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**ENHANCING COMPETITION
IN A POST-REVOLUTIONARY ARAB CONTEXT:
DOES THE TURKISH EXPERIENCE
PROVIDE ANY LESSONS?**

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Abstract

The purpose of this paper is to explore the possible role of the regulatory environment in enhancing competition in the post-revolutionary Arab societies, drawing on the experience of Turkey in the last decade. It provides a review of some institutional measures, which include remedies such as privatization, delegation of authority (in particular to relatively independent regulatory agencies), a competition law and its enforcement, liberalization, stakeholder participation in governance and monitoring, and open and non-discriminatory procedures for public procurement. The remedies also include forms of public-private participation schemes in order to attract private capital to finance the provision of public services, especially in infrastructure. In this paper, these remedies will be referred to as the competition-enhancing reform package. The paper uses Turkey as the main example from which useful lessons can hopefully be learnt.

JEL Classification: K2; K3

Keywords: Regulatory Environment; Competition; Law; Turkey

ملخص

الغرض من هذه الورقة هو استكشاف الدور الذي يمكن للبيئة التنظيمية من تعزيز المنافسة في المجتمعات ما بعد الثورة العربية، استنادا إلى تجربة تركيا في العقد الماضي. تستعرض الورقة بعض التدابير المؤسسية، والتي تشمل العلاجات مثل الخصخصة، وتفويض السلطة (ولا سيما وكالات تنظيمية مستقلة نسبيا)، وهو قانون المنافسة وإنفاذها، والتحرير، ومشاركة أصحاب المصلحة في الحكم والرصد، وإجراءات غير تمييزية للمشتريات العامة. وسائل الانتصاف تشمل أيضا أشكالا من مخططات المشاركة بين القطاعين العام والخاص من أجل جذب رؤوس الأموال الخاصة لتمويل الخدمات العامة، وخاصة في البنية التحتية. في هذه الورقة، سيتم الإشارة إلى هذه العلاجات باسم مجموعة الإصلاحات لتعزيز المنافسة. تستخدم الورقة تركيا كمثال رئيسي للدروس المفيدة.

1. Introduction

The purpose of this paper is to explore the possible role of the regulatory environment in enhancing competition in the post-revolutionary Arab societies, drawing on the experience of Turkey in the last decade. The pre-revolutionary regimes in these countries are often perceived to entail a distorted form of competition where firms with political connections have the upper hand, and where profitability results not from productivity but from privileged access to scarce resources controlled by the political authority or from politically established barriers to competition. It is well accepted that long-term growth, on the other hand, requires a system where creative destruction can work its way. This requires a policy and regulatory framework that constrains political authority in such a way so as to limit arbitrariness and discrimination in policy toward firms and ensures more equal access to politically controlled resources. The regulatory framework needs also to redirect public authority to address various market failures so as to reduce barriers to entry, and, in particular, to prevent anti-competitive behavior and foreclosure by dominant firms. More generally, transition to a more competitive environment requires institutional measures to ensure that state power is used to maximize citizens' welfare rather than the welfare of state elites and/or their constituencies.

This paper will provide a review of these institutional measures. These measures—or new rules of the game—include remedies such as privatization, delegation of authority (in particular to relatively independent regulatory agencies), a competition law and its enforcement, liberalization, stakeholder participation in governance and monitoring, and open and non-discriminatory procedures for public procurement. The remedies also include forms of public-private participation schemes in order to attract private capital to finance the provision of public services, especially in infrastructure. In this paper, these remedies will be referred to as the competition-enhancing reform package.

Significant variability across different jurisdictions notwithstanding, it would be fair to say that this reform package has gained global acceptance over the last three decades. Several developments have been instrumental in this. One important factor has been technological change, in particular the emergence of the possibility of introducing competition to industries that had until then been organized as state monopolies, for example electricity and telecommunications. The possibility of introducing competition did not mean that anti-competitive behavior no longer posed problems. The need to constrain anti-competitive behavior created a necessity for a new regulatory framework so that new entrants could have a chance of survival and gain market share. Another widespread reason was the desire of many governments to reduce the burden of infrastructure investments on the public budget and attract private investments instead. Although this “public finance” motivation for the reform package has been underlined for emerging economies, the literature suggests that it was an important consideration in the case of developed economies as well. A parallel development has been a tendency to seek contractual forms to shift the provision of various public services from within agencies of central or local governments to the private sector, in the hope that competition would enable the provision of these services more efficiently. International organizations such as the World Bank and the IMF expressed dissatisfaction with the performance of public enterprises, and the political mood in some countries reflected a similar disappointment and saw privatization as a solution.

These components of competition/liberalization, private participation and privatization were emphasized to different degrees in different jurisdictions. Hence the overriding concern in the European Union (EU) as a whole has been competition/liberalization, as well as the formation of a single market, and the emphasis on privatization has differed significantly across member states. The privatization component was emphasized in many World Bank and IMF programs in developing and transition countries, partly reflecting the ideological shifts in the post 1980 environment, and partly reflecting the need to generate public revenues

to help resolve fiscal and financial crises. It would be fair to say that the reform package and especially its privatization component are being subject to a more critical assessment now.¹

An important political dimension of the reform package has been the delegation of substantial regulatory rule-making and enforcement power from ministries and ministerial departments to what have been called independent regulatory authorities (IRAs). Several normative and positive explanations have been advanced for this transfer of power, including the insulation of the regulatory process from short term political influence, deployment of mechanisms of credible commitment to reduce fears of expropriation, ensuring that state intervention is implemented in a non-discriminatory manner and without favoring firms with political connections, and enhancing the state's ability to attract the necessary human capital for complex regulatory tasks. Delegation of rule-making authority to IRAs was also meant to reduce the discretionary powers of the political authority and attain a more rule-based and transparent framework for economic policy.

The paper will use Turkey as the main example from which useful lessons can hopefully be learnt. The country is an interesting example because it has adopted many elements of the reform package in the last two decades or so. Hence one can ask: To what extent have these institutional changes produced the desired results? Have adoption of new laws and establishment of IRAs really created a more competitive environment? Or were these changes merely cosmetic? It is hoped that a critical review of Turkey's experience may provide lessons about the likely outcomes of similar institutional changes elsewhere.

The paper is organized as follows. Section 2 will review the content and institutional set-up of a competition enhancing reform package. Section 3 will present an overview of the Turkish experience. On the basis of that experience as well as suggestions from the literature, Section 4 will discuss some tradeoffs and challenges in pursuing reform. Section 5 will conclude.

