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Domestic financing of economic development in Turkey: with special reference to the first five-year development plan, 1963-1967

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ABSTRACT

The purpose of this dissertation is to try to provide a critical analysis of the problem of domestic financing of the Turkish First Five-Year Development Plan, 1963-1967. More precisely, we shall be concerned with the following question: how the savings/income ratio in the Turkish economy could be raised from its pre-Plan level to that envisaged by the Plan as an investment/income ratio necessary for the attainment of the Plan's targets.

The study begins with a detailed introduction of the social and economic framework of Turkey in Chapter 1, in which the emphasis is put on the factors which are likely to be the most effective determinants of the saving capacity of the economy. This is followed by a review of the Plan's objectives in Chapter 2, which reveals the size of the Plan. Whether the financing of a plan of that size is within the capability of the Turkish economy is examined in Chapter 3 under the heading "Strategy for Financing of the Plan". However, even if the realization of the required finance is deemed to be within the means of the economy, it will certainly require some efforts by the public to raise the savings/income ratio above its pre-Plan level. In this connection, the performance of the private sector and the obstacles to a higher propensity to save in the private sector are analysed in Chapter 4. We are thus left with the major issue of the Public Sector's savings. Among the various kinds of public revenue, taxation is singled out due to its relative importance and studied in detail in Chapter 5. Then follows in Chapter 6 a sketch

of non-tax public revenues and public current expenditures and a

study of the financing of the deficit of the capital account of

the Public Sector.   The dissertation is completed with a chapter

summarizing the conclusions of the individual chapters.

Durham,   Mete Durdag
October, 1966.

DOMESTIC FINANCING OF ECONOMIC

DEVELOPMENT IN TURKEY

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DEVELOPMENT IN TURKEY

With Special Reference to the

First Five-Year Development Plan, 1963-1967.

A Dissertation Presented

by

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for the Degree of M.A. (Econ.) of the

University of Durham.

DURHAM

October 1966

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INTRODUCTION

The purpose of this dissertation is to try to provide a
critical analysis of the problem of domestic financing of the
Turkish First Five-Year Development Plan, 1963-1967.

My title is misleading if it is considered as suggesting
that this dissertation is concerned with the problem of providing
adequate funds for the investment programme of the Plan.   Such a
study would have involved dealing with the supply of investment
funds from financial intermediaries as well as with auto-financing.
Instead, the attention is focused here on the possibilities of
increasing real savings so as to match real investments envisaged
in the Plan.   More precisely, we shall be concerned with the
following question in this dissertation: how the saving/income
ratio in the Turkish economy could be raised from its pre-Plan
level to that envisaged by the Plan as an investment/income ratio
necessary for the attainment of the Plan's targets.

The breaking down of the financing process into two separate
aspects, namely, (a) the release of real resources from consumption
for investment, and (b) the transfer of these resources to investing
units, has become a widely used technique.   For example, Gurley and Shaw
in their American Economic Review article "Financial Aspects of Economic

Development", E. Nevin in his "Capital Funds in Underdeveloped
Countries", E. E. Jucker-Fleetwood in his "Money and Finance in
Africa", and Placido L. Mapa, Jr., in his (unpublished) Ph.D.
Dissertation "Development Financing in a Developing Economy"
concentrate on the role of financial institutions in providing
adequate funds for increasing capital formation. On the other
hand, A. Lewis in the chapter on "Capital" of his "Theory of
Economic Growth", V. F. Savaş, in his (published) Doctorate Thesis
"İktisadi Kalkinma nin Finansmani" (Financing of Economic Development),
Y. Hilmy in his (unpublished) Ph.D. Thesis "Domestic Financing of
Economic Development in Underdeveloped Countries With Special
Reference to Egypt", and S. R. Datta Gupta in his (unpublished) thesis
"The Financing of Planned Economic Development in India" deal almost
exclusively with the problem of increasing savings as a proportion of
national income.

The present study is conducted at the macro level. It
begins with a detailed introduction of the social and economic frame-
work of Turkey in Chapter 1, in which the emphasis is put on the
factors which are likely to be the most effective determinants of
the saving capacity of the economy. This is followed by a review
of the Plan's objectives in Chapter 2, which reveals the size of the
Plan. Whether the financing of a plan of that size is within the

capability of the Turkish economy is examined in Chapter 3 under

the heading "Strategy for Financing of the Plan". However, even

if the realization of the required finance is deemed to be within

the means of the economy, it will certainly require, as will be

seen, some efforts by the public to raise the saving/income ratio

above its pre-Plan level. In this connection, the performance of

the private sector and the obstacles to a higher propensity to

save in the private sector are analysed in Chapter 4. We are thus

left with the major issue of the public sector's savings. Among

the various kinds of public revenue, taxation is singled out due

to its relative importance and studied in detail in Chapter 5.

Then follows in Chapter 6 a sketch of non-tax public revenues and

public current expenditures and a study of the financing of the

deficit of capital account of the public sector. The dissertation

is completed with a chapter summarizing the conclusions of the

individual chapters.

In order to avoid the likelihood of getting involved in

speculating upon the Plan's projections in relation to the financing,

I have been careful to observe, as far as the scarce data have

permitted, this method. Estimates of the Development Plan and

Annual Programmes are set against the relevant performance of the

economy in the recent past and during the implementation period so

far; the determining factors of the past performance are analysed;

the measures envisaged in the Plan and taken in the course of implementation are assessed in the light of the analysis of the past performance as well as of the actual outcome of the Plan implementation so far.

The materials I refer to in this dissertation may be classified into three groups: (a) Theoretical works, (b) Statistical data about Turkey, (c) Works on those aspects of the Turkish economy which are relevant to my topic. Various aspects of the financing of capital formation in underdeveloped countries have attracted, particularly since the late 1940's, interests of many research workers, resulting in an accumulation of theoretical works on the issue. Therefore, I have met no difficulty in preparing the theoretical background of this dissertation. But the underdeveloped nature of the Turkish statistics has been a limiting factor. As will be seen in the text, the Turkish statistics have three important defects: (i) Their coverage is very limited; (ii) There is inconsistency between the data of the State Planning Organisation and those of the State Institute of Statistics which have been the basis of the official estimates until recently and are still used by many Government Departments; (iii) The data of the S.P.O., which are utilised in this dissertation, are lacking in clarity. For instance, it sometimes requires one to spend

considerable time and care to find out whether a table in an S.P.O. publication shows the actual or planned data. It is not unusual to meet a table comprising data expressed at different years' prices. As regards (c), it is disappointing that although a good many Turkish scholars trained in the Western Universities are holding posts in universities as well as in official and private institutions there are barely any published researches of academic value on the problems of the Turkish economy. Most of the articles in the few learned periodicals are concerned with those theoretical aspects which hardly have any relation to the realities of the Turkish economy. I could therefore scarcely have dispensed with the works on the Turkish economy made available in mimeographed form by the S.P.O., even though they are restricted to the use of the S.P.O. staff.

I have received great help from my supervisor Mr. M. K. Chowdhury. He has been most helpful to me in clarifying the various issues that have been encountered in the preparation of this work. He also has patiently kept instructing me about the methodology of my work. If there are any errors in my work, they remain my sole responsibility.

CHAPTER 1.

SOCIAL AND ECONOMIC FRAMEWORK OF TURKEY

Today there is a marked contrast with respect to development between the members of the world society, whatever the measure of development. If they are put on a scale in order of the degree of development, we have to name those towards the lower end of the scale as "underdeveloped". The differences between developed and underdeveloped countries are so significant in numerous aspects of their social and economic systems that to pick up only the difference in one aspect as the criterion of development would be an undervaluation of a host of other significant differences. Therefore, the introduction to the Turkish economy is made here in terms of a combination of its various characteristics rather than in terms of a single factor such as the level of real national income, which is the most widely admitted criterion of the degree of development. This will serve the purpose of acquainting us not only with an outline of the Turkish economy but also with the main determinants of the level of savings. For the social and economic structures of a country, with its value judgements, behaviour patterns, and institutions, are as effective determinants of the level of saving as the level of its real national income.

This chapter is composed of two sections. Section I deals with the social characteristics of Turkey, and Section II with the economic features within the context of the economic developments in the recent past.

I

SOCIO-ECONOMIC ASPECTS

1. <u>Population.</u>

The size of population, its composition, and its rate of growth have been of great concern in the economics of underdevelopment. The size of the population of a country has significance for its economic development with respect to its relation to the natural resources of the country. The well-known advantages of specialization and of the economies of large-scale production are materialized to a greater extent the greater the internal market, which is limited, among other things, by the size of population. On the other hand, the relation of the size of population to the natural resources may be such that it might result in the diseconomies of more intensive and extensive use of these resources. Viewed from this angle, it seems at first glance that Turkey, with an area of 780,600 km^2 and 31.4 million population in 1965, does not confront yet a population pressure on its natural resources. Table I shows the density of population in Turkey and in some other countries.

TABLE I.

DENSITY OF POPULATION IN TURKEY AND IN OTHER COUNTRIES.

Country	Density (Per km^2)	Country	Density (Per km^2)
Turkey	40	Brazil	7
Greece	61	India	118
Yugoslavia	70	United Kingdom ...	211
Ireland	41	France	79

Sources: U.N., Demographic Yearbook 1957, New York 1958,
pp.98-99.

For Turkey, O.E.C.D. "Turkey 1965/66" Paris 1966.

The figures given in Table 1 cannot have much meaning in the assessment of population pressure, if any, facing any of these countries. The size of population which creates the problem of overpopulation, changes from country to country according to the structure of their economies. The diseconomies of scale arising from a large population in relation to the natural resources show up most quickly in agriculture and in mining, whereas, industries, especially those making metal-products and basic chemicals, benefit most from a large market supported by a large population.[1] Being predominantly an agricultural country, Turkey actually is under the threat of over-population. In fact, the relationship between the

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1. W. A. Lewis, Theory of Economic Growth, G. Allen & Unwin Ltd., London 1963, p.324.

rural population and the arable land is not as favourable as the overall density figure given in Table 1.   Table 2 shows this relationship in Turkey in comparison with some other countries.

TABLE 2.

THE AMOUNT OF ARABLE LAND PER FARMER IN TURKEY
AND IN SOME OTHER COUNTRIES.

Country	Hectar Per Farmer
Turkey	2·41
United Kingdom	4·56
France	4·26
Italy	2·48
Greece	2·70
United States	25·68

Note: The figures for the countries other than Turkey were calculated from the figures in U.N., F.A.O., Production Yearbook 1960, pp. 3-5;   20-24.

Source: Prof. Dr. H. Cillov, Economics of Turkey (Turkish Text), Istanbul 1962, p. 78.

Furthermore, when account is taken of the fact that about one-third of the arable land in Turkey is left fallow[1] each year,

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1. The land is left fallow to regain heart due to the lack of adequate organic fertilisers and the inability of the farmers to afford it. This fact is a good indicator of the underdeveloped character of the Turkish economy.

this relationship deteriorates further, decreasing to an average of only 1·6 hectare per farmer. This is too small a size of land per farmer to work with modern equipments and methods. However, it would not be a valid argument to assert the existence of the over-population problem in a country only on the basis of the situation prevailing in one sector. This brings us to the question of the occupational structure of population in Turkey. ✗

The major part of the population derive their livelihood from agricultural activities. The ratio of the population engaged in agriculture to the total active population was 77·4% in 1962 while the relevant ratio for industry was only 9·8%.[1] A substantial part of the population active in agriculture adds little or nothing to output. In other words, disguised unemployment in agriculture is an important problem for the Turkish economy. According to the estimates of the State Planning Organisation the surplus or dispensable manpower in agriculture was 8·3 million out of a 9·86 million total agricultural active population in January, the month of lowest activity, though only 0·8 million in July, peak activity month, during 1962.[2]

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1. S.P.O., "Development Plan, First-Five-Year, 1963-1967", Ankara 1963, p. 420.

2. Ibid, p. 420. The surplus manpower has been estimated as the difference between the total manpower supply and the supply which would suffice to perform the various agricultural tasks of culti-vation, etc., with current techniques. Therefore, unless the agricultural techniques change the absolutely dispensable labour force is about 1 million in the agricultural sector.

The most striking aspect of the population issue is the relationship between the rate of population growth and the rate of growth of per capita income. The rate of population growth, together with the capital/output ratio, determines how much capital, or what rate of growth of national income, is necessary for preventing the standard of living from falling in spite of population growth.

Turkey's population was growing at an average rate of 2·81% p.a. during 1950-1955, 2·95% p.a. during 1955-1960 and 2·42% p.a. during 1960-1965.[1] This very high rate of population growth aggravates the problems of unemployment, external balance and low standard of living.

Even if it is assumed that the agricultural population can be kept at its present level which in fact contains a substantial degree of disguised unemployment, it would be necessary to create every year about 400,000 new jobs for new hands.[2] This would mean a 14% growth p.a. in the non-agricultural sectors,

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1. For the amount of total population since 1950, see p. 27 Table 9.

