period between 1980 and 1993 can be called as the "Ozal period" because it was late Mr. Ozal who designed, coordinated and implemented the free market reforms in this period as a top-level bureaucrat first, prime minister and the president later on. No doubt that Mr. Ozal was the single most pro-free market and liberal-minded leader Türkiye has ever had so far. He strongly believed the merits of free markets and open borders. All other political leaders that played a role in ruling the country in recent decades, including N. Erbakan, B. Ecevit, S. Demirel, A. Turkes, T. Ciller, M. Yilmaz, and Erdogan, were either directly against free market economy or had to accept it under pressure of the urgent conditions. It is interesting to see how practical and pragmatic most of the political leaders are,

i.e. changing direction easily when the conditions change, prefer to be “a man of opportunism” rather than being “a man of principle.”

Mr. Ozal, being the designer of the “24 January Stability Program,” initiated a set of market-oriented reforms first in the early 1980, and then as a prime minister (1983-89) and the president (1989-93). These reforms included opening up the economy to the outside world, liberalization of foreign trade and capital movements, switching to a flexible exchange rate regime, changing the development strategy from *import-substitution* to *export-led industrialization* policies. He encouraged private enterprises and entrepreneurs to get organized and open to outside markets. He ended government monopolies in certain industries, initiated the privatization process, and encouraged private sector to invest in certain industries such as health, education and the media. He also took steps to start the full-membership application of Türkiye to join the EU as a full member.

Thanks to these reforms, the country started to flourish in many fronts and almost all economic indicators improved in this period. This is a typical example proving that free market-oriented policies make a better job in increasing welfare and improving economic indicators.

2.5. The Lost Decade or 28 February Period (1993-2002)

The reason this period was named as “28 February” was that on this particular date (1997) the military generals put forward an ultimatum to the democratically elected Erbakan-Ciller coalition government to initiate a set of harsh measures against “irtica” (to topple down the religious-conservative associations, movements and enterprises), or resign otherwise. Thus, the coalition government had to resign in the following days because Erbakan was a religious-conservative leader and it was impossible for him to execute the orders coming from the military officers.

A puppet government was set up by the parties who were eager to implement these harsh measures. As New York Times’ famous journalist Thomas Friedman properly put it, Türkiye was “the most beautiful country in the world ruled in the worst possible way” in the rest of the decade.² A number of political, economic and legal measures were initiated to force the Muslim women covering their heads as part of their belief were forced to leave their schools, they were not allowed to take the university entrance exams, many people were forced to leave their jobs, positions and institutions because of their political-religious views, etc. Many Muslim-conservative businessmen and public employees were subject to negative discrimination for their life-style or political views.³

The perpetrators and initiators of the 28 February process claimed that it would last “a thousand years,” but as a universal economic law states, “intervention to the market has certain unforeseen and unintended consequences” (Acar, 2018). It actually came to an end when Erdogan emerged as a young, charismatic, energetic, ambitious political leader playing the role of the representative of those who were victimized in this process of illegality and oppression.

2.6. Erdogan (JDP) Period (2002-24): Swinging Between Free Market and Statism (Command System)

It is interesting to see how the same leadership can change and take U-turns within the same ruling period, a typical example of which is the Erdogan period in Türkiye. Justice and Development Party (JDP) has been ruling Türkiye since late 2002. Even though the composition of the Cabinet has changed from time to time, Mr. Erdogan has always been there as the leader of the government either as prime minister (2003-2014) or the president (2014-2024).

² He made this fantastic, strikingly accurate remark in the heydays of 28 February process at the end of 1990s during a seminar he delivered at Purdue University (1998) as an invited speaker when myself was among the audience as a PhD student at the Department of Economics.

³ Personally I was among the victims of 28 February process being subject to mobbing and negative discrimination as well. For instance, I was not allowed to join another university, I was not given permission to serve as a consultant to top-level bureaucrats or politicians, and our managers did not recognize the academic titles (associate professor) I received from the legal academic authorities (UAK) and withheld the implied financial remunerates, etc. There were simply thousands of examples facing the same difficulties.

Based on the attitude towards free market vs. command, free trade vs. protectionism, outward vs. inward-looking policies, this period can be clearly divided into two: pro-free market period (2002-2013), and anti-free market period (2014-2024). Following the footsteps of late Ozal, JDP governments followed pro-free market policies in the 1st decade based on market oriented, outward-looking, free trade policies accompanied by major economic, political, and legal reforms, taking EU-related homework seriously and initiating the necessary reforms.