2. A Competition Enhancing Reform Package

The adoption of the elements of the competition-enhancing reform package in most developing countries occurred as part of a transition from an economic policy regime where the state played a direct role in allocating resources to one where the market mechanism was given a more prominent role. From a normative point of view this required a new system of rules, or an overall regulatory framework to ensure that the market mechanism worked properly and that various forms of market failures were addressed.

2.1 The content

In most countries, at the heart of this new regulatory framework lies competition law which applies across industries a set of rules that outlaws anti-competitive agreements among firms and prevents dominant firms from exercising market power in an abusive manner. The main logic and language of competition law has also been more or less applied to other industries previously organized as public monopolies and which have been liberalized to allow entry by new players and where market structure makes it especially easy for incumbent players who own or control the basic infrastructure facilities (such as transmission and distribution networks, or fixed or mobile telecommunications infrastructure) to foreclose markets to these new players. However, in these so-called network industries competition law has been seen as insufficient to ensure effective competition and most countries have enacted sector-specific regulations that constrain the behavior of incumbents in an ex-ante manner and that ensure new players non-discriminatory access to network facilities.

¹ See, for example, Roland (2008) on privatization in general and Estache et al. (2009) for reform in utilities.

In industries where the service in question does not allow meaningful competition among multiple service providers and where it is desired that the private sector play an active role in the provision of the public service in question, mechanisms have been developed to ensure that the concession in question is awarded to those private players who are most fit. Hence the logic of competition has also been extended to public procurement. As stated by one observer “the main principle in public procurement is to facilitate open and non-discriminatory competition with free entry” (Limi 2011, 121). This is probably an oversimplification, since from the government’s perspective the procurement process starts with a decision about whether to produce the service in question in-house or whether to engage the private sector in its provision. This is then followed by an ownership decision: should the assets be owned by the government or the private sector, and if by the latter, for how long? Still, it would not be a mistake to state that the logic of a competitive process has become more prominent in the search for desirable mechanisms of procurement. In particular, designing procedures that are “open and non-discriminatory” has become an important principle that guides governments.

2.2 The institutional setup

Replacing direct and often discretionary state control with new forms of control through rules and procedures corresponds to a major realignment in the structure of the state and in the way state power is deployed. What made this restructuring even more drastic has been the specific institutional form that has accompanied it. In most countries adoption of the reform package has been accompanied by the establishment of IRAs which have been delegated the power to design and implement many of these new rules and procedures. Competition laws are enforced through independent agencies almost everywhere in the world, and IRAs have been established for network industries and other industries where market failures are apparent such as financial markets and banking industries and even other areas where governments interact with the private sector such as public procurement.

The literature has identified a number of reasons behind this delegation of authority:

1. Independence from the political realm is necessary so that regulatory objectives are differentiated from other political objectives. For example, the regulation of prices to contain monopolistic abuse should not be contaminated with other objectives such as fight against inflation (Ugaz 2002). Overall price stability is more effectively attained through other (monetary and fiscal) policies.
2. Efficient regulatory decisions can require a long-term outlook and politicians often have shorter term horizons (Ugaz 2002).
3. An independent body, relative to a ministry directorate, is more effective at providing regulatory credibility and commitment. Both are necessary to reduce the risk of expropriation in general but also specifically to reduce the risk of discrimination in favor of politically connected investors. Delegating the power of regulatory authority to an IRA that is not under the direct control of the political authority may be an effective institutional measure to generate this credibility.
4. Sector specific regulation often requires expert skills that may be difficult to attract within the confines of current personnel regime and pay scales of the public administration. Relatively independent bodies may be established with their own personnel policies.

In what sense are IRAs supposed to be independent? First they are expected to be independent from politicians. The literature has emphasized a number of formal conditions, discussed below, that characterize political independence, but it is also emphasized these *de-jure* conditions do not in themselves ensure *de-facto* independence. Independence also refers to independence of IRAs from the firms that they regulate or other interest groups that have a

stake in regulation. The term “capture” is often used to refer to influences by various players that make regulatory activity produce results that are different from those that serve the public interest, whichever way the latter is defined. Estache and Wren-Lewis (2010a) distinguishes between *capture of decisions* and *capture of information*, where the former refers to interest groups’ direct influence on decision makers and the latter to ability to withhold information and prevent it from being disclosed so as to appropriate information rents. They also distinguish between *ex-ante* and *ex-post* capture: ex-ante capture refers to interest groups’ efforts to influence laws and regulations whereas ex-post capture occurs within the existing legal framework (e.g. effort to inflate costs to get higher rates).

In reference to formal conditions of political independence the literature emphasizes the following (e.g. Thatcher 2011). First, independence means that the IRA can act without the approval of the ministry and that the ministry cannot overturn a regulation or decision handed over by the IRA. It also means that if the politicians want to change the behavior or the aim of IRAs, they have to do this by enacting laws rather than issuing instructions. Second, regulators cannot be dismissed by ministers at will, except on the basis of wrongdoing or incapacity. Typically regulators are appointed (or in some jurisdictions elected) for a fixed term. Whenever regulators are run by boards rather than a single director, there are often recommendations that board members should be appointed in a staggered manner. The third condition emphasized in the literature is financial independence. This usually means that the budget of the authority should not be at the discretion of the government. This condition is often implemented through earmarked taxes or special revenues earmarked to the agency such as license fees or penalties. Of course, even when these conditions are met, politicians may affect regulatory decisions through various means. For example, since in many jurisdictions appointment of regulators is a political process, this may give politicians the opportunity to appoint individuals who are likely to have similar preferences or who are more susceptible to influence.

IRAs are not meant to be completely independent from the political realm; after all their creation is a political act (often a constituting piece of legislation). The general formulation is that the determination of policy is carried out in the political realm and the task of the IRA is to design, implement and enforce the secondary legislation through which the policy is realized. Independence from the political realm also does not mean that IRAs are not accountable. Again, the literature lists a number of measures to ensure accountability. A classic list is provided by Smith (1997, 1):

- Rigorous transparency—including open decision-making and publication of decisions and the reasons for those decisions
- An appeals process
- Scrutinize the agency's budget, usually by the legislature
- Prohibit conflicts of interest
- Subject the regulator's conduct and efficiency to scrutiny by external auditors or other public watchdogs²

These can be taken as the basic measures to ensure the independence and accountability of IRAs. The institutional design of IRAs contains additional variables or dimensions that need to be decided on and how variations along those dimensions are likely to affect IRAs’ performance has been a subject of debate. These dimensions will be discussed in the sequel.

² Indeed, the Turkish experience, discussed below, provides compelling examples about how these elements may make a crucial difference in the performance.