2. Prof. Ö. C. Sarç, Population Trends in Turkey and their Economic Consequences, in the "Capital Formation and Investment in Industry". A report of the international conference on capital formation held at Istanbul August 1962, Istanbul 1963, p. 71.

which is too high a rate in comparison with the past performance
of 6·4% p.a. on average during 1950-62.[1] As a matter of fact,
the amount of new non-agricultural jobs required will possibly be
much greater than 400,000 per year because of the likely transfer
of labour force from agricultural to non-agricultural activities.
The present rate of population increase requires an increase in
the agricultural output of about 2·5 per cent per annum to feed
the population at the prevailing standards.   Since no more land,
as will be seen later, can be brought under cultivation, increasing
capital investment in agriculture will be required which is likely
to result in displacing some farmers every year.

The chronic current account deficit of Turkish balance of
payments is one of the chief obstacles to her economic development.
Yet, the rapid increase of population eliminates any possibility of
reducing this deficit by curbing the internal demand.

Among the members of the O.E.C.D. Turkey is the country
with the lowest per capita income ($192 in 1961). The other members
of the Organization aim at a 3% annual growth of per capita income

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1. 14% is the outcome of a rough estimate, that is, (0·4 million x
    100)/2·75 million in which 2·75 million is the non-agricultural
    labour force in 1961 (See Table 3).   The implicit and rather
    unreasonable assumption here is that productivity of labour is
    constant as the economy grows.   6·4% rate is calculated from
    Table 6 in p. 21 as the growth rate of non-agricultural N.N.P.

in the 1960's.[1]   In order to prevent a widening of the relative gap in per capita income, Turkey must achieve an average rate of 5·5% growth per annum in her national income.   This target could have been lower had the population grown at a slower pace.

2. Distribution of Income.

According to G. Myrdal's explanation of underdevelopment in terms of circular and cumulative causation, inequalities in the distribution of income by regions and economic sectors are the main cause of underdevelopment of a country.   However, without getting involved in a particular theory, the present essay takes it for granted that a close relationship exists between the state of distribution of income and the level and composition of consumption, savings, investment, and, hence, economic growth.   In addition, the nature of the distribution of income in a country has a great bearing on the psychological and political climate in which the economic development will take place.

No statistical data are available to show directly the distributional situation in Turkey.   Nevertheless, some more or less sound judgements can be reached indirectly through using the

1. O.E.C.D., "Turkey, 1962/63", Paris May 1963, p. 12.

available data.   It has already been shown that agriculture
provides occupations for about 77% of the active population in
Turkey.   The contribution by the agricultural population to the
national income, however, is too far from being commensurate with
its share in the total active population.   As shown by Table 3,
the share of the agricultural sector in the net national income
is around 40%.   There exists a considerable disparity between the
average remuneration in the agriculture and that in the non-
agricultural sectors.   The average agricultural income is, roughly,
21·3 per cent of the average income in the industry, 18·6% of that
in the services sector and 18·1% of that in the construction sector.

TABLE 3.

SHARES OF ECONOMIC SECTORS IN LABOUR FORCE AND NATIONAL INCOME, 1961.

Sector	Labour Force		Income		Average Annual Income per person (TL)
	Amount	% Share	Amount (million TL)	% Share	
Agriculture	9,800,000	78·0	18,245	41	1,860
Industry	920,000	7·3	8,010	18	8,706
Construction	260,000	2·0	2,670	6	10,270
Services	1,570,000	12·7	15,575	35	9,920
TOTAL	12,550,000	100·0	44,500	100	3,560

Source: O.E.C.D., Turkey 1962/63, p. 51 and inside of
the front cover.

According to the S.P.O., the per capita income outside agriculture is approximately three times that of the peasant (TL 2,740 p.a. versus TL 950 p.a.).[1]

Within the sphere of agriculture, the average peasant's condition is far worse than is implied by the above figures because of a substantially uneven distribution of land. Table 4 shows that close to 25% of the total cultivated area is operated by 1·5% of the families. One half of the cultivated area is worked by 10% of the farming families, while the other half is shared among the rest of the families. For about 85% of the families, the average farm unit per family is smaller than 10 hectares, which may not always support a family under the present conditions of the Turkish agriculture.[2]

The great inequality in the distribution of the cultivated land, which can better be seen with the help of a Lorenz curve as given in Diagram 1, results in a similar inequality in the distribution of agricultural income. According to an estimate made by Dr. Eva Hirsch, the first five percentiles of the agricul-

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1. S.P.O., The Interim Programme for the Year 1962, Ankara 1961, mimeographed, p.   . The average agricultural income is in fact even smaller than 950 TL p.a., because of the overestimate of the agricultural income which is explained in page 28-30 below.

2. H. Cillov, op.cit., p. 106.

tural population altogether receive less than 12% of the total

agricultural income while the top percentile alone captures more

TABLE 4.

DISTRIBUTION OF CULTIVATED LAND.

Farm Area (Decares)	Families		Cultivated Area		Average size of Farm Unit (ha).
	000	%	000 ha.	%	
1 - 20	773	30·6	836	4·3	1·1
21 - 50	797	31·5	2,790	14·3	3·5
51 - 75	336	13·3	2,097	10·8	6·2
76 - 100	216	8·6	1,915	9·9	8·9
101 - 150	168	6·7	2,018	10·8	12·4
151 - 200	92	3·6	1,648	8·5	18·2
201 - 300	68	2·7	1,712	8·8	25·1
301 - 500	39	1·5	1,520	7·8	39·9
501 - 700	17	0·7	1,015	5·2	59·5
701 and over	21	0·8	3,811	19·6	181·6
TOTAL	2,527	100·0	19,452	100·0	7·7

Source: O.E.C.E., Etudes sur les Politiques Agricoles,
Paris 1960, Vol. 1, p. 298, as quoted in H. Cillov,
op.cit., p. 107.

than half of the total agricultural income[1] (see Table 5).

DIAGRAM 1.

LAND SIZE DISTRIBUTION IN TURKEY.
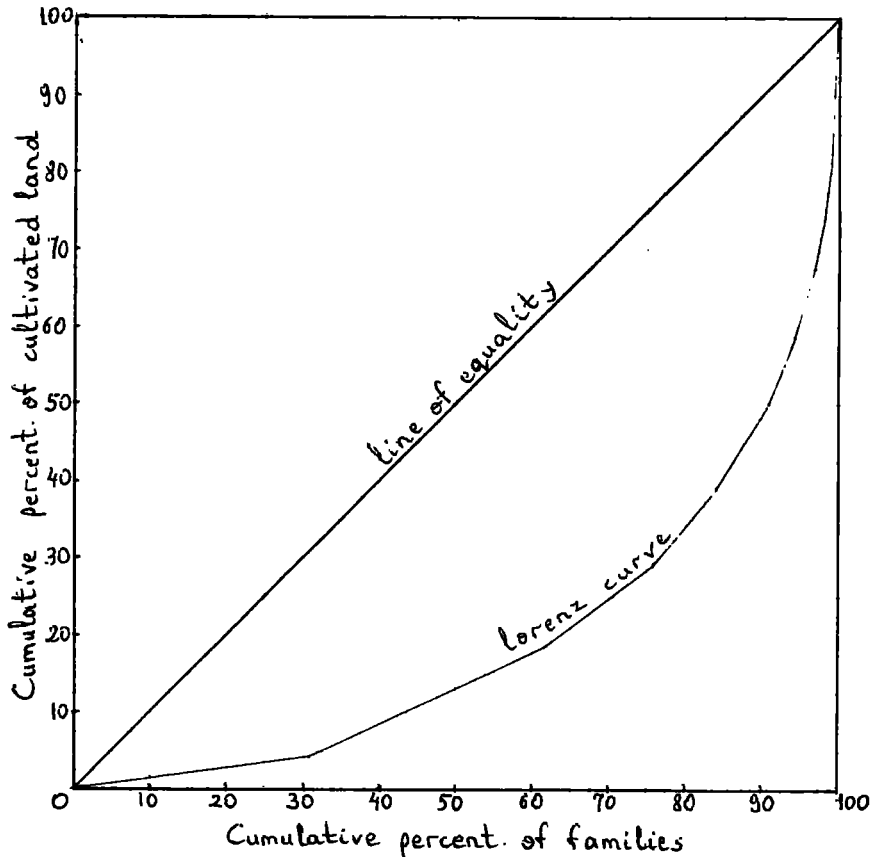
Source: Drawn on the basis of the data given in Table 4.

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1. According to the Enos Report, a 34% of the total agricultural
    income goes to the 4% of the agricultural population. (Quoted in
    H. Kizilyalli, Economic Effects of the Turkish Taxation System,
    mimeographed by S.P.O. in January 1965, in Turkish, p. 124).
    Prof. J. L. Enos' Report was published in the periodical "Yön",
    No. 59, dated 20/1/1963.

Today in Turkey, agricultural incomes are largely affected
by the weather conditions and the State's agricultural price policy.
However, the favourable weather and price conditions do not bring
much betterment to the peasant without land or with land of
subsistence size, but to the big landowner only.

TABLE 5.

DISTRIBUTION OF INCOME IN AGRICULTURE.

Percentile of Agricultural Population.	Share in Agricultural Income (%).	Percentile of Agricultural Population.	Share in Agricultural Income (%).
1	0·98	6	5·33
2	1·42	7	6·83
3	2·18	8	9·21
4	3·07	9	13·60
5	4·11	10	53·23

Source: Dr. E. Hirsch, Income Distribution in Turkish
Agriculture, Unpublished Ph.D. Dissertation,
Columbia Univ., 1960, quoted in H. Kizilyalli,
op.cit.

In addition to the sectoral inequalities, one can easily
observe the existence of regional inequalities in Turkey.   In
general, the coastal areas are better-off as compared with the
hinterland because of the favourable conditions for growing high

value crops and the tendency of the private industry to concentrate
in the coastal areas. The private enterprises working in the North-
West Turkey and in Izmir region represent 74% of the total private
enterprises.[1]

Reduction of the distributional inequalities through the
State's welfare measures is of insignificant degree in Turkey as in
all the underdeveloped countries, since the egalitarian policies of
a modern welfare state are too expensive for underdeveloped countries,
while the need for social security is much more pressing in these
countries than in the advanced ones. Beyond the medical assistance
granted to the needy by the State, there are three outstanding
institutions performing social security functions in Turkey: (a) The
Workers Insurance, (b) The Pension Fund which grants (old-age) pension
to civil servants and (c) The Army's Mutual Fund. Of these only The
Workers Insurance performs social security work in its broadest sense,
though it also has considerable limitations such as the absence of
insurance against unemployment and as being unable to extend its
activities to agricultural workers, non-manual workers and members
of some other activities. (Social security institutions are also
of great significance as sources of investible funds. We shall
turn to this point later).

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1. Dr. Ruşen Keleş, "The Rush to the Cities in Turkey" (Turkish) in
   Plânlama (periodical of the S.P.O.), No. 2, p.

3. Sociocultural Aspects.

Values and institutions prevailing in a country affect economic life through various channels such as consumption attitudes, labour efficiency, economic organization, attitude toward entrepreneurship, the general outlook on life, and the like. The values and institutions of the Turkish society have been for long, and still are, though to a much less degree, characterized by their traditional and conservative features. The wrong interpretation of Islam belittled the material and the present. Division of time between work and leisure in a way favouring the latter has become a way of life. Trade and manual works have long been, and still are in some quarters, considered degrading activities. The extended family system still constitutes the centre of social, economic and political life in Turkey. Its unfavourable effects on incentives to work and on the mobility of productive factors are common problems of all the underdeveloped countries.

Since the establishment of the Republic in 1923 much has been done to clear away the institutional barriers in the way of social and economic progress. Among many reforms the gradual spread of education has been most effective in breaking the traditional value patterns. But there is still much to be done in this field. The degree of literacy is far from being at a satisfactory

level. (In 1955 the percentage of illiterates was 43·6 among male population, and 75·6 among female population, aged 6 years and over). There is also an imbalance between various kinds of trained manpower supplied by the educational institutions and the demand for them. In breaking through the traditional cultural patterns a special role has been played by improved transportation and by more frequent commercial contact with urban centres.

The striking features of the Turkish society of our own day seem to me as follows: (a) The great majority is tied tightly to the land and most of them cultivate their own land, though there is considerable inequality in the distribution of land. This group is characterized with the conservatism in its value patterns. (b) One can easily observe the emergence of an organised labour force as a social and political power. There are, however, still many factors impeding the development of trade unions, such as the difficulties caused by the structure of the economy and labour force, and by the working class itself, not to speak of the antagonism of employers towards labour organisations. (c) The middle class is of great importance with regard to its control over social and economic life. This class is, however, grouped into two camps: the one being liberal in its attitudes but in favour of etatism in economic life, the other conservative in attitude but liberal in

economic policy. (d) Finally, there is a small group of traders, larger farmers and craftsmen that constitutes the wealthiest class. This group has also been serving as a source of recruitment of industrialists.