However, this reformist, charming, democratic-liberal period came to an end in the early 2010s. Due to a number of internal as well as external factors, JDP leadership changed their attitude more towards anti-free market, authoritarian, statist, protectionist, inward-looking policies since 2014. Among those factors are Gezi Park events (2013) FETO-related internal unrest and destabilization (15 July 2016 coup attempt), terrorist attacks in the south eastern regions, “one-minute” incident (deteriorating relations with Israel since 2009), challenging and self-ordained foreign policy against Nato and global forces, hence deteriorating foreign relations, miscalculations on the course of the Arab Spring, unproportional risk-taking appetite on regional and global conflicts accentuated by economic and political costs of the Syrian crisis. One can add more to this list as leaving independent Central Bank and financial discipline aside, rapidly increasing government expenditures, huge public deficits and resulting extraordinary monetary expansion in the aftermath of the Covid-19 pandemic, increasing uncertainty and country risks, reducing predictability. As economists underline frequently, when there is no political and economic stability, when uncertainty and risk is high, the businessmen and entrepreneurs will be reluctant to make new investments, which negatively affect employment opportunities and growth.

This policy shifts are clearly reflected by the course of economic indicators and economic performance of the country. As will be discussed in detail in the next section, the 1st period can quite possibly be described as a success story whereas the 2nd period is exactly the opposite.

3. ECONOMIC PERFORMANCE UNDER JDP RULING (2002-2022)

In this section we will critically evaluate the course of main economic indicators in Turkish economy under Erdogan or JDP administration since the early 2000s. These indicators include economic growth, GDP per capita, inflation, unemployment, budget deficit, current account balance, interest rates, FX rates, and FDI inflows.⁴

3.1. Economic Growth

Real economic growth is one the most important economic indicators reflecting whether total production in an economy is increasing, decreasing or stagnant. Increasing production is an indication for lively economic activities and increasing welfare, and vice versa.

As can be seen from Figure 1 below, economic growth in the last two decades has been quite volatile with several ups and downs. It showed severe negative growth (depression) in 2001, the year of the biggest economic crisis in the republican history, and 2009 which was due to global economic crisis triggered by the subprime mortgage crisis of 2008-09. One can see clearly the downward trend in real economic growth between 2010 and 2020. In other words, economic growth process in the 2000s is characterized by volatility, instability, and downward trend recently.

⁴ More can be found in Acar (2022) on the performance of Turkish economy in the 2000s. On a broader spectrum, Erdem *et al.* (2009) critically evaluate the macro economic performance of the governments in Türkiye between 1950 and 2007.

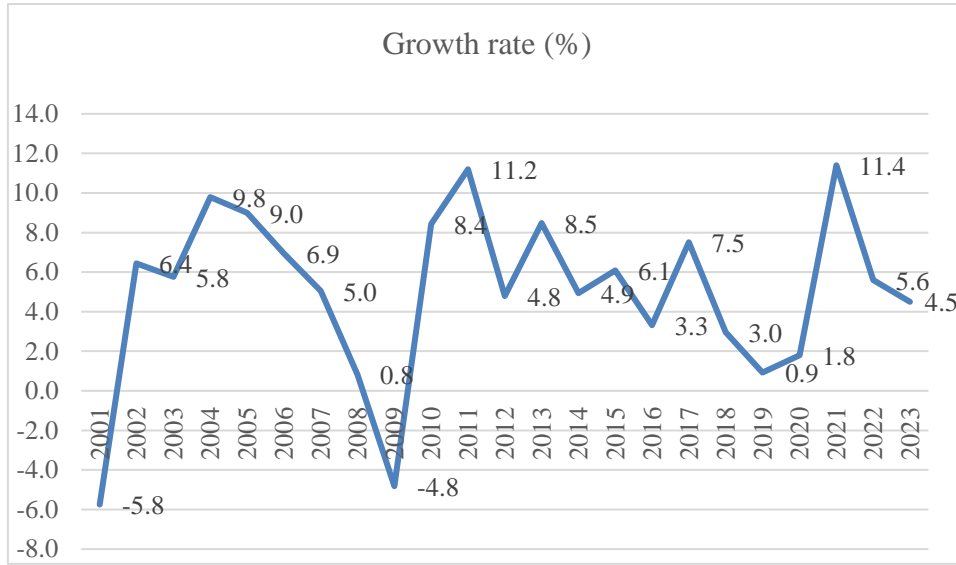


Figure 1. Real Economic Growth (2001-2023, % change over previous year)
Source: Turkstat (2024).

3.2. GDP per capita (\$)

GDP per capita is considered to be the most important indicator of average welfare level in a given economy. There can be richer and poorer social segments, but GDP p.c. shows on the average how well an economy is doing and how rich or poor is an ordinary citizen on average. Increasing GDP per capita means a country is getting richer and more prosperous.

