

PRIVATIZATION IN TURKEY

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Privatization most commonly means the transfer of state dominance in industrial and commercial activities partially or totally to the private sector through the sale of public assets¹.

The comprehensive privatization which was first carried out in England after 1980 constituted a model for many developed, rapidly developing and underdeveloped countries. Privatization practices are today seen in various countries whose economies are called liberal, socialist or mixed. This article is intended to present and discuss the privatization program of Turkey and its implementation from the national economy point of view. Before doing that, it will be useful to briefly explain the significance of the public enterprises (the PEs) in the Turkish economy².

The place and role of public enterprises in the economy

In Turkey, PEs emerged during the 1930s not for ideological but pragmatic reasons, mainly owing to the lack of private capital accumulation and initiative to give first impetus to development. Through their large scale investments and operations, they have become a major policy means used by governments in order to create the necessary industrial infrastructure, to prevent unemployment and to reduce regional imbalances in investment and income distribution. These enterprises also made significant contributions to guiding and supporting private sector, to providing ultimate consumers and

¹ The term privatization is used here in a narrower sense. Broadly defined, privatization is an umbrella term for various policies including not only asset sales but also deregulation contracting out and leasing. See Swann (1988) but also, pp. 1-2; Bishop and Kay (1988), p. 8.

² For detailed analyses of public enterprises with privatization experience in African and Arab countries See Ramanadham (1987); El-Naggar (1989).

private manufacturing firms with basic goods and services at subsidized prices and to training qualified executive staff, experts and entrepreneurs.

The generally accepted criterion for defining the PEs is the relative share of state ownership in total capital. In the latest legal arrangements made in 1983 and 1984, these enterprises, according to that share, were classified as follows :

- those which are wholly owned by the state : they are called public economic enterprises.
- companies in which public share is less than 100% : they are called "affiliated partnerships" when that share is more than 50% of total capital and "participations" otherwise.

Wholly state owned enterprises are also divided into two subgroups according to their field of operation and the aims to which they should give priority :

- those which operate in market according to commercial principles, namely, profitability and efficiency.
- those which are established in order to produce monopoly goods or basic goods and services in conformity with social requirements and the principle of efficiency.

All these enterprises, the number of which today is nearly 200, operate in a great variety of sectors, ranging from manufacturing, mining, energy and agricultures to services, such as commerce, banking, insurance, transportation, communication, construction, tourism, social security etc.

Table 1 : The share of PEs in the economy

	1980	1989
Industrial value added	28 %	26 %
Gross national product	11 %	17 %
Public investments	59 %	42 %
Total investments	37 %	19 %
Number of employees (thousand people)	584	715
Industrial employment	25 %	16 %

Source : High Audit Board, *General Report on PEs, 1984, 1989.*

In 1989, they accounted for 17% of GNP, a fourth of industrial value added, about 40% of the public investments and around a fifth of total investment in the economy; they employed more than 700 thousand people. As a result of the liberalization policies followed after 1980, their share in

industrial value added has slightly decreased, while their share in employment and investment has been most remarkably reduced (Table 1).

More than half or total of many important goods and services are produced by these enterprises (Table 2). They constitute monopolies in some sectors, while in others they work in a competitive environment and provide a great variety of goods and services which are also produced by private companies.

Table 2 : Share of PEs in total production

Type of goods or service	1980	1989
Coal	100	100
Copper ore	100	100
Boron minerals	100	100
Sulphur and phosphate	100	100
Cigarette and tobacco products	100	100
Petrochemical products	100	100
Locomotives and wagons	100	100
Communications services (Postal services, radio and television)	100	100
Freight carrying (railway)	100	100
Passenger carrying in		
- Railway	100	100
- Air	100	84
Packaged tea	100	91
Lignite	92	84
Electricity	83	86
Petroleum products	84	79
Sugar	65	78
Coke	84	63
Crude oil	40	65
Iron ore	57	57
Paper and cardboard	66	55

Source : High Audit Board, *General Report on PEs 1985, 1989.*

As usual in state controlled entities in developing countries, commercial objectives are subordinated to political preferences and social aims, such as creating large scale employment opportunities, developing backward regions

and redistributing income³. They are subject to much political intervention not only in their long-term plans and decisions on investment, pricing and employment but also in their day-to-day management. Their general directors and board members are chosen from among those holding similar views to the political party in power. They usually suffer from poor management, overstaffing, weak financial position, inadequate pricing policy and obsolete production technology. In order to operate productively and profitably and to compete with foreign companies in international markets, they need financial restructuring, rehabilitation and huge renewal investments.