II

A REVIEW OF THE TURKISH ECONOMIC DEVELOPMENT, 1950-62.[1]

1. National Income.

The general trend of growth of the Turkish national income in the period 1950-1962 has not been a steadily increasing one but has followed a path with considerable fluctuations. This is readily observable in Diagrams 2 and 3. The level of G.N.P. was 82% higher in 1962 than in 1950 (see Table 7), representing an average rate of growth of 5·1% p.a. This average rate of growth, however, is influenced to a great extent by the exceptionally high rates attained during the early years of the period in question.

The 1950-53 sub-period witnessed an exceptionally brisk economic activity. The average annual rate of growth in this

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1. The main sources of information referred to for this section are these: S.P.O. Development Plan 1963-67; and, the Annual Programmes for 1963 and 1964. O.E.C.D., Turkey 1962/63, Paris 1963. I.B.R.D., Development Performance and Prospects of Turkey, mimeographed, November 1965. Prof. Anders Östlind, Scope for Non-inflationary Expansion in Turkey, mimeographed by the S.P.O., Ankara 1962.

period was 11·6%. This very high rate of growth was achieved, it
is interesting to note, without a significant rise in the general
price level (see Table 8). Successive good crops during 1950-53
and the rapid extension of the cultivated area as a result of
mechanization resulted in agricultural surpluses which were easily
disposed of in foreign markets thanks to the Korean boom in inter-
national trade. Export proceeds increased sharply from
$197 million in 1948 to $363 million in 1952. The exchange rate
was TL2·80 to the U.S. dollar, and net exchange reserves stood at
$153 million in 1952. The greatly increased effective demand
stemming from the expansionist investment policy was thus matched
by the rapidly increasing agricultural production and by the
increased imports of both capital and consumption goods.

The potential inflationary pressure of the expansionary
policy burst into the open as from the late 1953 when the foreign
trade lost its function as a brake on domestic inflationary forces.
The depletion of the foreign balances and the return of unfavour-
able trade conditions for the export of primary commodities led to
the severe reductions in the imports of consumption goods as from
1953 on. Exports over the five-year period of 1954-59 were
stagnant at or around $300 to $350 million annually. During
1954-58 severe shortages were prevailing in the supply of not only

foreign consumer goods but also raw materials, fertilisers, half-processed goods, spare parts, etc., of foreign origin.   Bottle-necks were confronting producers, with resulting low productivity and high production costs.   The agricultural production also entered a period of stagnation as the limit of cultivable land was reached in the mid-fifties.   The growing deficits of the State Economic Enterprises (S.E.E.)[1] were being financed largely by the Central and commercial bank credit.   Between 1954 and 1959 money supply expanded by 160%.   The country was pushed into an increasingly severe and complicated system of price regulations, but to no avail.   Domestic prices more than doubled between 1954 and 1959;   net gold and foreign exchange reserves fell to $26 million by the end of 1959 and the exchange rate was TL9·00 to the U.S. dollar.

The average annual rate of growth in the period 1953-58 fell sharply to 3·8% from an average rate of 11·6% achieved in the period of 1950-53.   If we use three-year averages for the beginning and end of the period, the average annual rate of growth appears to be still as low as 4·3%.   The level of per capita

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1. From now on the abbreviation "S.E.E." will be used to denote the State Economic Enterprises.

income fell from T.L. 1,507 in 1953 to T.L. 1,332 in 1954 and
could not regain its 1953 level until 1958 (see Table 7)[1].

In August 1958, the Government reversed its inflationary
policies.   A comprehensive stabilization programme was drawn up
with the help of the I.M.F. and the O.E.C.D., involving devalua-
tion of the Turkish Lira, domestic credit controls, and consolida-
tion and funding of the external debts[2].   But inflationary price
rises could not be brought to a halt before 1960.   The revolution
in May 1960 led to some hesitation on the part of producers and
consumers which had a depressing effect on economic activity.
The annual rate of growth of G.N.P., on average, was 3% during the
period 1958-62.   If the year 1962, which may be considered as
marking the beginning of a new active period, is excluded, the
annual rate of growth in 1958-61 appears to be 2·1%, which is even
lower than the rate of population growth, 2·9%, prevailing in that
period.   The per capita real income had risen by less than 2%
through 1959 and 1960, and dropped by 4·6% in 1961.

1. The "per capita income" figures refer to the Net National
    Product per capita (at factor costs).   If we had considered
    G.N.P. per capita at market prices during 1953-58 we would have
    found that the per capita G.N.P. was growing as G.N.P. grew on
    average 3·8% p.a. while the rate of population increase was
    below 3% p.a.   The discrepancy between the growth rates of per
    capita N.N.P. at factor costs and that of per capita G.N.P. at
    market prices shows that indirect tax proceeds and depreciation
    allowances in National Income Statistics together grew at a rate
    higher than the rate of population growth during 1953-1958.

2. At the end of 1952, external public debt was $188 million.   At
    the end of 1960 it amounted to $931 million, including the 1958
    consolidation of commercial arrears and suppliers' credits, and
    the new stabilization credits.

TABLE 6

TURKISH NATIONAL INCOME AT CONSTANT PRICES (at 1961 factor prices)

(Million T.L.)

	1950	1951	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961	1962
Agriculture	12,106.8	14,613.4	15,557.2	17,033.8	13,675.6	14,916.6	16,212.6	16,621.2	16,621.6	17,618.5	18,376.4	17,420.9	18,275.8
Industry	4,051.3	4,390.1	4,756.1	5,238.0	5,486.9	5,706.3	6,078.3	6,519.8	6,976.0	7,321.6	7,302.0	7,220.4	7,815.2
Construction	1,322.0	1,375.2	1,658.4	2,299.9	1,904.8	2,000.5	2,029.6	2,511.7	2,700.2	2,739.2	2,260.6	2,364.7	2,485.3
Services	7,407.6	8,256.7	9,106.9	10,010.9	12,320.6	11,087.9	11,677.6	12,613.8	13,612.7	13,914.4	15,143.6	15,266.0	16,519.6
Domestic, Income	24,887.7	28,635.4	31,078.6	34,582.6	31,387.9	33,711.3	35,998.1	38,226.5	39,910.1	41,593.7	43,080.6	42,272.0	45,105.9
Income From Abroad	- 143.5	- 165.8	- 179.8	- 200.1	- 181.3	- 195.3	- 208.6	- 221.2	- 249.2	- 250.6	- 245.7	- 250.0	- 304.0
N.N.P. (at factor cost)	24,744.2	28,469.6	30,898.8	34,382.5	31,206.6	33,516.0	35,789.5	38,045.3	39,660.9	41,343.1	42,834.9	42,022.0	44,801.9
Indirect Taxes	2,738.3	3,170.5	3,440.6	3,826.1	3,452.0	3,714.9	3,966.5	4,213.4	4,728.7	4,779.0	4,998.0	4,998.0	4,927.7
N.N.P. (at market prices)	27,482.5	31,640.1	34,339.4	38,208.6	34,658.6	37,230.9	39,756.0	42,258.7	44,389.6	46,122.1	47,832.9	47,020.0	49,729.6
Depreciation	1,008.5	1,127.1	1,252.8	1,362.7	1,394.5	1,511.5	1,625.4	1,765.7	1,891.7	2,023.9	2,108.3	2,193.0	2,290.6
G.N.P.	28,491.0	32,767.2	35,592.2	39,571.3	36,053.1	38,742.4	41,381.4	44,024.4	46,281.3	48.146.0	49,941.2	49,213.0	52,020.2

Sources: S.P.O., First Five-Year Development Plan, 1963-1967;   Ankara 1963, p. 14-15.

For 1962 figures: S.P.O., 1964 Annual Program;   Ankara 1963;   p. 10.
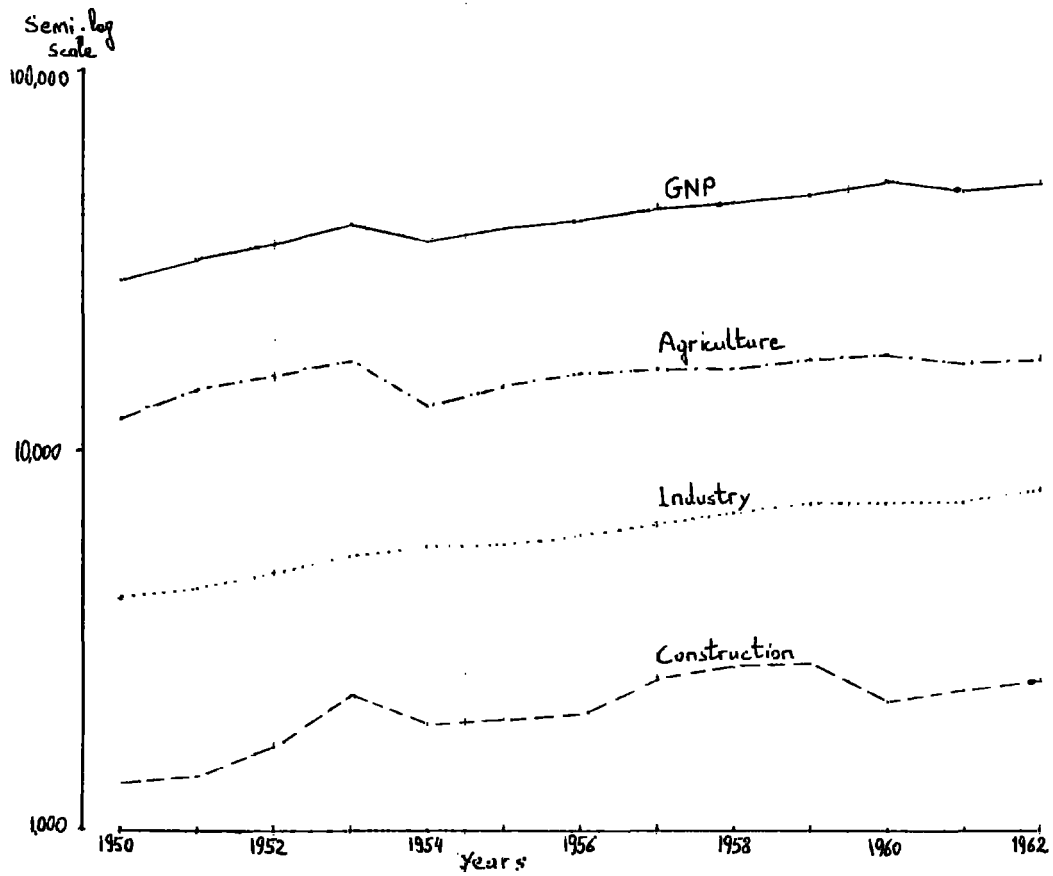
Diagram 2 — Level of GNP and Production of Some Sectors, 1950-1962.

(At 1961 prices; Million TL)

Both diagrams have been drawn on the basis of Table 6.
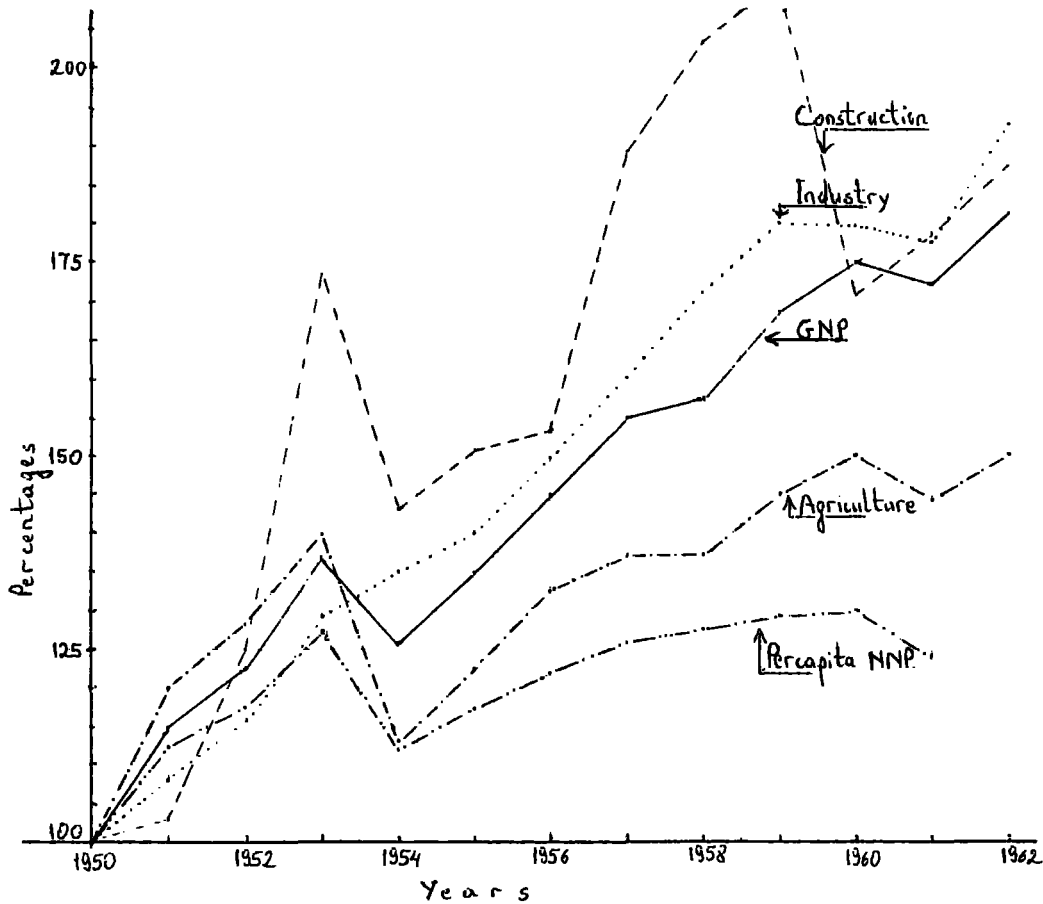
Diagram 3 — Indexes of GNP and Production of Some Sectors, and per capita NNP, 1950-1962.