One can see from Figure 2 that GDP p.c. has steadily increased from 2001 until 2013 where it reached a peak in the republican history (\$12 614). Afterwards, it started to fall down until 2020. As of 2023, GDP p.c. was able to reach where it was ten years ago, i.e. its 2013 level, which makes the last decade a stagnant period.

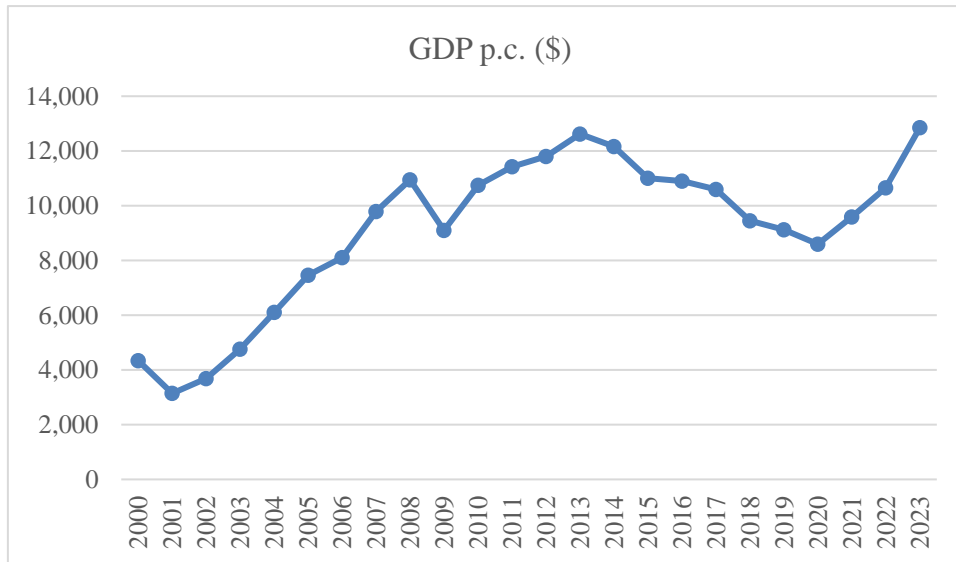


Figure 2. GDP per capita (2000-2022, \$)
Source: World Bank (2024), IMF (2024).

3.3. Inflation (CPI, %)

Inflation is a critical economic indicator to show whether there is price stability or not and the direction of life expenses. Existence of price stability means predictability, being able to make accurate calculations on the possible profitability of prospective investments, etc. On the contrary, if there is no

price stability, if inflation is high, that means there is no predictability, it is impossible to make accurate calculations or predictions on the profitability of the investments, hence leading to less investments and lower economic growth.

As Friedman & Friedman (2021) put it properly, inflation has many negative consequences: it reduces the efficiency of the price signals, lowers efficient use of resources, deteriorates income distribution to the detriment of lower and fixed-income earners. Surprise inflation causes unfair income transfers between the debtors and the creditors, and between employees and employers. In other words, inflation harms both consumers and producers, negatively affecting the growth performance of an economy. The only winner in an inflationary situation is the government who creates inflation by printing money through inflation tax, seignorage, and reduced real value of its debts. Figure 3 shows that inflation has always been a problem in Türkiye since the early 2000s, but at least it moved within single digits in the 1st decade of JDP ruling and it became out of control after 2017.

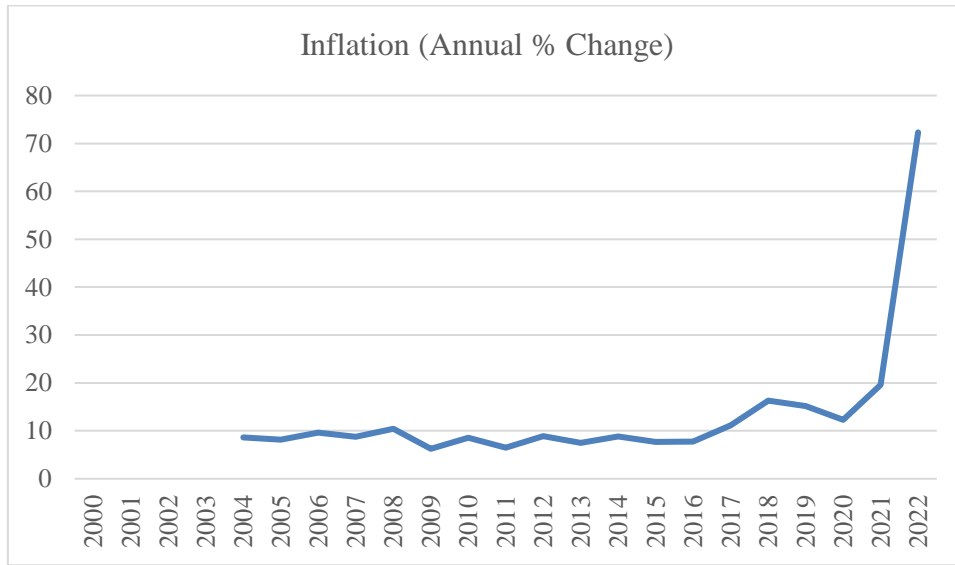


Figure 3. Inflation (CPI, 2000-2022, % change over the previous year)