For these reasons, the PEs have incurred considerable financial losses and increasingly become a heavy burden on general budget and a major source of rapid inflation towards the end of the 1970s. For example, their overall losses were at the highest level in 1978 and amounted to 49% of the budget deficit. In order to finance their growing deficits they required ever increasing budgetary subsidies. Direct transfers to the PEs, including capital payments from budgetary sources, accounted for 12% of total government expenditures⁴.

Since the government's limited financial resources caused delays in subsidies, they had to resort to expensive commercial bank credits under the guaranty of the government and substantial interest expenses began to accumulate. For example, between 1980-85 their interest payments increased more than ten times and reached TL.400 billion.

In the period after 1980, the number of profit making PEs rapidly increased and generally speaking they were no longer a drain on public sources, mainly because of high price increases resulting from the liberalization policies of the government. In 1989, for example, their overall profit amounted to 1.8 billion TL⁵.

The Turkish privatization program

The privatization in Turkey has been a current issue since 1985, as part of the liberal economic policy pursued during the last decade.

The legal and structural arrangements for privatization in Turkey was made by Law 2983 (March 1984) and Law 3291 (May 1986). The first law created the Housing Development and Public Participation Board at

³ See El-Naggar (1989), p. 86; Van de Walle (1989), pp. 603-604; Hemming and Mansoor (1988), pp. 3-5.

⁴ Figures were supplied from the Ministry of Finance and Customs and from *The State Economic Enterprises and Participations Annual 1981*, published by the Undersecretariat of Treasury and Foreign Trade, p. 713.

⁵ High Audit Board, *General Report 1989*, p. 167.

ministerial level as the policy-making body and the Housing Development and Public Participation Administration (HDPPA) under the Prime Ministry to carry out the policy. The second law granted the authority to make all decisions on privatization to the Council of Ministers in the case of PEs and to the Housing Development and Public Participation Board in the case of affiliated partnerships and participations. The HDPPA was splitted into two different administrations in 1989 : the Housing Development Administration (HDA) and the Public Participation Administration (PPA). Currently, the PPA determines sales conditions, the amount and price of shares to be sold, the banks and other intermediary institutions for public flotations in every privatization operation. In advance of a sale, the control over the enterprise to be privatized is transferred from the Ministry concerned to the Prime Ministry. Such an enterprise becomes a corporation whose shares are transferred free of charge to the PPA and is brought under the commercial law without being subject to the tedious formalities of incorporation, thus released from the Decree with power of law 233 governing the management of the PEs. Thereafter, the Board of the PPA has the authority to make all decisions on the management, operations and capital structure of the PE to be privatized, until the state's share falls below 50 percent.

The Privatization Master Plan (PMP), which was prepared by the Morgan as the consulting firm in May 1986, established the objectives and priorities of the Turkish privatization program and, by studying 32 enterprises which represent about 40% of industrial production and 60% of fixed capital in Turkey, it classified them into groups according to their prospects for privatization⁶. Also, action plans for the enterprises which should be given priority were prepared.

Objectives and priorities

As a result of extensive research and numerous discussions with the officials concerned, the Morgan Guaranty Bank specified fourteen potential objectives that were judged as being of most relevance to Turkey. These objectives were formatted into a questionnaire which was arranged by Morgan and Wyvern Research Associates. Questionnaire were than distributed to the senior officials who were responsible for economic affairs and mutually determined by Morgan and the State Planning Organization of Turkey (SPO). 20 respondents of the 26 recipients including ministeries,

⁶ Currently the number of the enterprises included in the privatization program rose to about 70.

undersecretaries, general directors etc. ranked the objectives in order of importance⁷.