3. The Experience of Turkey

Turkey's transition to a market oriented policy regime started in the 1980s. Before that Turkey was pursuing a model of import substitution industrialization with widespread state intervention through direct production and various forms of price controls, subsidies and directed credit. The economic presence of the state notwithstanding, however, the role of the private sector was important. In fact, the objective of state intervention was partly to help develop private industry, and private industry did develop albeit in a highly concentrated, oligopolistic and internationally uncompetitive manner.

Hence when Turkey started to move towards a more market oriented economic policy regime in the 1980s, there was already a relatively developed private sector led by diversified holding companies owned by dynastic families. Most of these holding companies actually developed starting in the 1950s. This followed a move from a single party to a multi-party regime—a decision taken in 1945—and in the election in 1950 the opposition won with a landslide and there was a change in the government. In any case, although not independent of the state and possibly highly dependent on it for capital accumulation as well as critical inputs, by the 1980s the private sector in Turkey was an important locus of economic and social power.³

*3.1 From discretionary capitalism to institutional reform*⁴

In the 1980s barriers to international trade and finance were reduced or removed, so were controls on domestic financial markets and more specifically on the banking system. However during the 1980s and 1990s governments in Turkey did not show a deep interest in developing a solid legal and regulatory framework for a market economy.⁵ This was especially true for the financial markets. The liberalization of the capital account itself was carried out without the approval of the central bank (and against warnings that liberalizing international finance under conditions of macroeconomic instability was not a good idea). The banking sector expanded rapidly without an effective system that would ensure that excessive risk-taking would be curtailed. This was especially relevant given the availability of arbitrage opportunities provided by borrowing in foreign currency and investing these funds into domestic assets, especially government securities bearing high real interest rates, reflecting some sort of collusion between the banking industry and fiscally profligate governments (Alper and Onis 2004). The weakness of regulation of the banking system not only encouraged excessive risk-taking, but also allowed several cases of gross corruption where banks assets were siphoned off by bank managers and owners (Atiyas and Emil 2005). Along with deterioration of public finances (see below) the weaknesses in the banking system was among the primary triggers of the financial crisis of 2000-2001.

Attempts to privatize state assets were undertaken through half-baked laws and often through decrees with the force of law. Governments basically tried to give substantial discretion to the executive or to specific agencies controlled by the executive, on the procedures and methodologies to be followed in the privatization process; in effect, they would have allowed governments to pursue privatizations in unaccountable and un-transparent ways. Most of these efforts were met by annulments by the Constitutional Court, in most cases on the grounds that the laws or decree-laws effectively transferred legislative authority to the executive: in other words, the Constitutional Court demanded that details of the procedures to be followed during privatizations, the options available regarding privatization methods and the like should be explicitly stated in the law and should not be left to the discretion of the

³ Ersel (2012).

⁴ This section borrows from Atiyas (2012).

⁵ An important exception is the enactment of a competition law, see below.

executive. In short, then, in the choice between rules versus discretion, the governments of 1980s and 1990s were clearly in favor of discretion.

Throughout the 1990s there were attempts to pursue privatizations or private participation in telecommunications and electricity without first establishing a regulatory framework to contain the exercise of monopoly power or to ensure the development of competition. With regards to the energy sector, governments tried to attract private capital through various contractual schemes entailing⁶ monopoly rights and government take or pay guarantees. Some of these contracts were awarded without a competitive tender procedure. These contracts have been later investigated by the High Court of Accounts and criticized for high costs, possible irregularities and incompatibility with competitive markets (Atiyas 2005). The contingent fiscal liabilities generated by these contracts also caused concerns.

What happened in the fiscal area during the 1990s can be best characterized by fragmentation and disintegration. The political science literature on Turkey has emphasized the importance of populism and patronage in political competition. In terms of fiscal policy, this means that the use of public resources to nurture political support is a central instrument of political competition. This puts pressure on public finances and creates a strong tendency to generate public deficits. Towards the end of 1990s budget “unity” broke down completely: there were various forms of off-budget expenditures, especially through state-owned banks in the form of support for agriculture and small enterprises. The real magnitude of these quasi-fiscal expenditures and their implied burden on the budget and public debt were at the time not shown in official statistics and disclosed to the public. It is generally accepted that hidden public debt also played an important role in the events leading to the crisis of 2000-2001.⁷

Overall, then, it can be said that while the scope of state intervention decreased in the 1980s and 1990s relative to the previous few decades, this period was nevertheless characterized by discretionary rather than a rule based policy environment. There were important initiatives during this period which were exceptions to this characterization. The first was the establishment of the Capital Markets Board (CMB) in 1982 to develop and regulate securities markets in Turkey. The CMB was the first independent regulatory authority (IRA), and, as discussed by Atiyas and Ersel (1994), it was evident that, since it entailed delegation of significant rule-making authority away from the government and ministries, it represented a counter-example to the centralization of policy making authority that characterized most of the 1980s and 1990s. One possible explanation for this move is the rapid and uncontrolled growth of non-bank financial institutions from 1980-81, which subsequently resulted in the “bankers’ crisis” of 1982, and lead to a loss of popular confidence in the non-bank financial system. CMB was seen as necessary to restore the confidence without which capital markets could not develop. The development of capital markets was seen in turn as a necessary component of the economic transformation the country was going through in the post-1980 period.

The second initiative was the enactment of a competition law in 1994 and the establishment of the Competition Authority in 1997. These moves can be explained by Turkey’s commitments under the Customs Union with the EU in 1996. Indeed, as will be discussed in more detail below, the path towards EU accession (as well as pressures from international agencies such as the IMF and the World Bank) played major roles in the evolution of Turkish economic institutions.

⁶ These were schemes involving Build Operate Transfer, Build Operate Own and Transfer of Operating Rights.

⁷ One could say that emergence of corruption in the financial sector and the disintegration of fiscal institutions were expressions of a more general institutional decay going on in the country as reflected in the emergence of para-military illegal gangs to pursue murders on behalf of the state or the overall Susurluk scandal involving the close relationship between the state and organized crime.

The program that was launched after the crisis of 2000-2001 entailed a number of significant institutional measures. In a way, the program adopted the “second generation reforms” proposed by international organizations such as the IMF and the World Bank, but by and large the reforms also coincided with those that Turkey had to pursue as a country in the process of accession toward membership to the European Union. Many of these reforms which were part of the recovery program launched in 2001 were adopted without much change and even extended by the AKP government that came to power after the elections of 2002.