Source: Turkstat (2024).

3.4. Unemployment

Unemployment is also among the critical indicators showing how successful an economy is in creating new job opportunities. A growing, lively, or booming economy where entrepreneurs are eager to make new investments there will be more new employment opportunities and job-creation, hence lower unemployment rates, and vice versa.

As figure 4 shows, unemployment rate has been fluctuating between 8.3% (2012) and 13.7% (2019), falling in the period 2009-12, and increasing in the period 2012-19. It should also be stressed that the youth unemployment is about twice as high, and “broadly defined” unemployment (i.e. when people who quit looking for a job due to despair are included in the labor force) is much higher than these figures.

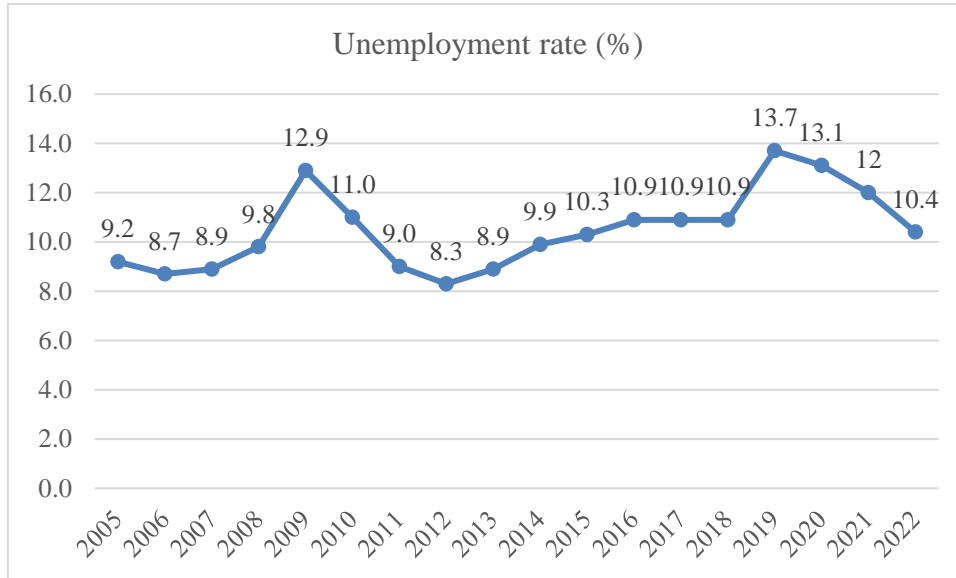


Figure 4. Unemployment (2005-2022, % of labor force)
Source: Turkstat (2024).

3.5. Budget Deficit

Budget deficit is a critical indicator that shows how well is a government doing in terms of balancing government expenditures with government revenues. The ideal state is a balanced budget where expenditures are financed by revenues, hence no need for new taxes, borrowing, or printing money as the worst alternative to finance budget deficits. In other words, growing budget deficits are dangerous in that they lead to public finance deficits which can be handled by only 3 ways, each of which has its own defect: increasing taxes reduces purchasing power of the citizens, internal borrowing leads to higher interest rates and hence lower investments (crowding out), external borrowing narrows the maneuver capability of the country in terms of adopting an independent foreign policy, and lastly, printing money leads to inflation which can be described as some sort of unjust taxation and robbing of the citizens by the government.