The most important objective of the privatization program was seen to be making the economy more responsive to market forces, thereby increasing industrial efficiency and the growth rate of the economy. The three most highly scored objectives all relate to this theme⁸. Then followed the widening of share ownership and the development of capital market (Ranked 4 and 5).

Generating revenues for the government was determined to be the least important objective (Ranked 14)⁹.

Based on discussions between Morgan and the SPO, 32 PEs were classified into three broad and eight subcategories by priority of sale¹⁰. The most important criterion in the classification methodology is economic viability, defined as the potential viability of the PE in a competitive environment without subsidies, import protection or price control. Expected future demand for and supply of the products, operating efficiency, quality of assets, financial performance were among the factors analyzed in order to determine the economic viability. Social and strategic importance in the PEs to the national economy were considered as well¹¹.

In the PMP, top priority has been given to 5 enterprises, of which two operating in transportation (USAS, THY), one in tourism (TURBAN), one in animal feed industry (YEMSAN) and one in cement sector (ÇİTOSAN). At the next stage two communication enterprises, namely TELETAS and NETAS, were envisaged to be privatized. Action plans, too, were prepared for these First Priority PEs in subcategories I (entire company is saleable) and II (majority is saleable).

⁷ The Morgan Bank, *Privatization Master Plan : Objectives of Privatization* (May 1986), pp. 6-16.

⁸ These objectives were (1) to allow market forces to stimulate the economy, (2) increase productivity and efficiency, and (3) to increase quality, quantity and diversity of the goods and services.

⁹ Among less important aims were to minimize financial support for the PEs by the Treasury, to free government administrators to work on policy and regulatory issues, to shift political ideology toward private ownership and to strengthen international economic and political ties by foreign investment.

¹⁰ The classification categories were as follows : First priority (I. Entire company is saleable, II. Majority is saleable, III. Large parts are saleable) Second priority (IV. Parts are saleable, V. Candidates for creeping privatization, VI. May be saleable, VII. Saleable with government support) Third priority (These are public service companies. Only partial privatization may be possible through subcontracting of services) See. The Morgan Bank, *Privatization Master Plan : SEE classification* (June 1986), pp. 4-11.

¹¹ *Ibid.*, pp. 18-25.

Methods of sale

The government has not determined a general method of sale applicable to all state enterprises. Besides, no legal restrictions have been imposed on potential buyers of shares offered to the public. The whole or part of the PEs to be privatized can be sold to domestic or foreign companies. However, as far as industries of strategic importance or monopolies are concerned, the government is likely to put specific limitations on prospective ownership and to retain a certain percent of stocks as "golden share".

In the sale of public assets the following methods are used :

- 1 - Offer to the public at a fixed price through the stock market,
- 2 - Block sale with tender offer to domestic or foreign firms,
- 3 - Block sale with delayed offer to the public.
- 4 - Offer to the public with delayed block sale : Initially to offer a small percent of government share to the public and then to sell the remaining part to a managing investor group through block sale as considered in the case of the Turkish Airlines and PETKIM (a monopoly in the petrochemical industry).

The results of implementation

Privatization in Turkey has so far been realized quite slowly. As of the end of 1991, the total proceeds from sales amounted to about TL. 1,6 trillion, of which 79% were through public flotations, mostly in 1990 (Table 3). Privatization costs, on the other hand, totalled some TL. 0,5 trillion. Thus, the difference between total proceeds and costs is only TL 1,1 trillion. On current plans, annual gross proceeds will exceed TL. 2 billion in the years ahead.

Considering heavy criticism on block sales in the previous years, privatization program has recently taken greater care to public flotations. However, compared with the annual proceeds from offers to the public expected at TL. 2 trillion for the last two years, only TL. 0.8 trillion in 1990 and TL. 0.3 in 1991 were realized¹².