TABLE 7

INDEXES OF G.N.P. AND PER CAPITA INCOME, 1950-1962

Years	Per Capita N.N.P. at 1961 Factor Cost (T.L.)	Index of Per Capita Income 1950 = 100	Annual Rate of Increase in Per Capita Income	Index of Total Income (G.N.P.) 1950 = 100	Annual Rate of Increase in Total Income
1950	1,181	100	-	100	-
1951	1,316	111	11	115	15
1952	1,391	118	6·3	125	8·7
1953	1,507	128	8·5	139	11·2
1954	1,332	113	-11·7	126	- 9·3
1955	1,393	118	4·4	135	7·1
1956	1,445	122	3·4	145	7·4
1957	1,492	126	3·3	154	6·2
1958	1,511	128	1·6	160	3·9
1959	1,530	130	1·5	167	4·4
1960	1,539	130	0·0	173	3·5
1961	1,469	124	- 4·6	170	- 1·7
1962				182	6·0

Source: S.P.O., First Five-Year Development Plan 1963-1967, p.15.

Note: In this table the per capita national income is shown in terms of N.N.P. at factor prices while the national income shewn in terms of G.N.P. at market prices. The

TABLE 8

GENERAL PRICE LEVEL (1950 = 100).

Years	Wholesale Price Index (Ministry of Commerce)	Chain Index of Wholesale Prices	Ankara Cost of Living Index (Central Statistical Office).
1950	100	 100	 100
1951	107	 107	 103
1952	108	.... 100·9	 107
1953	110	.... 101·8	 110
1954	121	 110	 119
1955	131	 108	 141
1956	153	 117	 151
1957	181	 118	 174
1958	208	 115	 208
1959	250	 120	 258
1960	263	 105	 264
1961	271	 103	 264
1962	286	 105	

Source: S.P.O., First Five-Year Development
Plan 1963-1967, p. 19.

(Continued from foot of page 23).

Note on Table 8 (contd.).

reason for this is this: the per capita national
income is usually used as a measure of economic welfare
while the national income is a measure of output or
production. For the former purpose N.N.P. at factor
costs is more appropriate whereas for the latter purpose
G.N.P. at market prices is preferable. (For the use of
various national income concepts for different purposes,
see U.N., E.C.A.F.E., Analysis of National Income in
Selected Asian Countries, Econ. Bull., Vol. III;
Nos. 1-2; 1952).

2. Product, Employment, and Productivity in Major Sectors:

     A. AGRICULTURE: The dominant place of agriculture in the Turkish economy has already been revealed, particularly by the section on the population issue (see Table 3 in p. 9).

     The agricultural production increased at a slower pace than G.N.P. during 1950-1962, 3·5% p.a. versus 5·1% p.a. This average of 3·5%, however, is heavily influenced by the performance of the agricultural sector through the period 1950-53, during which the average rate of increase in the agricultural production was 12·1% p.a. In the following sub-periods of 1953-58 and 1958-1961 the average rate of growth fell to 1·9 and 2·4% p.a., respectively.

     The agricultural production in Turkey is greatly influenced by climate. In the years of good weather, for example, in 1951, 1953 and 1956 agricultural production increased by as much as 21, 10, and 9%, but in the bad years of 1954 and 1961 fell by 20 and 5%. The influence of climate is intensified by the fact that much of the land brought under cultivation in this period was of marginal character and that the introduction of modern technology was not well-conditioned[1].

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1. These two factors are examined in some detail in pp. 30-34

In a study of the development of Turkish agriculture, one of the vital issues is of course the relationship between the growth rate of the population and that of agricultural production. As calculated on the basis of the data given in Table 9, the per capita agricultural produce has increased by 1·4% p.a. during 1950-55 and by 1·3% during 1955-60. As a matter of fact, the increase in the latter period possibly may be due in part to an overestimation of the agricultural income[1]. This is indeed disappointing in view of the fact that agriculture is the principal means of support for some three-quarters of the people, most of whom subsist on a deficient diet.

The data on employment in the agricultural sector are so scanty and undependable that no firm conclusions can be drawn from them. The average agricultural income shown in Table 3 is far from being a meaningful measure of productivity in the agricultural sector. Aside from the fact that it includes absentee landlords' income, the existence of a substantial degree of disguised unemployment and the large share of unpaid workers in the total labour force (55% in 1955) render it an unsatisfactory means for the measurement of productivity per person in the agricultural

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1. See pp. 28-30.

sector. Since the supply of labour as such does not create a
bottleneck in the agricultural production, it would be more
significant to consider the productivity per unit of cultivated
land or per unit of capital input which are , apart.from the
improved techniques, the use of better seeds,etc.,the real limiting

TABLE 9

INCREASES IN POPULATION, AGRICULTURAL PRODUCTION AND CULTIVATED
AREA DURING 1950 - 61.

Years	Population		Agricultural Production		Cultivated Area (including fallows)			Average Productivity Index
	Total (000)	Index	Index of Total 1950= 100	Annual In- crease %	Total (000 ha)	In- crease %	1950= 100 (III/VI)
	I	II	III	IV	V	VI Index	VII	VIII
1950	20,947	100	100·0	–	14,542	100	–	100
1951			120·7	20·7	15,272	105	5·0	115
1952			128·5	6·4	17,361	119	13·7	108
1953			140·7	9·5	18,812	129	8·3	109
1954			113·0	-19·7	19,616	135	4·2	84
1955	24,065	114·9	123·2	9·0	20,998	144	7·0	85
1956			134·0	8·8	22,453	154	7·0	87
1957			137·3	2·4	22,161	152	- 1·3	90
1958			137·3	0·0	22,765	156	2·7	88
1959			145·6	6·0	22,940	158	0·8	92
1960	27,830	132·8	151·9	4·3	23,264	160	1·4	95
1961			144·0	- 5·2	n.a.	n.a.	n.a.	n.a.
1962			151·0	5·0	25,348	174	–	87

Sources: The figures for the population and cultivated
area were taken from S.P.O., Development Plan
1963-67, pages 12 and 24.
The Index of the agricultural production was
calculated on the basis of the data given in
Table 6.

factors in the Turkish agriculture. Formidable statistical and
conceptual difficulties, however, are involved in the measurement
of productivity per unit of capital[1]. As regards the measurement
of productivity per unit of cultivated land, Table 9 may be
considered as having the necessary data for a rough estimation.
The agricultural production in 1960 was about 50% higher than in
1950, while the cultivated area expanded more than 60% during the
same period. This means that the average agricultural yield has
not increased but probably experienced some decline since 1950.
Actually, the average productivity per hectare throughout the
period 1954-1969 did not attain its 1950 level.

As a matter of fact, the estimation of the productivity per
hectare as made in Table 9 is nothing but the calculation of the
average yield per hectare used in the official estimates of the
total agricultural income. The State Institute of Statistics
estimates the total agricultural income from an estimate of the
total agricultural output, which in turn is based on the estimates
of the area sown under each kind of crops and that of yields per
hectare for each kind of crop. It has been established that the

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1. There are no statistics about the capital formation in the
   agricultural sector during the period 1950-1962. (O.E.C.D.,
   Turkey 1962/63, Paris May 1963, pp. 39-40.)

estimates about the agricultural yields are quite reliable whereas those concerning the areas sown to various crops suffer from a substantial degree of overestimation[1]. According to the State Institute of Statistics the total cultivated area was 24 million hectares in 1963. On the other hand, the preliminary tables of the 1963 Agricultural Census show the cultivated area as 15 million hectares. Still another estimate, made by Dr. G. Kazgan of the Istanbul University, mentions an area of something between 18 and 20 million hectares. The overestimation of cultivated area gives rise to three important points: (a) The national income estimates by the S.I.S. are influenced by the overestimation of the agricultural income. The State Planning Organization has there-fore been adjusting downward the national income estimates of the S.I.S. as from 1958. But Dr. Kazgan's estimate indicates that the overestimation begins at an earlier date, particularly as from 1955. Moreover, if the 1963 Agricultural census' results are somewhere near the truth, the downward adjustments in the S.I.S. estimates should be made by a greater degree than made by the S.P.O.

(b) The inequality in the income distribution between the sectors is possibly greater than is suggested by the available statistics.

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1. Dr. Gülten Kazgan, The Agricultural Income and the Land Reform, (in Turkish), published in the newspaper Cumhuriyet, 17/VII/1965.

(c) The excessive estimation is of the highest degree particularly in relation to the area sown under wheat, which is the subsistence crop for the major part of the agricultural population. This means that the income distribution within the agricultural sector is in fact worse than is indicated by the estimates based on the available figures for cultivated area.

There is no more surplus land which can be brought under cultivation; and, the ploughing of the poor steppe pasture has far exceeded safe limits[1]. The sown plus fallow area varied around 13 million hectares during the 1940's but stood at $22\frac{1}{2}$ million in 1956. By 1960 the crop area was 42% larger than that estimated as suitable for cultivation, that is, 16·4 million hectares, by Harvey Oakes, the U.S. soil management expert[2]. Deprived of the possibility of increasing the agricultural production by bringing new lands under plough, Turkey has to achieve a steady improvement in productivity in agricultural production. The immense importance of the issue calls for an analysis at some length of the factors which have hindered the improvement of productivity in the agricultural sector during 1950's. The low productivity of the Turkish agriculture is caused by the factors

1. U.N., F.A.O., "Mediterranean Country Report , TURKEY", Rome 1959, mimeographed, p. 1-3. (It is known in Turkey as Baade Report).

2. Eva and Abraham Hirsch, "Changes in Agricultural Output per capita of Rural Population in Turkey", 1927-1960, Economic Development and Cultural Change, July 1963.

which can be classified into two broad groups: structural and
technical factors.

Among the structural factors, the first to be considered
is the adverse effects on productivity of excessive population in
the agricultural sector. Since the limit was reached in extending
the crop area, the increase in population, on the one hand, and the
mechanization of farming, on the other, brought about an excess
population problem in the agriculture. This excess population
prevents the productivity from rising by hindering the extensive
use of new methods and by reducing the size of farm units to an
uneconomic extent. Furthermore, the population pressure has
resulted in the cultivation of those lands which should not have
been cultivated from the economic point of view[1].

Secondly, the present system of land ownership can also be
counted on in explaining the low productivity. In Turkey,
different types of ownership exist in combination. About three
quarters of the total families in the agricultural sector are
landowners (Table 10). The most of them are small landowners
(Table 5), and could not afford the expenses of soil conservation,
while there is no thought on the part of large landowners of

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1. S.P.O., 1964 Annual Program, p. 39. This point is particu-
larly stressed by E. & A. Hirsch, op. cit. They show that the
extension of cultivated area at the expense of pastures resulted
in the overgrazing and, hence, a decrease in the output per animal.

enhancing the value of land. Moreover, small landowners have not been able to unite by forming co-operatives and syndicates which could handle production more productively[1]. About 4 per cent of the total families work on the land belonging to others. In the face of the fact that the sharecropping and tenancy rights have not been based on precise contracts[2], the cultivator without security of tenure has no incentive to conserve land resources, improve the land with long term investments, and raise productivity[3].

TABLE 10

DISTRIBUTION OF PEASANT FAMILIES BY THE TYPES OF LANDOWNERSHIP.

	Number of families	%
Landowners	1,686,143	72·6
Semi-landowners	498,838	21·5
Tenant farmers	14·815	0·6
Sharecroppers	57·161	2·5
Labourers	9·734	0·4
Miscellaneous	7·984	0·3
Livestock breeders	47·716	2·1
Total	2,322,391	100·0

Source: Dr. H. Cillov, Economy of Turkey (in Turkish), p. 172.

1. S.P.O., Program for the Year 1962, p.
2. S.P.O., Development Plan, First Five Year, 1963-67, p.182.
3. Meier & Baldwin, Economic Development, John Wiley&Sons,Inc., New York 1957.