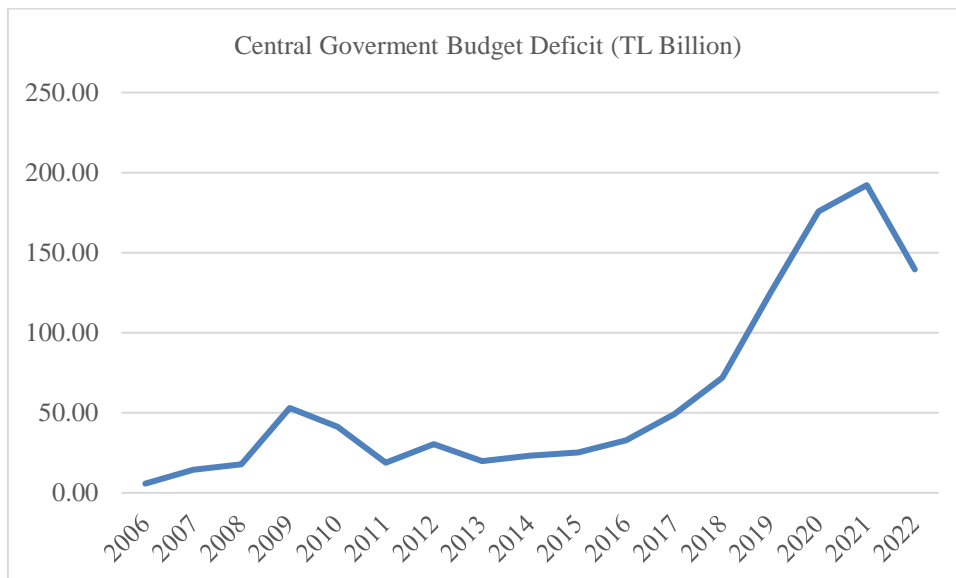


Figure 5. Central Government Budget deficit (TL Billion, 2006-2022)
Source: TC CB Strateji ve Bütçe Başkanlığı (2024).

Figure 5 shows that financial discipline has been lost after 2013 where central government's budget deficits grew tremendously reaching a peak at 2021 with TL200 billion. This has been one of the root sources of high inflation in Türkiye in recent years.

3.6. Current Account Balance

Current account balance (CAB) reflects the net result of a country's economic relations with the outside world in a given period, mostly taken to be a one-year period. It includes 4 major items: foreign trade balance, capital account balance, change in reserves and net errors and omissions. Broadly speaking, the accounting method of the current account is such that the deficit in foreign trade (merchandise & services trade, unrequited transfers), is balanced with a surplus in capital account (FDI and portfolio investment flows); if emerges, the gap is closed by a change in FX reserves, assuming no major error and omission.

As can be seen from Figure 6 shows, current account deficit has been quite volatile in the last two decades in Türkiye, swinging between as lower as zero (2001, 2019, i.e. the crisis years) and as high as \$74 billion (2011, i.e. high growth year). It shows a parallel course to economic growth increasing with high growth rates. In 2022 the amount of current account deficit was nearly \$50 billion. The main causes of high CA deficits are insufficient domestic savings, energy gap (i.e. oil and natural gas imports), high dependency to imported inputs.

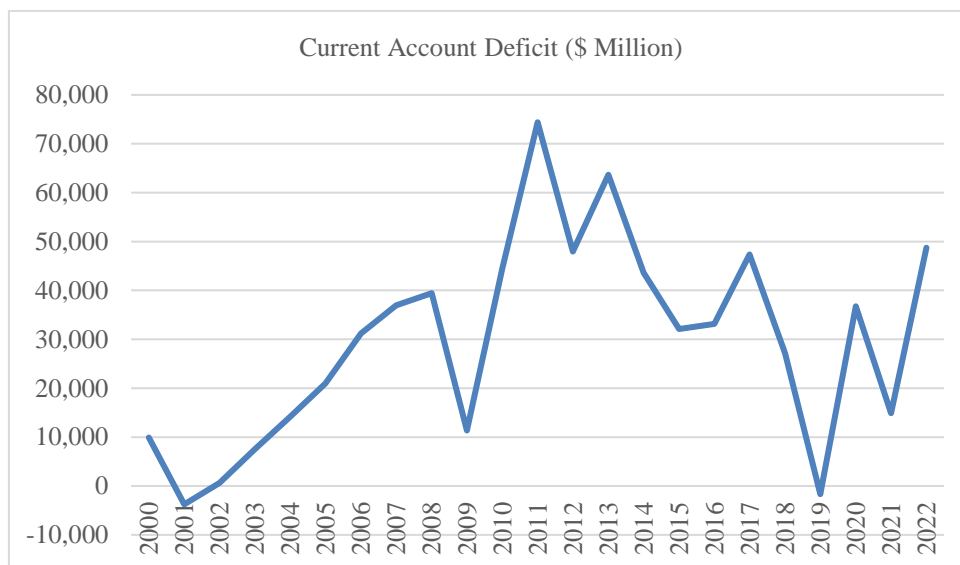


Figure 6. Current Account Deficit (2000-2022, \$ Million)

Source: TC CB Strateji ve Bütçe Başkanlığı (2024).