One of the most important steps undertaken in the reform program was to introduce independence of the central bank. A supportive fiscal policy stance played an important role in the success of monetary policy. A Public Financing and Debt Management Law adopted in 2002 subjected all central government borrowing and guarantees to strict rules and imposed reporting requirements on all debts and guarantees. The Public Financial Management and Control Law passed in December 2003 consolidated all fiscal operations of the government in an integrated general government approach, from the preparation to the closing stages of the budget. It also envisaged a three-year budget framework. These are measures that substantially improve fiscal control and transparency of the budget process. To the extent that any expenditure has to be executed within an established budget process and in a transparent manner, and therefore would be scrutinized by the public, it can be said that these measures also limit the discretionary powers of the executive. Overall the governments in the post-crisis era have been very successful in implementing a large fiscal adjustment even though observers have identified a significant number of slippages in the implementation of the new fiscal framework (Dedeoglu 2010).

Another critical dimension of the post-crisis program was strengthening the supervision and regulation of the banking system. The Banking Regulation and Supervision Authority (BRSA) was established in 1999 but its powers were significantly increased after the crisis. It has engineered a massive recapitalization of the banking system and has earned a reputation for being a strong regulator, a sharp contrast with the weak regulatory environment in the previous two decades. Tight regulation of the banking system is generally seen as a major factor behind the resilience of the financial sector in Turkey during the 2008-2009 global crisis.

Regarding competition proper, as mentioned above, a Competition Law, modeled after that of the EU, was already enacted in 1994 as part of a Customs Union with the EU. The Competition Authority is recognized to be a professionally competent and relatively independent agency, not only by domestic stakeholders, but by international peers as well (OECD 2005). The decisions of the Competition Board are required to be publicly available and published with justifications, which increases the transparency and accountability of the agency. This may have created an added source of discipline that has improved its performance. Maintaining independence may have also been easier due to the fact that it functions across many industries and does not deal in a continuous manner with a specific enterprise or groups of enterprises, a situation that could have facilitated capture.⁸ This does not mean that there are no shortcomings: there are instances of favoritism towards state owned enterprises, inconsistencies in decisions across cases or over time, insufficient or sometimes deficient economic analysis, excessive formalism and the like. Nevertheless these shortcomings do not change the basic fact that overall the agency’s decisions are seen to be

⁸ One should point out that most observers single out another important factor that may help explain the degree of professionalism of the Competition Authority: the high quality of the bureaucrats who were initially appointed as line managers and who have shaped the emerging culture of the agency.

free of systematic bias and to meet a minimum level of quality, at least relative to the rest of the RAs in Turkey.

In the area of privatization, by the end of the 1990s the legal infrastructure was almost complete. In effect, the executive had been forced to reduce the degree of administrative discretion and establish more transparent and accountable procedures for privatization. In addition, as discussed below, by 2001 legal regulatory frameworks were also established for the deregulation and privatization of industries which were hitherto dominated by public monopolies, namely telecommunications and energy. While privatization revenues generated until 2000 were below \$9 billion, more than \$30 billion has been raised between 2001-2010 (Onis 2011). Among privatized assets were large enterprises in industries such as petrochemicals, petroleum refinery, telecommunications, electricity distribution, banking, and alcohol and tobacco products.

Overall, privatizations in Turkey have been revenue-driven. The problem with revenue-driven privatizations is that the governments may overlook competition problems or indeed may endow enterprises to be privatized with monopoly rents in order to increase privatization revenues. The Competition Authority has been involved in the privatization process and has been able to influence some privatization transactions to ensure that measures are undertaken to reduce competition problems that may arise once assets are turned over to private ownership. For example during the privatization of Turk Telekom the Competition Authority has required that the provision of internet services be organized as a separate legal entity and that the cable TV infrastructure be separated from Turk Telekom. More recently, the Competition Authority has prevented investors from owning both gas and electricity distribution companies in the same region. The idea here was that under separate ownership gas and electricity distribution companies may enter each other's business areas and thereby give rise to a competitive process, whereas placing them under the ownership of a single investor will prevent the development of this form of competition.

In industries characterized by natural monopoly segments such interventions by the Competition Authority have limited influence on market outcomes; ultimately the evolution of market structure depends on the existence and effective implementation of a regulatory framework that protects competition, ensures access to network facilities by new entrants, presents exclusionary and discriminatory behavior by incumbents, etc. As discussed below, these competition-enhancing aspects of institutional change in industries characterized by competition problems have not been very strong in Turkey.

In the telecommunications industry, at the risk of oversimplifying, the story is one of substantial capture by the fixed line incumbent operator. The Telecommunications Authority (now the Information and Communications Technologies Authority, ICTA) was established in 2001 and Turk Telekom was privatized in 2005. Privatization has possibly resulted in a significant increase in productivity of Turk Telekom: Employment was reduced by almost 50 percent after privatization, reflecting the extent of politicization and over-employment under state ownership. However, Turk Telekom maintains dominance in the broadband internet services market (over 90 percent market share) as well as long distance and International calls markets (more than 50 percent market share). Until very recently Turk Telekom was protected from competition by high interconnection rates, delays in the licensing of new entrants, delays in the introduction of services that would allow new entrants greater command over the range of services that can be provided over the fixed line network. To most observers, these outcomes reflect Turk Telekom's influence over the Ministry of Transport and by consequence, over the IRA. While the telecommunications laws contained standard measures that have ensured ICTA's de-jure independence, the authority's de-facto independence was significantly curtailed (Atiyas and Doğan 2010).

However, the stance of the ICTA in the mobile industry provides an interesting contrast. Compared to the fixed segment the ICTA has adopted a more competitive stance in the mobile segment, as reflected, for example, in interconnection rates which have been quite low by international standards. Atiyas and Doğan (2010) argue that this may reflect the fact Turk Telekom's subsidiary is a new entrant in the mobile telecommunications markets. The interesting point here is that, if the ICTA's more aggressive pursuit of competition in the mobile industry can indeed be explained by political economic factors, this stance was carried out through the established rules of the game (i.e., lower interconnection rates) rather than by more coarse and discretionary interventions. In other words, the ICTA's tendency to favor Turk Telekom was curtailed by the new rules and had to be mediated by an overall more competitive stance. This suggests that perhaps the new rules did have some bite after all.

In electricity, the restructuring process in Turkey started with the adoption of the Electricity Market Law in 2001 which envisaged unbundling of distribution, transmission and generation assets, establishment of non-discriminatory access to the transmission and distribution networks and the formation of Energy Market Regulatory Authority (EMRA), the IRA responsible for electricity, natural gas and oil industries.