Regarding the technical factors accounting for the low productivity we can in the first place count the lack of modern technology. Despite the great emphasis put on mechanization of the farming by the agricultural development policy in the early 1950's, plough is still the most widely used tool of farming[1]. The modernization of agricultural technique in Turkey has been understood as the introduction of more and more tractors to the agriculture. In fact, the typical Turkish peasant /family has only ten to fifteen acres of land, which is far too small to make mechanization economically feasible, and, even on larger holdings, fragmentation often offers a further deterrent to mechanization[2]. Besides in countries like Turkey, where labour is abundant relative to capital, the objective should be to increase output per acre, not output per worker[3]. Investment in machinery to increase output per worker must be rather regulated to the availability of alternative employment opportunities for the workers displaced by the labour-saving innovations. To this end, the application of improved techniques which are not labour-saving but could raise productivity when applied to small-scale operations must have the

1. Dr. H. Cillov, op.cit., p. 187.

2. W. H. Nicholls, Investment in Agriculture in Underdeveloped Countries, American Economic Review, Papers and Proceedings, May 1955, p.

3. Meier & Baldwin, op.cit., p. 376.

priority over the capital-intensive mechanization. On the contrary, in Turkey, in the regions having the greatest numbers of relatively large farms, machinery investment per acre approximated that of medium to large commercial farms in the United States, where capital is relatively much more abundant and where machinery and fuel do not require foreign exchange[1].

The introduction of increasing amounts of tractors to the farming may, if not on the productivity ground, be justified, if it becomes an independent factor in increasing the total cultivated land. However, even this possible positive effect of mechanization was counteracted in Turkey by three facts: First, the expansion of cultivated area soon reached the marginal land. Secondly, the displaced tenants and sharecroppers[2] had to take land of poor quality because of lack of any other and of the absence of better employment opportunities. Finally, it destroyed part of the communal pastures and contributed to the decline in the output of animal products.

Apart from lack of modern farming equipment and unbalanced mechanization, the unsatisfactory condition of irrigation facilities

1. W. H. Nicholls, op.cit., p.

2. According to Prof. Brandon the one-third of the land brought under cultivation by tractors during 1948-52 was previously cultivated land. See: W. H. Nicholls, op.cit., p.

and inadequate use of fertilizers must also be counted among the
technical reasons for the present low productivity of the Turkish
agriculture. Approximately two-thirds of the Turkish territory
is sub-arid. There are wide variations in rainfall from one year
to another, and drought is a constant threat[1]. Under these
conditions the development of irrigation facilities appears as a
substantial problem. But, today, most of the cereal production
is carried out without irrigation. However, the problem facing
Turkey at present is not the lack of primary irrigation facilities,
but how to benefit most from an unbalanced irrigation development
which took place during 1950's. In 1957 the area under irrigation
lagged about 54,000 hectares behind the area commanded in the
Department of Hydraulic Works projects. It is therefore necessary
to increase investment in the facilities such as land levelling and
drainage for assuring that lands are actually irrigated[2].

The amount of fertilizers used in the Turkish agriculture
is very low. There are many reasons for it. First, natural
fertilizers are mostly used for other purposes. Secondly, the
prices of artificial fertilizers are high compared to crop prices.
Thirdly, the necessary technical knowledge and personnel are not
available to carry out an extensive programme for increasing use
of fertilizers.

1. U.N., F.A.O., op.cit., p.
2. F.A.O., op.cit., p.

B. INDUSTRY: With agriculture growing at a slower rate than G.N.P., the share of all the non-agricultural sectors in G.N.P. obviously increased.

TABLE 11

CONTRIBUTION OF NON-AGRICULTURAL SECTORS AND OF INDUSTRY TO N.N.P. IN 1959-62 AND CHANGE FROM 1950-53.

(percentage of aggregate product)

Sectors	1950-53	1959-62	Change
All Non-agricultural	50·0	58·1	+ 8·1
Industry[1]	15·5	17·3	+ 1·8
Other Non-agricultural	34·5	40·8	+ 6·3

1.   Industry = Manufacturing + mining.

Source: Table 6.

It is seen from Table 11 that as the share of agricultural production in N.N.P. diminished from 50·0 per cent, on average, in 1950/53 to 41·9 per cent in 1959/62, the contribution of industry and other non-agricultural sectors went up by 8·1 per cent in that period.   Table 11 also demonstrates that non-agricultural pursuits other than industry increased their shares by 6·3 per cent against a small increase of 1·8 per cent in industry.   Non-agricultural sectors other than industry comprise small-scale and unorganized

units in trading, transport, construction, and services -- exceptions
are a few large-scale State enterprises in public services and the
government employment of civil servants. So long as labour supply
remains abundant and capital scarce, a shift from agriculture is
likely to move into these activities because of high employment
potentials and low capital requirements there. In fact, economic
development in Japan and Latin American countries has been
accompanied by a shift from agriculture, first, to these sectors,
and, then, to industry. Even though productivity in these sectors
may be lower than in industry, they have no doubt helped greatly to
contain the social unrest that might have developed if large-scale
unemployment instead of the underemployment today prevailing, had
occurred, as a result of the failure of industry to absorb all the
new labour force plus the overflow from agriculture. Actually,
over the past decade, the services sector has shown the highest rate
of absorption of the new labour force with 5·6 per cent per annum
as against 5 per cent in industry and 3·9 per cent in agriculture[1].

Although industry has not increased its share in G.N.P.
significantly, it has obviously attained a considerable increase in
its total output. There is no industrial production index covering

1. O.E.C.D., "Turkey, Economic Surveys by the O.E.C.D., 1963",
   Paris 1963, pp. 9-10.

the country's entire production[1], but according to national income estimates, industrial production -- including mining but excluding construction -- almost doubled in real terms in the course of the period 1950-1962 (see Table 12 and Diagram 3). The average rate of increase in that period was 5·7 per cent per annum, which is higher than 3·5 per cent and 5·1 per cent rates attained by agriculture and the total output, respectively.

TABLE 12

INDEX OF INDUSTRIAL PRODUCTION

(At 1961 prices)		1950 = 100
Years	Index	Changes over previous year (%)
1950	100·0	-
1951	108·4	8·4
1952	117·4	8·3
1953	129·3	10.1
1954	135·5	4·7
1955	140·9	4·2
1956	150·0	6·5
1957	161·0	7·2
1958	172·2	7·0
1959	180·8	5·0
1960	180·3	- 0·2
1961	178·3	- 1·1
1962	193·0	8·2

Source: Table 6

1. Ministry of Commerce and C.S.O. publish industrial production indices covering partial production.

The expansion of industrial production attained the greatest rate in the early fifties. Its average rate of growth in 1950-53 was 9 per cent per annum against a rate of 5·9 per cent in 1954-58 and only 2·9 per cent in 1959-62. Comparing industry with agriculture, the first sub-period witnessed a greater increase in the agricultural production, while the industrial sector's performance was better in the other two sub-periods.

Available employment statistics cover only the insured workers, who comprise little more than one-quarter of the total employed outside agriculture. Moreover, changes in the basis of these statistics make any clear conclusions difficult. We, therefore, have to content ourselves with some round figures with regard to such issues as employment and productivity in industry. About 10 per cent of the active population are employed in industry (mining, manufacturing, public utilities and construction) (see p. 5). Of these, 850,000 persons are engaged in manufacturing. Employment in industry has been growing over the last decade at an annual rate of 5 per cent, whilst output was increasing 7·5 - 8 per cent per annum[1]. From this we can deduce that productivity per worker in industry has been increasing over the

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1. O.E.C.D., op.cit., p. 10.

last decade.   Assuming that employment in the industry defined
as manufacturing plus mining has also grown at an average rate of
5 per cent per annum, productivity per worker appears to be about
10 per cent higher in 1960 than in 1950 according to the index of
industrial production in Table 12.   In view of the scarcity of
capital in Turkey, changes in productivity per unit of capital in
industry may be considered a better indicator of economic progress.
The lack of data about the distribution of capital formation
amongst various productive sectors, unfortunately, deprives us of
such an indicator.

The performance of the industrial sector has undoubtedly
been hindered by such structural factors as the dominance of small-
scale production, the lack of diversification of production, and
the absence of an active enterpreneurial class.

The industrial production outside the public sector is
dominated by small enterprises using primitive techniques.
550,000 persons out of a total of 850,000 persons, who are engaged
in manufacturing (both public and private), work in establishments
employing less than 10 people.   But the value added to the
national income by the workshops employing less than ten workers
is only as large as that created by the private enterprises
employing ten or more workers.   This situation is one of the main
causes of the prevalence of low productivity and high production
costs.

The development of production of a range of simple consumer goods has been a feature of recent years. The establishment of plants engaging in the assembly of imported parts has also been an attractive field of investment, particularly for foreign private capital. The production of intermediate and capital goods has been relatively a small portion of the total industrial production. In 1962, two-thirds of the total value of production in manufacturing industry were created in enterprises engaged in the production of foodstuffs, beverages, tobacco and textiles. The production of metallic products (including basic metal products) , machinery, transport equipment, electrical machinery and agricultural equipment altogether amounted to only about 12 percent[1] of the total production of the manufacturing industry. The lack of an adequate diver= sifacation of the industrial production renders the Turkish economy particularly the industrial sector, vulnerable to the balance of payments difficulties. The development of bottlenecks is therefore a constant threat to the industrial production.

Enterprises in the private sector, even including corporations, are mostly family concerns. The management is held within the family, with a consequence that ownership and the functions of

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1. Calculated from Table 36 of the 1964 Annual Programme.

administration become inseparable.   Private enterpreneurs are also
reluctant to admit capital from outside their families.

The absence of an active enterpreneurialclass and of an
adequate pooling of private capital necessitated the government's
participation in production as from the early thirties.   At
present, about 40% of total industrial production is supplied by
the State Economic Enterprises (S.E.E.s).   The group of the S.E.E.
also includes important public utilities and various financial
institutions.   More than 60% of financial services, such as
banking, insurance, etc., are carried out by official institutions.
During the 1950's, an important expansion took place in the
productive capacity of the S.E.E., but this was accompanied by an
economic and financial disorder because of interferences with price,
output and personnel policies of the enterprises by the political
authorities.

3. Product Allocation and Consumption Level:

An important result of economic development, as well as
being a contributing factor to it, is the change in the allocation
of resources between consumption and investment.   There are no
reliable figures showing the allocation of the Turkish national
income between consumption and investment expenditures.   The

Turkish National Income is estimated only from the production
side. The State Institute of Statistics has recently published
its estimates of National Expenditure for the period 1950-1963.
But we avoid using these estimates here because neither their
G.N.E. figures nor the comprising items of them correspond to
the data supplied by the S.P.O. which are used throughout this
essay[1]. The S.P.O. gave in the Interim Programme for the Year
1962 its own estimates of National Expenditure during 1959-1962[2].
However, the 1961 figures in the S.P.O. estimates are provisional
and the 1962 figures are the programmed figures. As regards the
1959 and 1960 figures of the S.P.O. estimates, there are some
contradictions between them and the data given in the later
publications of the S.P.O. Therefore, an attempt is made in
Table 13 to estimate National Expenditure on the basis of data
made, either directly or indirectly, available by the S.P.O. (see
Note on Table 13).

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1. The presence of an overestimation of agricultural income in
   the S.I.S. National Income Statistics has already been
   revealed in Pages 28-30.

2. S.P.O., Programme for the year 1962, Ankara 1961, mimeographed,
   p. 34b.

TABLE 13

GROSS NATIONAL EXPENDITURES, 1950-1962.

(Million T.L. at current prices)

| | G.N.P. | + X - M | = G.N.E. = | INVESTMENT | | | CONSUMPTION | | |
				Total	Private	Public	Total	Public	Private
1950	10,384	140	10,524	1,000	673	327	9,524	1,785	7,739
1951	12,270	263	12,533	1,260	772	488	11,273	1,928	9,345
1952	14,320	554	14,874	1,836	1,088	748	13,038	2,404	10,634
1953	16,821	460	17,281	2,088	1,077	1,011	15,193	2,163	13,030
1954	17,114	499	17,613	2,518	1,462	1,056	15,095	2,337	12,758
1955	21,060	503	21,563	3,007	1,518	1,489	18,556	2,954	15,602
1956	24,334	217	24,551	3,260	1,423	1,837	21,291	3,152	18,139
1957	30,528	224	30,752	4,017	1,718	2,299	26,735	3,403	23,332
1958	36,108	349	36,457	5,042	2,005	3,037	31,415	4,187	27,228
1959	44,703	1,356	46,059	6,989	3,446	3,543	40,070	5,712	34,358
1960	48,963	1,224	50,187	7,779	3,749	4,030	42,408	6,153	36,255
1961	49,081	1,575	50,656	7,368	3,305	4,063	43,288	6,370	36,918
1962	55,248	2,178	57,426	8,096	3,860	4,236	49,330	6,751	42,579
1950-2	100	2·59	102·59	11·08	6·87	4·21	91·51	16·54	74·97
1960-2	100	3·25	103·25	15·17	7·12	8·05	88·08	12·57	75·51

Note on Table 13:   ·

        The G.N.P. figures for 1950-1960 have been taken
from S.P.O., Development Plan 1963-1967, p. 13; for
1961 and 1962 from O.E.C.D., Turkey 1963/64, Paris,
August 1964, p. 43.