3.7. Interest Rates

Turkish political leadership has been sensitive to lowering the interest rates as something forbidden in Islamic teachings. Apart from a philosophical-intellectual discussion whether the “riba” (Qur’anic term used to denote usury) and “interest” in modern sense is the same thing in every sense, it is part of our reality that interest is given and taken in our daily economic affairs.⁵ Figure 7 shows that in general interest rates declined when the economy was showing a lively performance until 2010, started to increase after 2013 where other economic indicators started show a negative course.

Contrary to economic rationality and sound orthodox economic theory suggesting to implement tight monetary policy when there is high inflation, Turkish political authority intervened to the financial market in the opposite direction. Central bank policy interest rates were forced to be reduced under political pressures after 2018 from 22,5% in 2018 to 7,5% in 2022. The advocates of this so-called (and later abandoned) “Turkish model” argued that lower interest rates, and resulting high FX rates (expected depreciation of the domestic currency) would result in higher investments, higher growth, less external borrowing, lower current account deficits, etc. However, this irrational policy did not produce the good results announced and hoped for. On the contrary, FX rates jumped (as shown by Figure 8), expectations

⁵ It is worth thinking and needs reconsideration whether the classical Qur’anic term “riba” coincides with today’s concept of interest used in banking and financial markets of the modern economies. There are a number of plausible reasons to think that they are quite different. See Ozturk and Sahin (2021) for an important discussion on riba versus interest.

deteriorated, inflation and current account deficit increased rapidly. This policy is given up only recently and the Central Bank policy rate (i.e. one-week repurchase, or CB's lending rate) was gradually increased to 50% in the aftermath of 2023 general elections when the top-level economic authorities were changed.

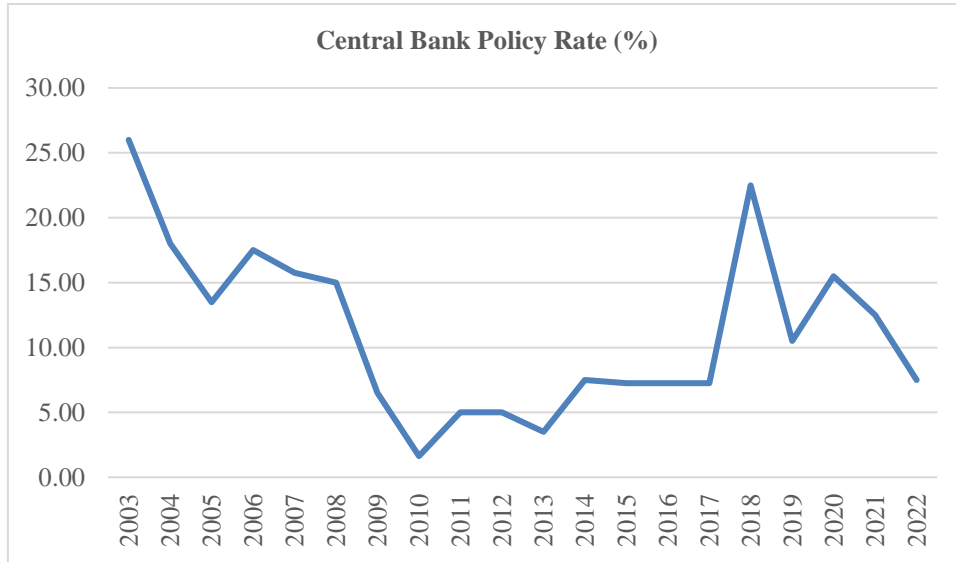


Figure 7. Interest Rates (Central Bank Policy/1-week Repo Rate, %, 2003-2022)
Source: Central Bank (TCMB) (2024).

3.8. FX Rates (Currency Depreciation)

Foreign Exchange (FX) rates show the purchasing power of one currency against other currencies. If an economy grows, FX earnings increase and current account balance shows a surplus, then the currency representing that economy appreciates, i.e. its purchasing power increases. The opposite is true when an economy goes into crisis, shows negative growth and current account deficit, then the local currency depreciates.

This reality is reflected clearly in Figure 8 below: Turkish currency kept its value more or less stable, even slightly appreciated when the economy showed a lively course until 2013. After that TL started to depreciate against USD when other economic indicators were also deteriorating. Notice that after interest rates were politically forced to be reduced in 2018, depreciation rate has accelerated clearly.