The electricity restructuring process has been driven by privatization. Privatizations themselves have been structured so as to generate maximum possible revenues for the government. As a result, competition and consumer welfare has taken a secondary role, since there is a danger that high purchase prices will eventually reflect themselves in higher consumer prices. Privatizations have been delayed significantly, and privatization of generation assets, where productivity increases are most likely to occur as a result of competition, has not even started. Hence, in fact, ten years after the launch of the restructuring process, the extent of competition is still limited to about one quarter of generation capacity, the rest of the capacity being either under non-competitive contracts inherited from the past, or under government ownership. Moreover, the government is still perceived to be quite active in setting some of the retail prices while in principle this should be under the authority of the EMRA.

It should be stressed that it is not government ownership of these assets that prevents the development of competition: there are examples of countries where governments own significant parts of generation assets but still have competitive markets. What Turkey could have done is to horizontally break up and corporatize these assets, place them under competent management and give them the mandate of behaving in a competitive manner. The primacy of privatization as the driving force of the restructuring process has precluded this option.

These problems notwithstanding, the restructuring model *has* been successful in attracting new investments in capacity by the private sector without any non-competitive contracts, of the order 3-4000 MW each year since 2008. This is largely due to the fact that under the new model a wholesale market was established where prices are determined by supply and demand. In effect, the establishment of a wholesale market meant that the government relinquished a significant tool that could in principle be used for expropriation or favoritism.

In the area of procurement, Turkey has adopted a Public Procurement Law (PPL) in 2002, largely modeled after the EU Public Procurement Directives. Again, the accession process has been an important motivation in the adoption of the Law, and ostensibly in the many amendments that have been implemented since then. The PPL permits domestic preferences; there is a price advantage of up to 15% for domestic contractors offering domestic products. In procedures for contracts below the thresholds, contracting authorities may restrict participation to Turkish companies. The number of amendments since has been high, and as reported by SIGMA (2008) "some of these amendments were introduced on an ad hoc basis

by individual ministries and Parliamentarians rather than as part of an overall government strategy. These amendments have introduced exemptions that had not been envisaged under the *acquis communautaire*.” Importantly, private sector utilities (in the water, energy, transport and telecommunications sectors) are not covered in the PPL. The PPL also established a Public Procurement Authority. SIGMA’s (2008) assessment of the PPA was that it was a “stable and strong institution. It has already largely contributed to the establishment of a modern public procurement system and, in general, has the capacity to implement procurement legislation effectively.” Recently investigations were launched against some PPA staff and a member of the Board on the grounds that they have accepted bribes from business people and engaged in corruption in close to 100 public tenders.

In most cases discussed above, the delegation of regulatory authority to a relatively independent agency resulted in an overall increase in the transparency of the policy making process. Even though there are variations across IRAs, they generally work in a more transparent manner relative to ministries: putting draft regulations up on websites for public consultation has become routine. To different degrees, the decision making processes of IRAs are bound by procedural rules that are encoded in regulations; such rules reduce discretion and enhance predictability. The Competition Agency and the ICTA are required to provide justifications for their decisions. Requiring IRAs to provide justifications for their decisions makes a major contribution to transparency and accountability and makes judicial reviews more effective and credible. Even though implementation differs across agencies (more effective implementation in the case of the Competition Authority), this requirement allows stakeholders to be more demanding in terms of transparency.

There is one area where developments regarding transparency and accountability have been in the reverse direction, and that is the case of the Housing Development Administration (TOKI). TOKI is directly attached to the Prime Ministry. It builds public housing with the collaboration of private contractors. It has free access to public land and wide discretionary powers over land that is under its control. Construction activities of TOKI are exempt from the Public Procurement Act; TOKI is also exempt from the Public Financial Management and Control Law. It has been reported that its assets have reached about 2% of GDP, though financial information about its activities is hard to find because of lack of financial reporting.⁹ While most of the IRAs reported above are audited by the High Court of Accounts (*Sayıştay*), which reports to the Parliament, TOKI is audited by the High Audit Board (*Yüksek Denetleme Kurulu*), which is attached to the Prime Ministry, implying that the financial transactions and activities of TOKI are not being audited by an independent body. It is also known to be an efficient developer and has built over half a million residences, 85% of which consists of social housing. In short, TOKI has the ability to manipulate land rent in a highly discretionary and non-transparent manner meanwhile supporting a network of construction companies.

3.2 Assessment

The review presented above suggests a number of comments. The first has to do with the role of crises. The fact that economic crises facilitate or sometimes trigger a process of economic policy reform has been emphasized frequently in the literature and in that sense Turkey is no exception. It is interesting to note that central bank independence, regulation of the banking system and measures that enhanced the controllability of the budget figured prominently in the aftermath of the crisis of 2000-2001 as these were among the most problematic areas prior to the crisis. The second aspect that needs to be emphasized is the role of international agencies and especially of the European Union. The IMF and the World Bank played a significant role in the adoption of the reform laws in many areas including

⁹ See Atiyas (2012) for more details.

telecommunications and electricity, but the prospect of membership to the EU played a crucial role: It increased acceptance of and created legitimacy for reform and at the same time it vastly reduced transaction and bargaining costs among stakeholders in Turkey by providing templates of what was largely perceived as best practices in a wider range of areas including telecommunications, energy, competition law, banking and public procurement. Third, it is clear that the Turkish experience towards a more rule-based policy environment has been an uneven process. Even though most IRAs were given formal independence, de-facto independence varied significantly across agencies. Still, even in cases where independence was more nominal than real, the mere existence of a new set of rules and formal institutional arrangements seems to have helped these industries to become more competitive. This is suggested by the experience in the mobile industry and wholesale electricity markets mentioned above.

While this paper has emphasized the institutional dimensions of enhancing competition, the Turkish experience does underlie the importance and complementarity of the broader economic policy framework. After all the institutional and competition enhancing measures described above were undertaken in an environment of more or less liberalized product and financial markets, a process that started in the 1980s. Liberalization of domestic markets was complemented by liberalization of foreign trade and international finance. As examined in Atiyas and Ozan (2011/2012), however, both labor productivity and total factor productivity increased faster in the 2000s relative to the 1980s and 1990s, perhaps reflecting improvements both in the institutional environment and macroeconomic stability in the last decade.

Finally, it is not yet clear whether the emergence of these institutions represents a new equilibrium and whether they are compatible with the underlying political institutions in Turkey. The important role of the perspective of EU accession was mentioned above. This perspective has been weakening in recent years and it remains to be seen how this will affect the conduct of economic policy in Turkey. Recently there are signs that the government may be considering steps that will reduce the powers of IRAs. The government recently passed a decree law which authorized ministries to “inspect” the activities of agencies associated with the ministries. The decree law gives ministries the authority to harass agencies by subjecting them to inspections. These inspections would concentrate primarily on procedural and not substantial issues. More importantly, ministries still cannot overturn IRA decisions. However, it is very possible that this power to inspect will be used to curtail the de-facto independence of IRAs. In addition, several members of the governing party and the Prime Minister have been quoted in the press complaining about the excessive authority of the IRAs and the fact that they lack political accountability.