        The figures for Net Exports of goods and services
for 1950-1960 have been taken from K. Kurdaş, "Basic
Factors Impeding a Rapid Growth of the Turkish Economy",
in the Capital Formation and ....., op.cit., p. 36,
Table 1.   They had been estimated on the basis of the
official rate of exchange and by taking into considera-
tion actual devaluations such as the Treasury Tax at
this rate.   The figures for the 1961 and 1962 Current
Account Deficits have been taken from the O.E.C.D.
Turkey 1963/64, p. 24; and Turkey 1965/66, p. 22.
The official rate of exchange was TL.2·80 until 1959
and TL.9·00 thereafter to the U.S. dollar.

        The Gross National Expenditure figures have been
found by adding the Current Account Deficit figures to
the G.N.P. figures.

        The Total Investment Figures for 1950-1960 have
been taken from S.P.O., Development Plan, p. 15; for
the divi:·sion of the total investment between Public
and Private Sectors, Mr. Kurdaş's data were used.
Mr. Kurdaş arrives at the private sector's investment
figures by subtracting the public investment from the
total investment.   His public investment figures cover
the whole public sector's investments, excluding those
of the enterprises in which the State's share is less
than 51% of the capital.   The 1961 investment figures
have been taken from the O.E.C.D., Turkey 1962/63, p. 38,
and the 1962 figures from the O.E.C.D., Turkey 1962/63,
p. 38 and Turkey 1965/66, p. 34.

        Total consumption figures are the residuals of
G.N.E.'s minus Investment.

        The current expenditures of the Public Sector,
excluding Local Authorities, for 1950-1960 are given in
the S.P.O., Development Plan, p. 17.   According to the
data given in the S.P.O., Programme for the Year 1962,

Note on Table 13 (contd.):

p. 346, and The Progress Report on the Implementation
of the 1963 Annual Programme, p. 32, the current
expenditures of Local Authorities are about 1/7th of
the total public current expenditure.   Assuming that
the same relationship held good during 1950's as well,
we could estimate the total current expenditures for
the public sector as a whole for 1950-1960.   The 1961
and 1962 current expenditure figures have been taken
from S.P.O., The Progress Report, ibid, p. 32.

        The figures for private consumption are found
as residuals.

        Mr. Kurdaş expresses that the data in his
Table 1 have been compiled by the S.P.O., The O.E.C.D.'s
above-mentioned Reports about Turkey also make use of the
statistics submitted by the S.P.O.

As seen from Table 13, the share of consumption expenditures

in G.N.P. fell from 91·51% in 1950/52 to 88·08% in 1960/62, dropping

by 3·43% of G.N.P.   No part of this fall, however, has been

allotted to the improvement of the external balance.   On the

contrary, the Table shows that the share of foreign sources in the

total resources rose by 0·66% of G.N.P. between 1950/52 and

1960/62.   The drop in the share of consumption together with the

increase in the foreign resources accounted for the increasing of

the share of total investment from 11·08% of G.N.P. in 1950/52 to

15·17% in 1960/62.

The arithmetic mean of the share of investment in G.N.P.

in 1950/52 and 1960/62, that is, 13·1% of G.N.P., could be regarded

as a rough estimate of the average rate of gross capital formation during the 1950-1962 period.   Relating this to the average rate of growth of G.N.P. in the same period, that is, 4·7% p.a. as calculated from Table 7, gives us an incremental capital-output ratio of 2·79.

Apart from its changing share, the investment expenditure has undergone a significant change also in its composition.   While the private sector provided a larger proportion of total investment in the beginning of the period, the Government's share has become larger towards the end of the period.   The share of the private sector's investments seems to have almost stagnated around 7% of G.N.P. whereas the Government's share has almost doubled by rising from 4·21% in 1950/52 to 8·05% in 1960/62.

Despite the increase in the share of public investment, the proportion of total resources used by the public sector did not change in terms of the percentage of G.N.P., remaining at about 20% in 1960/62 as it was in 1950/52.   This means a decline in the share of public current expenditure in G.N.P. from 1950/52 to 1960/62 has taken place.   It does not of course follow from this that the absolute level of public current expenditure has not increased. Actually, it has, in money terms, increased at an average rate of 11·7% p.a. during 1950-1962.   However, if allowance is made for a 9% p.a. increase in prices, it is hardly likely that the increase in

public current expenditure in real terms has kept pace with a

population growth $_\wedge$close to 3% p.a.   The political and economic

(of)

difficulties encountered in raising the share of public revenue in

G.N.P., together with the Government policy of investment drive,

have certainly been the main factors limiting the growth of the

share of public current expenditure.

Judging from the constancy in the share of the public

sector in G.N.P. as indicated above, it may be estimated that the

total real expenditure of Public Sector has increased at about the

same rate with the real G.N.P., that is, 4·7% p.a. during 1950/52 -

1960/62.   This reveals the fact that the per capita Government

spending[1] has risen somewhat during the fifties, since the rate of

population growth was about 2·9% p.a.

The part of G.N.P. left to the private sector increased

slightly from 81·84% in 1950/52 to 82·63% in 1960/62.   This increase

was made possible by the increasing share of foreign sources in total

resources as well as a slight decline in the share of the public

sector.   Of the increase in the share of the private sector, some-

thing less than 1/3rd was devoted to increasing the share of private

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1. The likelihood is that the rate of growth of Government expenditure
   as a whole is likely to be faster than that of population. (A. R.
   Prest, Public Finance in Underdeveloped Countries, London 1962,
   p. 15.).

investments while the rest was used for raising the share of private consumption in G.N.P.

The higher share of private consumption in 1960/62 than in 1950/52 reflects the fact that private consumption expenditures have grown at a greater pace than G.N.P. Actually the rate of growth of G.N.P. in money terms was on average 15·1% p.a. during 1950/52 - 1960/62 whereas that of consumption was 15·3% p.a. in the same period. This appears disappointing in view of the fact that the Turkish economy has to base its first Development Plan, which requires an immense saving effort from public, on such a record of high consumption propensity in the period immediately preceding the plan. If one allows for changes in the cost of living and in population, it can be estimated that per capita real consumption, excluding such collective consumption expenditures made by the Government as education, health, etc., rose from TL.430 : in 1950/52 to TL.528 : in 1960/62, increasing by 2·1% p.a. as compared with a rate of growth of 1·9% p.a. in per capita G.N.P.[1].

1. The cost of living deflator used here is calculated from Table 8 as 103 for 1950/52 and 264 for 1960/62. The population is calculated from Table 9 as 21,472,000 for 1950/52 and 28,503,000 for 1960/62. The G.N.P. figures are from Table 6. The rate of growth of per capita G.N.P. and that of per capita consumption, however, is not strictly comparable; but we would have had a more accurate comparison had we had the estimate of the G.N.E. at constant prices as well.

CHAPTER 2

OBJECTIVES OF THE PLAN

In Chapter 1 the social characteristics and economic development in the recent past of Turkey have been reviewed with a view to preparing the background for a study of the method of financing of the "First Five-Year Development Plan, 1963-1967". The background information will be completed with this Chapter by setting out the targets envisaged by the Plan. (The resource requirements of the Plan will not be dealt with in the present Chapter since the discussion of that will occupy us throughout the remaining part of my dissertation. In the next Chapter, however, when we study the cumulative nature of the Plan within the Financing Strategy, we shall have an opportunity to observe the specifications of the Plan with regard to the resource requirements). In the first section we shall have a look at the objectives of the long-term plan. In Section II, the objectives of the First Five-Year Plan will be viewed, the emphasis being put on the conflict between them and on the extent to which they have hitherto been fulfilled.

I

OBJECTIVES OF THE PERSPECTIVE PLAN

The objectives of the First Five-Year Plan have been determined within the context of the objectives of a Fifteen-Year Perspective Plan. It is therefore illuminating to outline the objectives of the Perspective Plan before we discuss those of the First Five-Year Plan.

The basic long-term objectives are to attain the highest possible level of employment at satisfactory income levels, to achieve balance in external payments, and to establish social justice.

The G.N.P. is expected to increase by 175 per cent in 1977 above its 1962 level, growing at an annual compound rate of 7 percent. But a population growth of 3 per cent per annum, which is assumed to prevail during that period, will allow an increase only by 78 per cent in per capita gross income. This increase in total production will be accompanied by a change in the structure of production. The share of agricultural production in G.N.P. will go down from around 44 per cent in 1962 to about 30 per cent in 1977. This will also be reflected in the changing distribution of active population among the sectors, agriculture's share falling

from 77 per cent in 1962 to 58 per cent in 1977.

Even an expansion of that scale of production will not suffice to provide employment for the new labour force plus the existing unemployed and underemployed. It is estimated that, during the Perspective Plan period, 6·8 million new jobs will be available while the amount of new workers seeking employment will amount to 7·5 million.

Achievement of an egalitarian distribution of income is one of the major objectives. In this connection, the needs of the masses have guided the distribution of both investments and public current expenditures. The stress has been laid on distributing the burden of development more equitably. An extensive system of social security has also been proposed to contribute to the establishment of social justice.

Financing of the realization of these targets would not be possible only from domestic sources. External resources are therefore expected to continue accommodating the savings gap until the end of the second five-year plan in 1973. It is planned that the external deficit of an order of 4 per cent. of G.N.P. in 1962 will gradually diminish and the economy will attain a self-sustained character by 1973.

We are thus confronted with a multiplicity of objectives. This is, however, a common feature of all social and economic problems, distinguishing them from technical problems. It is the search for a balance between limited means and various ends that gives rise to an economic problem. Where there is a multiplicity of ends, various ends may not be harmonious but may be in conflict with each other. This is indeed the case faced by the planners in every country. In the case of Turkey, the above-mentioned objectives -- to secure a 7 per cent. rate of growth against a rate of 4·7 per cent.[1] realized in the last decade, to achieve external balance, to approach the full-employment and to secure an egalitarian distribution of income.-- are clearly in conflict with each other, particularly in the short-run. To achieve more of one end may be possible only at the expense of achieving less of another end. A rapid growth, for example, will be easier to achieve if concentration in some industrial sectors and in already developed regions is permitted.

To get out of this dilemma the Turkish planners have rightly decided to sacrifice relatively in all objectives but a

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1. This is the average rate of growth achieved during the period 1950/52 - 1960/62 which represents better the trend of the growth of G.N.P. during the last decade than the rate of 5·1% belonging to the period 1950 - 1962.

7 per cent. rate of growth of G.N.P. in the First Five-Year Plan period.   Let us now consider the implications, conflicts and the degree of fulfillment attained of the objectives of the First Five-Year Plan.

II

OBJECTIVES OF THE FIRST FIVE-YEAR PLAN

The main objectives of the Plan can be stated under four headings in parallel to those of the Perspective Plan.

1.   To Secure a 7 per cent. Rate of Growth:-

The central objective is to attain a 40 per cent. growth of G.N.P. in the end of the first five-year.   On average, this means a 7 per cent. year-to-year increase in G.N.P.   This rate has been considered by the planners as the necessary rate of growth for the following reasons: (a) Assuming that the population would grow 3% annually during the Plan period, the 7% growth rate would enable Turkey to increase its per capita income by about 4% annually.   This would allow Turkey to narrow the gap between her per capita income and that in the O.E.C.D. countries which aim at increasing their per capita incomes by 3% per annum during the

1960's[1].   (b) A lower rate of growth would render the problem of

unemployment insoluble in the near future[2].   An international

comparison may also show that the Turkish target rate of growth

of G.N.P. is not very high: Israel aimed at 9·5% in her 1962 -

1966 Plan, Japan at 7·8% during 1958 - 1970, Yugoslavia at

11·3% during 1962-65, Egypt at 6·8% during 1961 - 1966.   However,

whether a 7% target rate of growth is too high or not can better

be considered in relation to the performance of the economy in

the recent past.   As already seen, the Turkish economy grew at

an average rate of 4·7% p.a., during the period 1950/52 - 1960/62.

But if the actual year-to-year changes are observed from Table 7,

it can be seen that the years with a growth rate, say, above 6%

are not exceptional but account for more than half of the thirteen

years period of 1950 - 1962.   The conspicuous element behind the

high growth rates, however, was always the effect of a good harvest.

Since a favourable projection of good harvests for the whole Plan

period could not be a basis for the choice of a 7% target rate,

the decision must have been based on more feasible assumptions.

Actually the determinants of a 7% target rate of growth

have been the estimates that the incremental capital-output ratio

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1. O.E.C.D., Turkey 1963/64, p. 12

2. See page 64-68.

would on average be 2·6 during the Plan period and that an 18%

of G.N.P. would on average be invested annually in that period.

