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Regulatory regime change in Turkish banks: Reactive or proactive?

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ABSTRACT

This paper examines the positive contributions made toward restructuring the regulatory framework of Turkey's banking and financial sectors prior to and post the 2000–2001 financial crisis. Drawing on a framework initially developed by Onis and Senses (2007, 2009) and further referred to by Onis (2009, 2010) it argues that financial reforms undertaken by the Turkish government would not have been successful without the strong support of domestic coalitions. While the external pressures put on the Turkish government from the International Monetary Fund, The World Bank and the European Union for financial reforms were necessary to kick start the reforms as a reactive process, these pressures on their own may have served only the interests of financial business elites at the expense of the broader stakeholders. Empirical data for the study was collected from documentary analysis of key financial institutions and interviews with twenty major Turkish regulatory agents and other stakeholders. The paper then discusses how the perceptions of these stakeholders are embodied into, and have influenced, regulatory regime change in Turkey from a reactive state to a more proactive one.

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1. Introduction

The purpose of this paper is to examine the legislative and policy responses to global corporate governance scandals in Turkey and to evaluate their potential impact on the Turkish domestic regulatory landscape through in-depth interviews with a wide range of stakeholders in the Turkish banking sector and other sectors affected by the changes in the regulatory regime. Prior research has paid inadequate attention to capturing the roles of institutional and regulatory factors in the Turkish regulatory framework. Twenty in-depth interviews with key regulatory actors in Turkey provide political and economic imperatives for successful institutional reforms in Turkey. It is suggested that the regulatory functions of the Turkish state have improved since the financial crisis of 2000–2001. Prior to the crisis, the Turkish regulatory framework had reacted to external pressures imposed by the International Monetary Fund (IMF), the European Union and the World Bank. However, since the financial crisis, it is argued that a domestic coalition of regulatory agents, banks and public companies that have become increasingly dependent on foreign capital has contributed significantly to the development of a more sustainable regulatory framework in Turkey.

The paper examines regulatory change in Turkey during a transition period when Turkey was harmonizing its regulatory framework with the European Union following the financial crisis of 2000–2001. Crises often demonstrate that the existing regulatory system is not sustainable and that policy and structural changes are needed. The first section of the paper therefore highlights the background of the Turkish political landscape and economy leading up to the financial crisis of 2000–2001. Section 2 is concerned with regulatory reforms in terms of the provision of financial reporting, capital market reforms and especially reform of the banks. Some of the pertinent outcomes of these reforms are also discussed in this section. Section 3

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Table 1
The cabinets and ruling parties (1993–2003).

Political parties	Ruling period
DYP-SHP	21.11.1991–25.06.1993
DYP-SHP	25.06.1993–05.10.1995
The minority government was not approved by the Parliament	05.10.1995–30.10.1995
DYP-CHP	30.10.1995–06.03.1996
ANAP-DYP (minority government with support from DSP)	06.03.1996–28.06.1996
RP-DYP	28.06.1996–30.06.1997
ANAP-DSP-DTP (minority government with support from DSP)	30.06.1997–25.11.1998
DSP	11.01.1999–28.05.1999
DSP-MHP-ANAP	28.05.1999–18.11.2002
AKP	28.11.2002–23.03.2003
AKP	23.03.2003 onward

Source: The official website of the Turkish Grand National Assembly, 2011 (http://tbmm.gov.tr).
Notes: DYP, Dogru Yol Partisi; SHP, Sosyal Halk Partisi; CHP, Cumhuriyet Halk Partisi; RP, Refah Partisi; ANAP, Ana Vatan Partisi; DSP, Demokratik Sol Partisi; DTP, Demokratik Toplum Partisi; MHP, Milliyetci Harekat Partisi; AKP, Adalet ve Kalkinma Partisi.

describes the banking reform in Turkey, addresses its processes and nature and provides insights into key regulatory actors. Section 4 reports the results of reforms and ends with some concluding remarks.

2. The background of the Turkish political landscape and economy

From 1993 to 2002, Turkey experienced political and financial instability. Since November 2002, Adalet ve Kalkinma Partisi (the AK party) has been in power, and the government has remained relatively stable. This section highlights some of the main political and economic characteristics of this period, together with some significant macroeconomic indicators.

2.1. Cabinets and ruling parties

From 1993 to 2003 the Turkish political system was characterized by frequent changes of political parties participating in coalition governments with other minority parties.

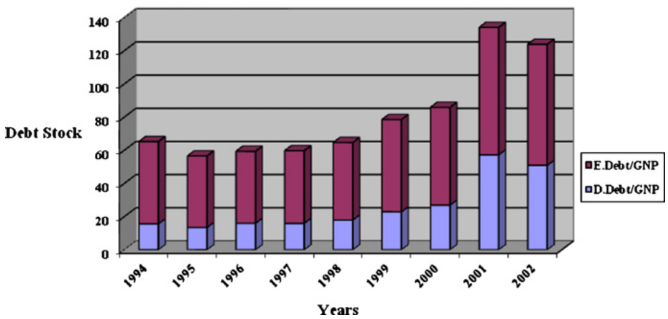
A full list of governing cabinets and political parties from 1993 to 2003 is shown in Table 1.

Notably, during this period, no Turkish government served for more than 3.5 years, even in instances when they were elected for a 5-year term. One of the possible results of this instability was chronic inflation during the 1990s. Fiscal dominance, composed mainly of a budget deficit and unsustainable debt stock, was believed to be the main determinant of this high inflation. The economy became unstable and suffered from crises as a result of its unsustainable debt dynamic and the unhealthy structure of the financial sector. Sporadic state intervention, chronic inflation and high public deficits were the main factors that repressed the development of Turkish financial markets. However, it was also argued that the corporate and banking sectors might be forced to choose external foreign funding over domestic funding with higher interest rates, which would have increased the need for fair reporting, transparency and improved corporate governance (World Bank, 2003).

Table 2 depicts the dramatic changes in debt dynamics during the last decade. In 1994, the ratios of domestic and external debt to gross national product (GNP) were 15.62% and 49.59%, respectively. By the end of 2002, these ratios had increased to 50.96% and 72.92%, respectively.

We now turn to some of the unsuccessful economic policies pursued by the Turkish government prior to the financial crisis in 2000–2001. In December 1999, the government introduced an exchange rate-based stability program with the

Table 2
Debt stock in Comparison with GNP.



Sources: The Under Secretariat of the Treasury, 2011 and the State Institute of Statistics.

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