4. Evaluation: Trade-Offs and Challenges of Enhancing Competition

This section will discuss some elements and tradeoffs that need to be considered in the design and implementation of a competition-enhancing reform program. It will try to draw on lessons from theory, the Turkish experience and empirical studies.

4.1 A brief review of empirical evidence

Empirical evidence on the role of IRAs on economic outcomes generally focus on infrastructure industries. There is quite a bit of evidence that there is a positive correlation between the presence of an independent regulator and sectoral performance. Many studies focus on the telecommunications industry. In a widely cited paper Wallsten (2001) examines the effect of privatization and regulation in the telecommunications industry of 34 African and Latin American countries. He finds that privatization in the presence of an independent regulator is positively correlated with telecom performance measures such as connection capacity, penetration and labor productivity. Privatization alone, however, is associated with

few benefits, and is negatively correlated with connection capacity. A positive correlation between the presence of an independent regulator and sector performance, especially penetration, has been found in other studies as well, see Estache and Wren-Lewis (2010b and 2009) for reviews. The impact of IRAs however does depend on the details of the regulatory framework. For example Estache and Rossi (2005) focuses on the electricity industry and finds that privatization with the existence of an independent regulator utilizing incentive regulation is associated with higher efficiency relative to firms under public ownership. By contrast, the efficiency of privatized firms under rate of return regulation is not significantly different from those of the public firms. More recently, Cambini and Rondi (2011) look at investment rates of utilities in Europe and find that regulatory independence has a positive effect on investment.

Another way in which the presence of an IRA may affect economic outcomes is that they may reduce transactions costs. Guasch, Laffont and Straub (2007 and 2008) find that the existence of an independent regulator decreases the extent of renegotiation of concession contracts in the water and transport sectors. The reason could be that the presence of a regulator may have improved the contract design to begin with, which in turn would reduce future conflicts. Also, under the presence of a regulator, disputes may be handled within the regulatory framework, with no need to change the initial contract.

There is also some evidence on factors that influence the degree of formal independence of regulatory authorities. In a recent study using data from 175 IRAs worldwide from seven industries, Hanretty and Koop (2012) find that independence is more likely or higher in utilities and financial markets. Independence is positively associated with “replacement risk” which captures the frequency with which governments are replaced with government with different partisan compositions. In countries where replacement risk is high and consequently policies may change frequently, delegation may enhance policy stability, which will have a positive effect on investments. Independence is also negatively associated with the number of veto players in the political system. This is captured, for example, by the number of parties in government, the number of constitutional bodies that may influence policy (such as the number of legislatures), the degree of homogeneity of parties in the parliament, etc. The reasoning behind the negative correlation is that the higher number of veto players may be a functional equivalent of more independence in delegation, because more veto players make policy changes and reversals more difficult, reducing the need for independence of IRAs. These results in general provide support to theories that see delegation to IRAs as a solution to regulatory credibility and risk of expropriation.

A few studies attempt to measure the association between formal and de-facto independence, but here the problem is that measuring the degree of de-facto independence on a consistent basis across countries is very difficult. In the limited number of studies on Europe, the relation between formal and de-facto independence is found to be weak. Given this weak relationship, the fact that many studies have found a positive relation between the presence of an independent regulator and economic performance mentioned above is interesting.

There is also evidence that the regulatory environment interacts with other characteristics of the political environment. One important variable in that regard is the extent of corruption. Wren-Lewis (2011) examines the impact of corruption on the efficiency of electricity distribution companies in Latin America and the Caribbean but this paper also examines whether that impact depends the institutional environment, namely ownership of the distribution assets and the establishment of IRAs. The theoretical analysis shows that corruption should have a negative effect on efficiency. The impact of degree of independence of the agency, however, depends on the relative corruptibility of agencies versus politicians. For the specific case of electricity distribution companies in Latin

America and the Caribbean, Wren-Lewis (2011) finds that the overall degree of corruption does indeed have a negative impact on the efficiency of distribution companies. Moreover, the presence of an IRA significantly reduces this effect. Privatization is also found to lower the negative effect of corruption on efficiency, but this finding is not robust to controlling for the endogeneity of ownership.

4.2 The politics of enhancing competition

Institutional reform has a basic paradox: Important elements of the competition enhancing reform package entails delegating substantial discretionary authority from the ministers and agencies that they control to IRAs. Assuming that the IRAs are more independent than ministerial departments, the delegation therefore entails significant dispersion of previously centrally held political power. Hence while delegation is partly to ensure that regulatory decisions are insulated from political influence the paradox is that at the same time, this act of delegation itself is a political act. The question is: when is such delegation in the interests of those who currently hold political authority? That is, when is delegation incentive compatible with political power?

Both the theory and empirics behind IRAs suggest a few answers to this question: An important dimension of the act of delegation is an increase in regulatory credibility and a decrease in expropriation risk. This suggests that governments will be interested in delegating if they have a strategic interest in attracting private capital, both domestic and foreign. This may be true for several reasons. The cost of public finance or the existing level of public debt may be high. Or governments may be interested in allocating public funds primarily to social sectors such as education, health, poverty alleviation or even support for SMEs, and rely on private investment for infrastructure industries. Hence the “public finance” motive for liberalization would also favor the creation of a competitive environment. Even there the political elite always have the alternative of striking special deals with individual investors and share monopoly rents. The cost of that would be slower growth, so governments under a popular mandate and political pressure to deliver high growth would have better incentives to create a competitive environment. In addition, enhancing the competitive environment would also create a more conducive setting for the growth of small and medium enterprises. For these reasons one might think that post-revolutionary Arab societies would contain the correct political incentives for improving the level of competition.

Another possibility is that governments may be interested in encouraging the competitive process in some industries while continuing to regulate the creation and distribution of rents in others. This seems to be part of the story behind the experience in Turkey. It seems that the government opted in favor of competition in tradable sectors as well as (at least to a degree) in electricity and telecommunications while continuing to play a much bigger role in construction and urban development.