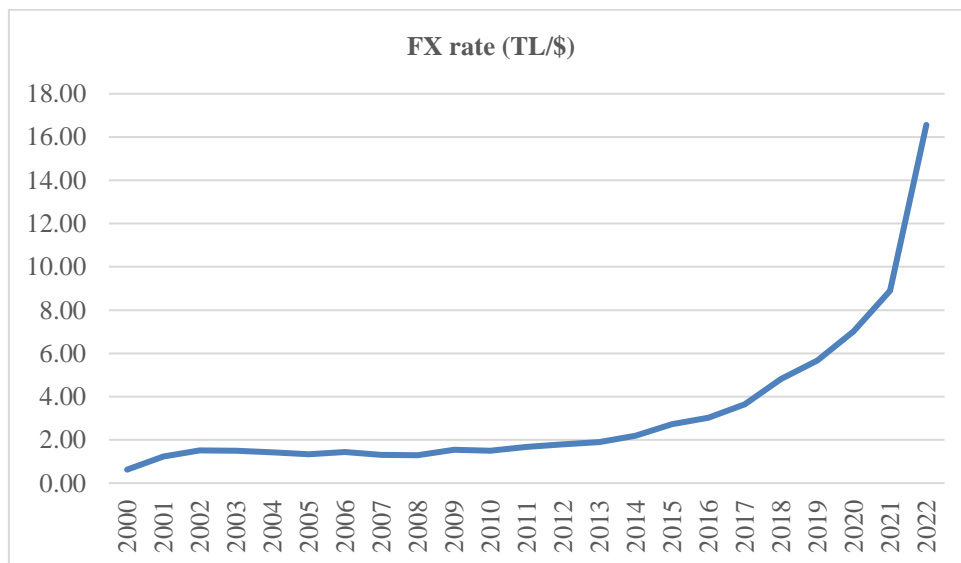


Figure 8. Foreign Exchange Rates (Depreciation of TL against \$, 2000-2022)
Source: Central Bank (2024).

3.9. FDI Inflows

Foreign Direct Investments (FDI) are critical for the developing countries who would like to have a growing economy, hence need growing investments, but does not have enough resources to finance the investments necessary for economic growth. This is especially true for a country like Türkiye where domestic savings are not sufficient to finance domestic investments. Traditionally internal savings rate (domestic savings as percent of GDP) is around 15% where the investment rate (as percent of GDP) is nearly 20% in Türkiye, which accounts for the nearly 5% current account deficits in the long run.

As depicted by Figure 9, FDI inflows showed a volatile course in Türkiye in the last two decades. It showed a lively course in the 1st decade and jumped from \$1.1 billion in 2002 to reach its peak at \$22 billion in 2007 when Türkiye started full membership negotiations with the EU. But it slowed down in later years to fall as low as \$7.8 billion in 2020, slightly increasing afterwards.

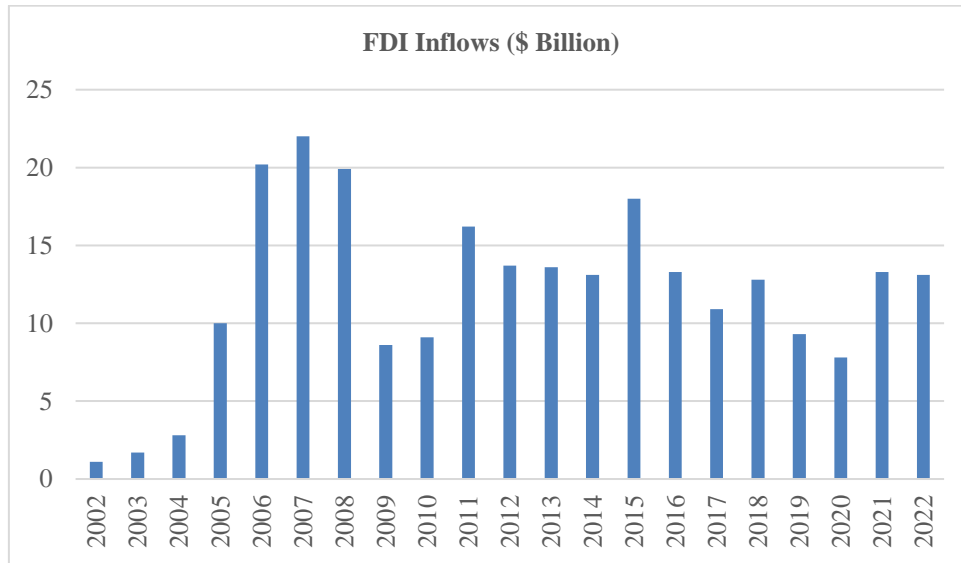


Figure 9. FDI Inflows (\$ Billion, 2002-2022)

Source: Sanayi ve Teknoloji Bakanlığı (Ministry of Industry and Technology) (2024).