¹² Due to the atmosphere of uncertainty caused by the October elections, implementation nearly halted in the second half of 1991.

Tabb 3 : Privatized Companies.

Company	Business	Public share (%)	Public share sold (%)	Dates of sale	Proceeds from sales (TL.million)	Privatization technique
3 Fodder companies of YEMSAN	Animal feed	15-40	15-40	1986	227	Block sale through tender offer
TELETAS	Communication	40	22	1988	15.400	Offer to the public
USAS	Airport services	100	70	1989	32.015	Block sale with delayed offer to the public
5 Cement Companies of CITOSAN	Cement	96.6-100	51-99.9	1989	245.008	--
4 Fodder Companies	Animal feed	13.3-45	13.3-45	1989	3.625	Block sale through tender offer
Others	Miscellaneous	20-88.3	20-88.3	1985-1991	170.797	--
Erdemir	Iron and steel	51.5	2.9	1990	132.393	Offer to the public
Kepez Elektrik	Electricity	43.7	8.2	1990	23.457	--
Cukurova	-	25.4	5.5	1990	96.995	--
Arçelik	Consumer durables	15	5.8	1990	50.162	--
4 Cement Compnies	Cement	35.3-49.2	2.9-31.2	1990	97.500	--
Celik Halat	Steel	29.3	13.2	1990	19.546	--
PETKIM	Petro-chemical	100	8.1	1990	384.463	Offer to the public with delayed block sale
THY	Airline	100	1.5	1990	13.930	--
3 Cement Companies	Cement	13.42-99.8	12.7-39.9	1991	128.315	Offer to the public
Migros	Marketing of consumer goods	42.2	36.4	1991	18.199	--
Ditas	Oil tanker	14.8	2.5	1991	865	--
Tüpras	Refining	100	1.6	1991	24.279	--
Petrol Ofisi	(Gas stations) Distribution	100	4.0	1991	57.863	--
Gima	Marketing of consumer goods	54.7	4.2	1991	1.661	--
Tofas Manufacturing Co	Automotive	23.1	0.9	1991	25.810	--
Tofas Trading Co	Automotive	39	1.4	1991	4.075	--
Tofas Trading Co	-	39	16	1991	42.205	Block sale with delayed offer to the public

Source : The Public Participation Administration.

At the first stage of privatization program, implementation has included telecommunication, cement industry and airport services (USAS). Whereas those rendering traditional public services such as gas, postal service, railways and coal industry have remained outside the privatization list for the time being.

The privatized companies have been chosen from among those with high profitability and those using modern technology. This is why such companies are expected to attract interest of domestic and foreign investors more easily and to contribute to the development of capital market through public flotations.

Because of its high rate of profitability and modern technology in telecommunication industry. TELETAS has been selected as the first large enterprise to privatize and 20% of its capital offered to the public in 1988. Out of the total proceeds of TL. 15,4 billion, TL. 8,2 and TL. 5,9 billion were from the offer for sale to the general public and employees, respectively. In order for employees to buy shares easily a credit of about TL. 3 billion has been provided and expected to be repaid by equal installments over one year.

Before sale 38% of shares belonging to PTT were transferred to the PPA, 20% of which were offered to the public in the Istanbul Stock Exchange (ISE) and the remaining 18% were held as golden share. This method of sale is certainly in conformity with the aim of developing capital market and widening capital market and widening share ownership.

The same method of sale, however, has not been used in the sales of ÇİTOSAN and USAS both of which were sold to foreign companies in February 1989. Payment in foreign exchange and high technology transfer account for the preference of this method.

In the case of ÇİTOSAN, 90% of five cement factories' capital were sold to a French cement firm (Société Ciment Français) by tender offer in return for \$ 105 million.

Pursuant to the provisions of the sale agreement, the French firm made the following commitments :

1. Renewal investments at the level of \$ 75 million will be realized in the next four years.
2. 10% of the nominal capital will be held by the government as golden share.
3. 39% of the shares will be sold to the public in the future, and 10% of public flotation to the employees working in the cement factories concerned.