Assuming that those who hold political power are convinced of the necessity of reform, one still has to consider the issue of broader popular political support. The global experience seems to suggest that public support for the adoption of a regulatory reform program is not a major constraint. Assuming that the reforming government is willing and has a winning coalition in the legislature adoption of the program can only be hindered through popular discontent expressed through mass protests that create political instability and perhaps violence. This is not likely to occur save for a few components or instances such as privatization that is expected to create substantial unemployment, an eventuality that may generate substantial resistance from labor and trade unions. It should be possible and relatively easy to deal with this problem by including in the reform program well designed labor adjustment programs that aim at compensating the losers. With significant expected productivity increases from privatization, financing such programs should not be that

difficult.¹⁰ Privatization has other potential political hazards that the literature has identified, these will be mentioned below. The rest of the regulatory reform program is not likely to generate significant political sentiments that would result in mass protests.

Popular support for the sustainability of the program is a different game because in the medium term popular opposition and discontent cannot be disconnected from electoral politics; if there is popular discontent with the program then the opposition may win elections on an anti-reform program and the program may be reversed. In the medium term the main means through which popular support can be maintained seems to be through successful implementation of the regulatory reform program: if public services are successfully provided and if access to services is successfully enhanced, this should be an important factor that ensures public support. In any case, over the medium term one should expect a positive concordance in the sense that successful reform would generate its own political support. But this potential of positive concordance also suggests a constraint: the reform has to deliver over a reasonable time frame if it is going to be politically sustainable. This can be called the deliverability constraint. Note that while partly a technical issue, high level of delivery also hinges on ability to curb capture and corruption.

Political support for the reform as well as the degree of success in implementation is also related with the way in which reform is carried out. In many developing countries regulatory reforms are adopted during or immediately after major economic crises, often as part of conditionality imposed by multilateral organizations such as the World Bank and the IMF. As discussed above, this was certainly the case in Turkey (see Ozel and Atiyas, 2011) for telecommunications and electricity. This is often done without much discussion and in a top down manner. Laws are typically prepared by relatively small teams of believers, with little or no public consultation. In fact, the Turkish experience suggests that the reforming team often carries out its work in secrecy exactly because of fear of resistance from the rest of the political (and bureaucratic) elite. This is expedient in the short run: If the government has a majority in the enacting body, swift adoption is assured. The Turkish experience also suggests that lack of wider ownership creates major hazards over the medium term which also hurts the deliverability constraint. This works in various ways. First, secrecy and bypass creates resentment, and resentment of the bureaucracy creates resistance and hurts implementation. But perhaps even more importantly, bypass also prevents the establishment of a common understanding about the objectives of the program and more importantly how the various parts of the program fit together. For example restructuring in the electricity industry is quite a complicated project consisting of multiple dimensions. Consistency among these dimensions is a must. However, in the case of Turkey it took a tremendous amount of time for the bureaucracy (and even the private sector) to really understand the different dimensions of the restructuring process. This has resulted in faulty designs of incentive mechanisms and very long delays in implementation.

4.3 The role of privatization (vs. liberalization)

The Turkish experience suggests that the role of privatization in curbing inefficiency and capture in industries where competition is limited or non-existent was exaggerated. The literature suggests that (under contractual incompleteness) relative to private ownership, public ownership performs better for allocative efficiency and worse for productive (or cost) efficiency (e.g. Schmidt 1996). Hence regulators and policy makers face a trade-off. In the case of Turkey, electricity distribution suffered from high electricity losses and theft. They are being privatized and their tariffs are subject to incentive regulation with loss targets. If

¹⁰ After the privatization of Turk Telekom, the incumbent telecom operator in Turkey, employment was reduced by almost 50 percent. This did not create an uproar thanks to a program that gave options to workers either to opt out with a hefty severance pay or find employment elsewhere in the government.

companies can decrease losses to levels beyond the targets, their profits increase. This is a potentially high powered incentive to cut costs, but the obvious welfare loss is the surplus that is captured by the distribution companies. This is a clear example of the efficiency-rent extraction trade-off discussed in the literature on regulation under asymmetric information (e.g. Laffont and Tirole 1993).

Martimort and Straub (2009) also suggests that collusion between regulators and private firms may lead firms to appropriate a larger share of increases in efficiency in the form of higher prices, especially for firms in sectors involving large fixed costs and requiring high mark-ups to cover total costs (such as water, roads, port and airport construction). The authors suggest that this result may explain the widespread dissatisfaction with privatization in Latin America even though many studies find that privatization leads to efficiency increases.

This is not meant to suggest that the public finance justification for privatization (i.e. privatization to raise revenues) may not be justified under certain circumstances. The purpose here is to suggest that, absent competition, the benefits of privatization may be exaggerated and that under certain circumstances it is worthwhile to think of alternatives, especially public management reform, corporatization, etc.

4.4 Separation of powers and the special role of a competition authority

In the literature on regulation under asymmetric information, one way to ensure that the (non-benevolent) regulator acts in the public interest is to make the payments made to the regulator contingent on the report that the regulator provides to the government on the costs of the firm.¹¹ As emphasized by Dal Bo (2006) making contingent payments to regulators is not a realistic option. An alternative proposed by Laffont and Martimort (1999) is the separation of regulatory powers. The Turkish experience actually seems to support this suggestion.

In Turkey the competition authority and sector-specific regulators have quasi-concurrent powers over anti-competitive behavior in the regulated industries. Of course, the existence of concurrent powers is likely to increase regulatory uncertainty whenever the respective agencies reach conflicting verdicts on specific issues. Separation of powers may also lead into inter-agency conflict and push agencies into a power struggle to maximize their jurisdiction. It may also induce firms in the regulated industries firms to abuse the separation of powers by picking and choosing agencies so as to maximize the likelihood of a favorable decision. In the Turkish case the degree of regulatory uncertainty has been reduced through a division of labor that has emerged over time: the competition authority has come to limit its intervention into areas of market behavior that are not directly regulated by the sector-specific agencies. This of course reduces the welfare enhancing impact of separation of powers, but this loss of impact can partly be compensated by vesting the competition authority with a strong advocacy role. Under an advocacy duty, the authority submits its opinions in areas where it has no direct jurisdiction. It turns out that such opinions can have a critical role in increasing the overall transparency and accountability of the regulatory system.