Although in Chapter 1 the incremental capital-output ratio for

the period 1950/52 - 1960/62 was roughly calculated as 2·8, the

estimate of an average capital-output ratio of 2·6 seems to be of

the right order in view of the presence of underemployed and idle

resources by the beginning of the Plan period[1].   As regards the

investment ratio, the planned average rate of investment, that is,

18·3% of G.N.P. per annum, rising from 17% of G.N.P. in 1963 to

19·4% in 1967, seems to be quite high as compared with the13·1%

attained in 1950/52 - 1960/62.   But it must be remembered that

the investment/income ratio already exceeded 15% of G.N.P. in the

immediate pre-plan years.   In this connection, one can also argue

that the economic planning is not merely a process of extrapola-

ting the prevailing trends, but is to be utilized for effecting

changes in the trends of the strategic aggregates in the economy.

Nevertheless, it is obvious that the postulated investment/income

ratio should not be beyond the possibility of the economy's

mobilizing the adequate resources.   The Plan has not actually

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1.   See Chapter 3, page 80-81

seen it possible to raise all the required resources from domestic sources[1].

The growth of G.N.P. is planned to be accompanied by a change in the structure of production.   The share of the agricultural sector in G.N.P. is estimated to decline from 43·8% in 1962 to 38·3% in 1967.   On the other hand, the share of the industrial sector will rise from 16·8% in 1962 to 21·4% in 1967.   The extent of the proposed structural change appears to be considerable when it is compared with the corresponding change in the last decade or so.   The Plan envisages a fall of 12·5% in the share of agriculture during the Plan period as against a 16% drop during a period of about ten years in 1950/53 - 1959/62 and a 27·4% increase in the share of industry during the first five-year Development Plan against a 11·6% increase in the 1950/53 - 1959/62 period[2].   It is envisaged in the Plan that the agricultural sector would grow at an average rate of 4·2% p.a. and industry at 13% p.a.   It has been shown in Chapter 1 (pp.25 and 38) that agriculture and industry have grown at the rates of 3·5% p.a. and 5·7% p.a., respectively, during 1950 - 1962.   It is thus seen that the target rate

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1. The specifications of the Plan with respect to the financing is examined in detail in Chapter 3.

2. The ratios for the period 1950/53 - 1959/62 are based on Table 6 in Chapter 1.

of growth for industry has been set very high in comparison with that
attained in the pre-Plan period whereas that for agriculture has been
set at a relatively low rate.

How far has the objective of a 7% rate of growth of G.N.P.
hitherto been fulfilled ?   Table 14 provides a bird's-eye view of
the fulfilment of the main objective of the Plan, that is, 7% growth
per annum of G.N.P., together with the changes in its composition.
During the first four years of the Plan period, including the
preliminary year of 1962, the average rate of growth of G.N.P. has
been 5·8% p.a.   Only in 1963 the target was attained, even exceeded.
The second best year was 1962, with a growth rate of 6·1%.   It was
however very good harvests that made it possible to achieve high
growth rates in 1962 and 1963.   The agricultural production has
stagnated at its 1963 level during 1964 and 1965.   For the whole
period of 1961-65, the average rate of growth of the agricultural
production is 3·4% p.a., which is not too much below the target rate
of 4·2%.   However, if the relatively important share of agriculture
in G.N.P. is taken into account, the shortfall becomes significant.
The industrial sector has been growing at a much higher rate than in
the pre-Plan decade -- 7·9% versus 5·7% -- and has been steadily
stepping up its growth rate.   But the shortfall between the realized
and target growth rates of industry is considerable and has been

TABLE 14

RATES OF GROWTH OF G.N.P. AND CHANGES IN ITS STRUCTURE, 1961-65.

(at 1961 prices)

	1961		1962			1963			1964			1965			Actual Average Rate of Growth (%)	Target of the Plan
	Million T.L.	% of Total	Million T.L.	% of Total	Change %	Million T.L.	% of Total	Change %	Million T.L.	% of Total	Change %	Million T.L.	% of Total	Change %		
Agriculture	17·3	40·6	18·2	40·6	5·6	19·6	40·5	7·4	19·6	39·1	-0·2	19·8	37·4	1	3·4	4·2
Industry	7·3	17·2	7·8	17·3	6·9	8·4	17·4	8·0	9·1	18·1	8·6	9·9	18·8	9	7·9	13·0
Services & Construction	17·9	42·2	19·0	42·1	5·8	20·4	42·1	7·3	21·7	42·8	6·3	23·2	43·8	7	6·7	7·2
Domestic Income	42·5	100·0	45·0	100·0	5·9	48·4	100·0	7·5	50·4	100·0	4·1	52·9	100·0	5	5·5	
G.N.P.	49·1	-	52·1	-	6·1	56·0	-	7·5	58·4	-	4·3	61·5	-	5·3	5·8	7.0

Sources: The figures for 1961-1964 inclusive are from S.P.O., A Summary of 1966 Annual Programme, (First Draft), mimeographed, p. 43, Tables 1 and 2. The 1965 growth rates have been taken from O.E.C.D., Turkey 1965/66, p. 6, Table 1, and other data have been càculated by applying these rates to the 1964 figures. The target figures are from S.P.O., Development Plan, p. 136.

responsible for a good part of the failure of G.N.P. to attain the
7% target rate of growth.

2. To Reduce the Balance of Payments Deficit:-

Turkey entered the Plan period suffering from a chronic
external deficit, which averaged 1,300 million TL or 2·8% of the
G.N.P. in 1959 - 1961.   With the reactivation of the economy in
1962 it rose to 2,100 million TL (about 4% of G.N.P.).   According
to the Plan, it should reach 4·1% of G.N.P. in 1964 and then decline
to 2·8% of G.N.P. by 1967.

The foreign assistance to underdeveloped countries has a
two-sided effect for the aid-receiving country: it supplements
domestic resources and contributes to foreign exchange balances.
In the case of Turkey, in which the demand for her exports of primary
commodities is not very elastic and considerable efforts will be
needed to develop significant amounts of new exports, the contribu-
tion of foreign aid to exchange reserves is more important than to
total investment resources.   In other words, the target rate of
growth in Turkey would have to be reduced by considerably more than
the share of aid in the total investment, i.e., 18% on average during
the Plan period, if aid were eliminated, since the productivity of
domestic investment would then be considerably less.

The fulfilment of the second objective in the early years
of the Plan implementation can be seen from Table 15.   In the
transitional year 1962, the deficit on the balance of current
accounts reached 4·4% of G.N.P., exceeding the target by 0·4% of
G.N.P.   A divergence of the same order from the target took place
in 1963, i.e., an actual deficit of 4·5% against a planned deficit
of _____ ‾ ‾   _ _ _ _   ·4·1% of G.N.P.   The main

TABLE 15

PLANNED AND ACTUAL DEFICIT ON THE BALANCE OF
CURRENT ACCOUNT, 1962 - 1964.

$ million

	1962		1963		1964	
	Plan	Actual	Plan	Actual	Plan	Actual
Imports (c.i.f.)	560	622	567	687	627	542
Exports (f.o.b.)	325	381	348	368	374	411
Balance of Trade	-235	-241	-219	-319	-253	-131
Invisible Items (net)	- 78	- 41	- 79	- 9	- 69	- 45
Infra-structure and Off-shore*	45	40	47	49	49	40
Balance of Current Account	-268	-242	-251	-279	-273	-136
Deficit/G.N.P. (%)	4·0	4·4	4·1	4·5	4·1	2·3

* This is the official label used for the foreign currency
earnings from the establishments and activities of N.A.T.O.
in Turkey.

Sources: S.P.O., "Development Plan, 1963-1967", and Annual
Programme for 1963, 1964 and 1965.

reason of the divergencies from the targets both in 1962 and 1963 lies in the fact that the actual imports exceeded considerably the estimates in those years.

With reactivation of the economy, the value of "normal" imports -- i.e. excluding U.S. surplus commodities -- increased sharply in 1962. Imports of capital goods rose considerably, but the largest increase was in raw materials. The strong measures taken progressively since the beginning of 1963 to curb imports started showing their effects in the second half of 1963. Contrary to imports, exports in both 1962 and 1963 exceeded the forecasts in the Plan. They reached an exceptionally high level in 1962, but dropped slightly in 1963. The decline was smaller than that fore-seen in the Plan, largely because of higher prices obtained for tobacco and of satisfactory cotton exports.

Since additional measures were taken in 1964 to curb imports more and since neither the increase of industrial production nor the volume of investment attained the forecasts of the Plan, the imports in 1964 stood at well below the level foreseen in the Plan. On the other hand, the steps taken in 1963 to encourage the growth of exports and the bumper tobacco crop of 1963 were reflected in export earnings of 1964, making these earnings reach a record level at $411 million. The relatively small volume of the deficit in 1964 (2·3 per cent of

G.N.P.) was therefore due to the factors of a temporary character
rather than to the favourable changes in the structure of the
foreign trade of Turkey. As a matter of fact, given the present
small share of manufactures in Turkish exports -- in 1963, "indus-
trial products" accounted for 20% of total exports, the more
important items of this group being petroleum products, copper and
food items -- it is unlikely that any increase in this group's
share will have a large total effect in the next few years before
the end of the Plan period. Thus, an expansion in exports in the
rest of the period will require improvements in agricultural
productivity and in the corresponding processing and marketing
facilities. As regards the trend of imports in the coming years
of the First Five-Year Plan, it must be pointed out that the bulk
of imports now represents essential commodities. To achieve still
some more reductions in imports through the import-substituting
projects depends on the speed of new productive investment; but
this, in turn, will necessitate a heavy dependence on the imports
of capital equipment in the rest of the Plan period.

Apart from the formidable difficulties in improving the
balance of current accounts, the accommodation of its deficit is
also made more difficult by the repayments of foreign debt falling
due in the Plan period. The servicing of the external debt,

excluding interest payments which are included in the "Invisible Items (Net)" in Table 15, have followed a trend rising from $97 million in 1962 to $114 million in 1963 and to $140 million (34% of the total export earnings) in 1964, a trend which is most likely to continue rising in the coming years as well[1]. In view of the foregoing facts, it seems rather safe to assume that even the maintenance of the external deficit at its level in the beginning of the period will be difficult, not to mention the reduction foreseen in the Plan.

3. To Secure a Progressive Reduction of Unemployment:-

The planned rate of growth of G.N.P. and the change in the structure of production which is expected to take place over the future will not be sufficient to solve the employment problem of the Turkish economy even by the end of the Fifteen Year Perspective Plan. The unemployment in Turkey as in all underdeveloped countries is a structural problem, arising mainly from the shortage of capital in industry. Recognizing this, the Turkish planners have given priority to projects tending to create employment and to the exploration of the intensive application of labour-using and capital-saving

1. O.E.C.D., "Economic Surveys, Turkey, 1964", Paris, August 1964, pp. 35 and 40.

technology in agriculture, construction and handicrafts[1]. More labour-intensive but less efficient methods of production can, however, increase employment today at the expense of producing less surplus which provides investible funds for more output and employment tomorrow. The First Five-Year Plan, considering the conflict between "maximum output" and "maximum employment" in the short-run, has rightly aimed at the reduction of unemployment so far as it does not hinder the achievement of a 7 per cent. growth of G.N.P. per annum.

Structural conditions in Turkey, which have been explained in Chapter 1, necessitates the creation of employment in non-agricultural sectors if the problem of unemployment is to be solved; but this, in turn, under the present structure of production, requires a heavy dependence on imported capital goods and raw materials. Thus once more there is a conflict between the objectives of the Plan; this time between the second and the third objectives.

Lack of statistical data on employment, which has already been pointed out in Chapter 1, makes difficult the observation of the actual developments in the state of employment. The S.P.O. estimated the total labour force in the three major sectors in 1961 according to the information from the 1955 census concerning the active population

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1. S.P.O., 1964 Annual Program, p. 30.

of 15 years of age and above, and from the 1 per cent. sample results
of the 1960 census.   From this estimation the S.P.O. arrived at the
labour force projections by major sectors for the Plan period, which
are shown in Table 16;.   It is estimated that the opening up of new
employments would not be on a scale sufficient to absorb all the
increases in the labour force, though the numbers of those unemployed
would decline from 1·5 million in 1962 to 1·18 million in 1964.

As the industrial production in 1962-64 failed to expand as
much as anticipated by the Plan and as it is unlikely that real wages
fell in those years[1], it seems quite safe to assume that the actual
figures for industry in 1962-1964 remained below the levels shown by
Table 16.   Accordingly, since it is unlikely that there will be any
slowing down in the rate of population growth in such a short time,
either the actual figures for the unemployed or the actual figures
for the active population in the agricultural and services sectors
must have turned out to be greater than those given in Table 16.
In the absence of an unemployed payment system in Turkey, it is more
reasonable to suppose that the increases in the total labour force
have somehow squeezed themselves into employment in either agricul-
tural or services sectors to earn their living rather than assuming
that they have stayed as unemployed.   This means that the active

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1.   O.E.C.D., "Turkey 1963/64", p. 13;   and, see p.   of this work.

TABLE 16

EMPLOYMENT PROJECTIONS OF THE PLAN

(In Millions)

	1961	1962	1963	1964	1965	1966	1967
Agriculture	9·80	9·86	10·00	10·14	10·28	10·42	10·56
Industry	1·18	1·25	1·34	1·44	1·54	1·65	1·77
Services	1·57	1·63	1·78	1·94	2·12	2·31	2·52
TOTAL ACTIVE POPULATION	12·55	12·74	13·12	13·52	13·94	14·38	14·85
Unemployment and Underemployment		1·5	1·3	1·18			
TOTAL LABOUR FORCE		14·24	14·42	14·7			

Sources: S.P.O., "Development Plan, 1963-1967", pp. 419-20.