As for USAS, its new owner, SAS (the Scandinavian Airlines Service Partner) transferred 70% of its capital at a sale price of \$ 14 million and committed to make an annual dividend payment of 21 % of gross profit to

the PPA over the next ten years. In addition, SAS will sell 30% of capital to individual investors after a certain period of time and give priority to the employees working in USAS.

Recently, the two monopolies (PETKIM and the Turkish Airlines) have been able to offer only insignificant part of their capital for sale to the public with attractive terms, such as selling a certain number of shares to the employees and the retired persons by installments.

Obstacles to privatization

The rationale for the Turkish privatization program is the contraction of state activities in industry and commerce and the allocation of government funds mostly to traditional public services, such as education, defense, health, and to infrastructural investments. It would not be wrong to say that privatization is a mode introduced by external pressures from the IMF and the World Bank, as in other developing countries¹³.

But the Turkish government has not been able to fully clarify the objectives, priorities, method of sale and sales prices determination of its privatization program. This led to the fact that the privatization program of the government has not yet enjoyed much popular support.

On the other hand, some important constraints cause the implementation to remain much behind the program. The low level of national income and domestic savings, the relatively small capital market and high inflation are the main reasons for poor prospects especially in public flotations. Besides, the public seems to fear that privatization will adversely affect the income distribution and worsen the unemployment problem. Block sale of public enterprises having strategic importance and monopoly power to foreign firms at prices below a fair market value particularly arouses objections. This method may take the form of foreign debt-equity swaps, as in Latin American countries¹⁴.

Concluding remarks

Since the Turkish privatization policy has a short history, it is still early to say whether it has been influential in improving the performance of public enterprises, relieving the burden on the Treasury and widening the share ownership.

The success of implementation should be measured not only the total sale proceeds of the number of privatized companies but also by higher

¹³ Aylen (1987), p. 15; Shirley (1988), p. 35.

¹⁴ Blackwell and Nocera (1988); Hemming and Mansoor (1988), p. 11 .

profitability, efficiency and better distribution of resources, resulting from a competitive environment.

Those public enterprises which necessitate new investment in large amount, having old technologies but making profit only because of their monopoly power may perhaps be sold to the public through a successful campaign. But this would mean to deceive the public. If the monopolistic advantages of a public enterprise continue when it is privatized, this, in turn, means that the increase in economic efficiency expected from competition cannot be realized.

The place and role of the PEs in the Turkish economy, on the other hand, is much more important than in advanced countries. Thus, it is quite difficult to assert that these enterprises have only been a burden on Treasury.

Liberalization policies, no doubt, necessitate the working of the PEs according to the principles of market economy. However, it is impossible to realize this policy by privatizing a large part of the PEs under the present conditions. Those producing goods and services of strategic and basic nature must be kept out of the process and selling to foreign companies in particular must be avoided. Besides, unless the necessary competitive conditions are created the privatization of state owned monopolies means, in fact, that they are replaced by private companies having monopolistic power, foreign ones in some cases. This would be even more harmful to the economy.

Because of its favorable contributions to the widening of share ownership and improving the capital market, offer to the public should be given priority. Whereas, the present size and development level of the Turkish capital market renders the privatization of these enterprises through public flotations in a short time almost impossible. In fact, the government has not been able so far to sell any of its majority shares in large enterprises to the public.

In view of the prevailing conditions, it can be said that many PEs will inevitably remain in public sector for many more years. Thus, the achievement of their isolation from political influences, their financial and economic rehabilitation and restructuring should be considered an issue as important as privatization on the agenda of Turkey. Otherwise, the public sector will only include inefficient enterprises losing more money than ever before.

The new coalition government coming to power after the October 1991 elections has not yet announced its program in relation to PEs and privatization, in detail. As broadly declared so far, the government seems to be determined to continue carrying out privatization program, but gives priority to making the PEs autonomous and restructuring them before speeding up the implementation.