Note that even when regulatory agencies are not corrupt, sector specific regulators and the competition authority may legitimately have somewhat different preferences: For example, electricity or telecommunications regulators may have an interest in network expansion and they may attach a lower weight to the development of competition in their respective industries. A critical dimension of the separation of powers problem is to place the authority

¹¹ The non-benevolent regulator is modeled as the middle layer of the three-layer principal agent hierarchy with a (benevolent) government at the top, a firm with private cost information at the bottom and the regulator. The regulator obtains private signal about the cost of the firm and reports that to government. However, the firms can bribe the regulator into reporting false information, or claiming to have generated no information.

to regulate mergers and acquisitions under the competition authority. Mergers and acquisitions potentially play a critical role in the evolution of market structure and are critical determinants of the degree of competition in the medium and long term. Undue increase in concentration raises the likelihood of anti-competitive behavior and it becomes much more difficult to protect consumer welfare through conduct remedies. Regulating mergers gives the competition authority the power to prevent increases in concentrations that are likely to lessen competition.

An important dimension of regulating concentrations is the role of the competition authority in privatizations. As mentioned earlier, a critical danger of privatization in concentrated or monopolistic industries is to turn public into private monopolies. The incentives of governments (especially the Treasury or the Ministry of Finance) during privatization are towards raising maximum revenues to the detriment of developing competition. This would not only run counter to the agenda of developing competition but would also represent a big threat to generating political support for the reform agenda. The Turkish experience suggests that engaging the competition authority in the privatization process may be an effective way to decrease the likelihood that public monopolies are turned into private monopolies. The competition authority in Turkey has taken critical decisions during the privatizations in electricity, telecommunications and transport (ports) industries that have helped reduce (to some extent) the creation of private firms that hold excessive market power.

One important detail in this regard is that normally competition laws do not empower competition agencies to prevent ownership changes that *do not increase* the degree of dominance in the market. So normally a competition agency would not be able to prevent the purchase of a monopoly by a private investor that does not have a prior presence in a specific industry. The Turkish Competition Authority has gone out of its way to usurp that power through a communiqué, and for reasons that are hard to understand, this (albeit welfare enhancing) transgression has not been legally or politically challenged. It may be wise to actually endow the competition authority with such power in the laws that form the legal basis of privatizations.

4.5 Empowering consumer groups

In environments where the risk of capture of the IRA by the firms that it is supposed to regulate is relatively high (or where the information advantage of the regulated firm is relatively high) one remedy that has been proposed is to develop publicly funded consumer advocacy groups. Besides compensating for the threat of capture by firms, establishing publicly funded (but not controlled) consumer advocacy groups may help with generating political support for the sustainability of the reform program. Consumer advocacy groups may also help create a wider base of legitimacy for the reform program and help with the objective of creating new sources of social and political power. But one should also note that this requires education, expertise, and active media etc. The literature suggests that such initiatives may be effective. There is empirical evidence, cited in Del Bo (2006) that in the US regulated prices are lower in states where there are consumer advocates.

4.6 Selection of regulators

There is evidence cited in Dal Bo (2006) that the method of selection of regulators may have an impact on regulatory outcomes. For example, some studies show that when the regulators are elected, or appointed by legislators, or when executive appointments require legislative approval, regulated prices tend to be lower, possibly reflecting the influence of consumers. It should be pointed out that most of these studies are on the US and may be less relevant for countries with parliamentary systems, especially when the government parties also hold majorities in the parliament. What is not clear in some of this research is whether electoral influence works through incentives or through selection of different types of regulators.

Besley and Coate (2003) explores the following idea: When regulators are appointed by the executive, sensitivity of regulatory policy to voter preferences is dimmed because “regulatory policy becomes bundled with other policy issues that the appointing politicians are responsible for.” By contrast, when regulators are elected, their stance on regulation is the only salient issue so that the electoral incentive is to run a pro-consumer candidate. They find evidence that support the idea that elected states are more pro-consumer in their regulatory policies in that they allow less pass-through of fuel costs to electricity prices. Overall, these studies suggest that elected regulators are more pro-consumer. Of course, this does not immediately suggest that from a social welfare point of view this is a better design because it may reflect populism and lower than optimal prices, possibly endangering future investments. On the other hand, in environments where capture by regulated firms is the more powerful distortion, elected regulators may be a welfare-improving remedy.

In any case, obviously the preferences of the board or the directors play a crucial role in the performance of the agency. This, in turn, means that the procedure set for the appointment of the regulatory agency is very important as well. Often regulators are appointed either by the executive or the legislature. In parliamentary systems, separation of powers is weak so the executive branch of the government often has ultimate influence on the appointments. While from a social welfare point of one would desire that people who are appointed would be types who would protect the independence of the agency and who would try to encourage decisions that would maximize a well accepted measure of welfare (say total or consumer surplus). Above all, this would require people with competence and integrity. It is very difficult to find procedural ways to reduce the influence of the executive so as to increase the quality of appointments. Perhaps a better way to improve the quality of appointments is to increase the transparency of the appointment process. For example, both the executive and the opposition can have the right to nominate candidates, information about whom can be made public before the executive makes its final choices. In addition, the opposition may have the right to question the candidates in hearings held at the relevant parliamentary committee. Under such a procedure, the executive would still have the final choice, but may have to better justify its choices.

5. Conclusion

This paper has drawn from the experience of Turkey to discuss various changes in the regulatory environment that can be instrumental in enhancing competition in post-revolutionary Arab societies. Presumably the enhancement of competition entails a transformation from a regime where profitability relies on special political connections to one where success is predominantly driven by productivity. This in turn requires a policy and regulatory framework in which the political authority is constrained in its ability to discriminate among firms on the basis of political connections.

Establishing a non-discriminatory policy and regulatory framework often entails institutional remedies whereby substantial amount of decision and rule making authority is delegated to agencies that are relatively independent from the government and individual ministries. The paper has discussed the objectives and characteristics of this delegation, the nature of the independence and other dimensions such as accountability and transparency.

The paper has also reviewed the experience of Turkey where such delegation has occurred in the last decade or two, albeit imperfectly and in a way that is non-uniform across sectors. Even in its imperfect form, and where de-facto independence of the new agencies is questionable, it has discussed examples where the new rules of the game did have some bite in limiting the extent of capture. It has underlined the particular importance of the role of crises, international organizations and the perspective of accession to the EU. Moreover, it has discussed that in the case of Turkey enhanced transparency and accountability in some

sectors occurred simultaneously with increased discretion in others. The jury is still out, however, on whether the new institutions will survive political dynamics where the EU anchor is becoming weaker.

There is quite a bit of evidence that the presence of IRAs especially in infrastructure industries is associated with better performance. The presence of IRAs also seem to moderate the negative impact of corruption on efficiency. There is also evidence that independence of IRAs is higher in environments predicted by theory, that is environments where political “replacement” risk is higher and the number of veto players is lower. The verdict is yet to be spelled out but the Turkish experience as well as the empirical evidence suggests that institutions that enhance competition may play a role in creating an environment that is more conducive to investment and growth.

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