3.10. General Economic Performance by Period Since 1980s

As mentioned above, as far as the economic perspective adopted and policies implemented are concerned, the recent history, i.e. 1980 and onwards, can be divided into four distinct periods: The Ozal period (1980-93), 28 February period (1993-2002), 1st Erdogan period (2002-13) and 2nd Erdogan period (2013-23).

The Ozal period and the 1st Erdogan period were characterized by relatively more market-oriented, outward-looking policies based on free markets, free trade, less market interventions. On the contrary, 28 February period (1990s) and the 2nd Erdogan period were characterized by more government interventions, protectionism, inward-looking, anti-free market and anti-free trade policies. As shown by Acar (2022, 2023), in general economic performance improves with free market, free trade and outward-looking policies and it goes down with anti-free market policies (Table 1).

Table 1. *The Course of Economic Indicators in Türkiye (1980-2023)*

Indicator	1980	1993	2002	2013	2023	Ozal period (1980-1993)	Feb.28 Process (1993-2002)	1 st Erdogan period (2002-2013)	2 nd Erdogan period (2013-2023)
GDP (billion \$)	90.7	238.4	230.5	951	1119				
Growth (GDP, %)*						7.7	-0.37	13.75	1.64
GDP p. c. (\$)	2 041	4 116	3 492	12 480	13110				
Growth (pc GDP, %)*						5.54	-1.81	12.28	0.49
Growth (X, %)*						13.65	10	13.95	5.16
Unemp. (%)	8.6	9.4	10.8	9.7	9.1				
Inflation (CPI, %)	94.3	75.6	29.7	7.4	64.8				

(* Annual average. Source: Acar (2023), Turkstat, Ministry of Treasury and Finance.

Table 1 demonstrates clearly that economic performance goes up with pro-free market policies and falls down with anti-free market policies. As such, real annual average economic growth was much faster (7.7%) in the Ozal period (1980-93) characterized by free market reforms than February 28th Process (1993-2002) where Turkish economy experienced negative growth (-0.37%). Similarly, real economic growth was much faster (13.75%) in the 1st Erdogan period (2002-2013) characterize by freedoms, free market reforms and change than in the 2nd period (1.64%). Similar trends have been observed with regard to p.c. GDP, export growth, and inflation.

CONCLUSION

This paper argues that there are basically two types of mentalities shaping our world-view, the way we look at, see and interpret things, extract judgments from our experience and realities we face: authoritarian, radical-salafi mentality, and moderate, democratic-liberal mentality. In harmony with these two types of mentalities, there are two major economic systems human beings have developed so far: command system and free market system, or the socialist system and the capitalist system. In other words, free market economy and command economy are simply reflections or natural results of these two fundamentally different mind-sets on economic and political grounds.

The socialist, command economic system is based on collectivist decision-making, central planning, prices determined by government bureaucracy, government controlled economic activities and the public authority deciding on what, how and how much to produce. As a much better alternative, free market system is based on individual decision-making, market forces or demand and supply determining prices and answering the questions what, how and for whom to produce. Free market economy has five pillars: private property, freedom of choice and entrepreneurship, competition, free trade and limited government. The superiority of free market system over command system can be shown both on material, factual, historical grounds, as well as moral, philosophical, and intellectual grounds. It leads to higher level of welfare, faster growth, bigger wealth as well as it provides a larger set of choices before individuals in every sense.

In reality, there is not a hundred percent free market system with no government intervention and prices determined solely by demand and supply. Yet we can talk about countries adopting more pro-

free market policies versus those adopting more of a central planning, anti-free market, statist policies based on central planning and frequent government intervention.

After trying a closed, centrally planned, inward-looking policies based on protectionism and import-substitution development policies, Türkiye switched to free market system in the early 1980s under the wise leadership of late Ozal, a determined liberal-democrat leader strongly supporting free market system.

But this process was not an easy and smooth one. There have been road accidents, back-and-forths, U-turns and fluctuations on the road. As such, 1990s can be described as a 'lost decade' in terms of anti-free market and anti-freedom policies, statism, protectionism, government interventionism and discriminations.

More interestingly JDP ruling since the early 2000s can be divided into two different periods. The first decade, between 2002-2013 was more of a pro-free market, less interventionism, more free trade, reformist and liberal period. From 2013 onwards, however, there was a U-turn due to certain internal as well as external factors and government adopted more of an anti-freedom, anti-free market, statist, inward-looking economic policies. The course of main economic indicators fluctuated accordingly. Our findings based on the official figures show clearly that economic performance rises with pro-free market policies and falls with anti-free market ones.

As a policy implication of our findings, we suggest that political authorities return to the reformist, pro-freedom and free trade, outward looking, free market economic policies with minimal government intervention and maximum playing ground for entrepreneurs and individual decision-makers.

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