S.P.O., "1963 Yili Programı", p. 59.

S.P.O., "1964 Yili Programı", p. 46.

Note on the methods of projections: For the calculation of the
total labour to be employed in industry and services during
the Plan period the S.P.O. relied on the estimated production
increases and the labour force elasticity coefficient based
on production-employment series of previous years. Employ-
ment in construction, which is included in the item "industry",
was calculated on the basis of investment targets, the
estimated share of construction in investment and the labour
coefficients in construction. In projecting the manpower
requirements of the agricultural sector, the labour require-
ments of the main crops under both irrigated and dry farming
were first determined and additional requirements were found
according to the increase in irrigated areas. /contd.

Note on Table 16 contd.

        The above projections were revised in 1963. Unfortunately, I do not have all the revised data but only for 1964. According to the revised estimates, the total labour force in 1964 was 13·8 million while the total employment reached only 12·4 million, leaving a remainder of 1·4 million underemployed and unemployed.

population in these sectors has grown bigger than that foreseen in

the Plan. On the other hand, the production of these sectors

remained below the targets set for them in the Plan. It follows

from these developments that the existing problem of disguised

unemployment in the agricultural and services sectors has been

aggravated during the early years of the Plan implementation.

    4. To Secure an Income Distribution in Conformity with
       Social Justice:-

It has been shown in Chapter 1 that the per capita income in

Turkey is very low in comparison with that in the advanced countries,

and that the average rate of increase in the per capita income had

been slow during 1950-1962. It has been also pointed out that

considerable disparities exist in the distribution of income and

wealth. The studies made by the S.P.O. have revealed that the

economic and social policies of the 1950's, particularly inflation,

have worked towards widening the disparities in both interpersonal

and interregional distribution of income[1].

The conflict between raising the output and achieving a more equal distribution of income made it impossible to adopt the latter as an objective of the First Five-Year Plan. However, since economic planning can both shorten the interval before a satisfactory standard of living for all is reached and indicate the selection of some welfare measures which do not prolong the interval greatly, the Plan has adopted it as a long-term objective but to be approached in the First Five-Year period only as far as it does not hamper the attainment of the first objective. Consequently, the elimination of the inequalities, in the sense that everybody will benefit by a fair distribution of income, a social security system and the equality of opportunity, is proposed to be realized by 1977 through the measures checking inflationary forces, redistributive financial policy and providing the individual with facilities such as education and health services to develop his own abilities.

It is very difficult to assess at this stage of the Plan implementation the effectiveness of the measures concerning the present objective. But there are some indicators which may give us a rough idea about the fulfilment of the objective.

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1. S.P.O., Development Plan 1963-1967, pp. 45-51.

In 1963 only 83 per cent. of the funds allocated for
investment in education and 30 per cent. of the investments in
agricultural education were realized.   Although the educational
investment in 1964 is expected to mark an improvement over 1963, it
is still expected to fall short of the programme targets.

A programme of socialization of health services is in progress,
but because of delays in investments in health the programme targets
are not being realized within the time limits envisaged by the Annual
Programmes.   Moreover, in the regions where health services were
already socialized the programme loses some effectiveness because of
the lack of co-ordination with such activities as road construction,
water, telephone, school and transport services.

There is an improving trend in the developments of social
security institutions.   Those falling within the scope of various
social security institutions constituted 29 per cent. of 2·5 million
people employed in the non-agricultural, wage-earning and salaried
occupations in 1963.   This ratio was 34 per cent. in 1964, and today
38·4 per cent. of 2·9 million people employed in the non-agricultural
occupations are covered by the social security institutions.

As regards the elimination of the disparities in income
distribution, various measures were introduced to that effect during
the early years of the Plan period.   The amendments to the Law on

Collective Bargaining, Strikes and Lockouts and the Social Insurance

Law, are the new measures which protect the low income classes.

The amendments to the taxation of private cars and to the

Inheritance and Devolution Laws, and the taxation of real estate

and agricultural incomes can be considered as measures reducing the

disparities in the income distribution.   On the other hand, the

difficulty of preventing /tax evasion continues to be a drawback for

an equitable income distribution.   Also, the taxation of agri-

cultural incomes, which was first introduced in 1963, has not been

effective to mitigate the unequal income distribution in the agri-

cultural sector.   In effect, tax measures must be supplementary

to a comprehensive land reform if the great income inequality in

this sector is to be eliminated.   But the frustration of the

efforts put into that effect since the May 1961 Revolution proves

that the realization of any significant land reform in the near

future is out of question unless the power structure of the country

changes.

CHAPTER 3.

THE STRATEGY FOR FINANCING THE PLAN

In the preceding chapters we have made an introduction to the main economic problems of Turkey and reviewed the basic objectives of the First Five-Year Development Plan. The present chapter discusses the strategy adopted by the Plan with respect to the financing of economic development during the period 1963 - 1967. This discussion will consist of the following points, each of which being taken up in a separate section below:-

1. The breaking down of the total saving requirements between domestic and foreign savings;

2. The cumulative nature of the process of domestic financing;

3. The breaking down of the domestic financing between private and public sectors;

4. The attitude of the Plan towards deficit financing.

I

As seen in the last chapter, the basic objective of the Turkish Development Plan is the attainment of a 7 per cent. compound rate of growth in G.N.P. per annum. The rate of investment required to attain this rate of growth has been calculated as

18·3 per cent. of G.N.P. on average on the basis of the assumption that the incremental capital-output ratio during the plan period would be 2·6 on average, rising from 2·43 at the beginning to 2·77 at the end of the period (see Table 18). It is taken for granted that the rate of investment envisaged by the Plan is of the right order in order to realize the Plan's objectives. Accordingly, the main problem of the financing policy appears to be how to raise the rate of total saving so as to match the rate of investment envisaged by the Plan[1], as the rate of total saving in the Turkish economy has always been below the rate proposed by the Plan[2].

The extent of the increase required in the domestic savings, which is what matters from the point of view of our dissertation, depends in the first place on the volume of foreign savings which is likely to be available to the economy in the course of the plan period. But, since the calculation of foreign saving requirements of the Turkish Plan has been made on a residual basis, the determining factor of the burden to be placed on the

1. This follows from the fact that real investments can be financed only by real savings as the aggregate realized investment is always equal to the aggregate realized savings in a national economy.

2. The trend of savings in the Turkish economy in 1950-62 is examined in p.83-87 below.

domestic financing of the investment programme has not directly

been the availability of foreign savings. On the contrary, the

policy decision on the rate at which domestic savings could feasi-

ibly be increased during the plan period has been the determining

factor of the volume of foreign savings required.[1] The difference

between required savings and domestically feasible savings

constituted the required foreign savings. To this, the debt service

obligations of the pre-plan debts have been added; and from this,

the expected inflow of private foreign investment and P.L.480 aid[2]

have been deducted in order to arrive at the foreign aid that must

be obtained. This current account deficit has also been checked

for its consistency with the estimated imbalances in the supply

(i.e. imports + domestic production) of and demand (i.e. final+

intermediate) for commodities and services[3].

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1. Professor Jagdish Bhagwati, O.E.C.D. consultant, "Some Reflec-
   tions on the Critigues of the Turkish Plan", a confidential
   report to the S.P.O., May 1964, mimeographed.

2. The United States Congress passed in 1954 the Agricultural Trade
   Development and Assistance Act which came to be known by its
   serial number, Public Law 480. The fundemental idea behind the
   law, as laid down in its preamble, is to make most efficient use
   of the U.S. surplus agricultural commodities.

3. This check has been made according to Tinbergen's method of
   successive stages and iteration through a sectoral breakdown of
   the production and value added levels (This method is explained
   in J.Tinbergen & C.B.Hendricus, Mathematical Models of Economic
   Growth,McGraw-Hill Book Comp.,Inc., New York 1962). A different
   technique is used by H.B.Chenery and M.Bruno in their article on
   the Israeli economy in the Economic Journal,March 1962. They
   simultaneously calculate and match the current account deficit
   from both the savings and the structural aspects.

In an international comparison, the share of the foreign savings in the total savings in the Turkish Plan appears to be on the low side with the result that a relatively greater burden is placed on domestic financing in Turkey than in many other under-developed countries.   It is, on average, ·18 for the Turkish Plan as against ·39 for Israel, ·30 for Greece, ·30 for Nigeria, ·22 for India, and ·56 for Korea[1].   The foreign saving requirements of the Plan cannot be reduced by increasing the export earnings and private foreign investments.   Increasing export earnings cannot give additional resources to Turkey which foreign aid can do.   As regards the private foreign investments, the Turkish regulations for attracting such investments are very generous and, according to Professor Bhagwati, if anything, these regulations need to be tightened to prevent an excessive burden building up on the balance of payments in the future through profit repatriation[2].

The rate of domestic saving foreseen in the Plan cannot be claimed to be too low either on the ground of the economy's past performance or in comparison to the efforts of other underdeveloped countries in this respect.   The rate of domestic saving to be

1. H. B. Chenery, "Foreign Assistance and Development Planning" in the Capital Formation and Investment in Industry, a report of an international conference held at Istanbul in August 1962, Istanbul Matbasi, Istanbul 1963, pp. 305-20.

2. J. Bhagwati, ibid.

attained in 1967, namely, 16·5% of G.N.P., is almost twice as high

as the average rate of domestic saving obtained in 1950-52, that

is, 8·5%.   This means that the Turkish public in 1967 will have

increased its average propensity to save by approximately 100% in

a decade and a half.   If we compare the 1963-67 average rate of

domestic saving aimed at in the Plan, i.e., 14·8% of G.N.P., with

the average rate in the immediate past, e.g. 12% of G.N.P. in

1960-62, it is seen that about a 23% increase in the average pro-

pensity to save is to take place during the plan period.   This is

not a modest target in terms of the sacrifice required from a

nation with a low standard of living and a high rate of population

growth.   In fact, the average domestic saving ratio of ·148 in

the Turkish Plan compares favourably with ·159 of Greece, ·154 of

Chile, ·150 of Israel, ·139 of Philippines, ·108 of Nigeria,

·162 of India, ·071 of Pakistan, ·092 of Korea[1].   In order to

obtain the above-mentioned increase in the domestic saving ratio

the Plan envisages a marginal propensity to save of ·27, which

compares yet more favourably with that in other countries: ·176 in

Nigeria, ·165 in Pakistan, ·246 in Greece, ·266 in the Philippines,

·29 in Israel, ·325 in Chile[2].

1.   These figures were calculated from the Table 1, H. B. Chenery,
     ibid.
2.   These figures were taken from J. Bhagwati, ibid, who had quoted
     them from H. Chenery, Approaches to Development Planning, a
     paper presented to the Congress of the International Economic
     Association, Vienna, Sept. 1962.

From the angle of the strategy for financing the Plan, the most significant point with the foreign component of the total saving requirements is its trend as foreseen in the Plan. As shown in Table 18, the share of the foreign in the total saving is planned to contract as from 1965[1]. This is another way of expressing the fact that, since Turkey cannot rely in the long run on foreign aid to realize her economic development, it is necessary for her to increase the share of the domestic saving in the total saving so as to achieve a self-sustained economic development in the near future[2].

II

The method of calculation of investment (saving) requirements of the Turkish Plan can be summed up in this formulation:-

$$\frac{\triangle Y}{Y} = \frac{I}{Y} \cdot \frac{1}{v}$$

where Y denotes the national income, I total investment and v incremental capital/output ratio. The Plan uses this formulation to calculate not only the total amount of /gross investments that is likely to

---

1. It is proposed that this contraction will continue until the foreign aid requirement becomes nil at the end of the Second Five-Year Plan.

2. Here we are implicitly assuming that a 7% rate of growth in G.N.P. will continue to be the target and that the capital/ output ratio will not show any decline.

be needed during the Plan period but also the amount of annual gross investment requirements to achieve a 7% growth in G.N.P. per annum.

Table 50 of the Development Plan summarizes the yearly projections of G.N.P., consumption, investment and current account deficit. That table is reproduced here as Table 17, which serves as a hypothesis for our explanation of saving requirements of the Plan. According to the Plan, in order to raise the level of G.N.P. from 52,700 million T.L. in 1962 to 73,900 million T.L. in 1967, the amount of total investment must be raised from 8,600 million T.L. in 1962 to 14,300 million T.L. in 1967. In other words, the attainment of a 40% increase in G.N.P. during the Plan period requires a 60% increase in the amount of total investments. Consequently, while the G.N.P. would be increasing at an average rate of 7% p.a., investments would be increasing at an average rate of 10·7% p.a. The planning of a higher rate of increase in investment than in G.N.P. implies that the productivity of the additional investments would be declining. If the productivity of additional investments could be maintained constant, the total investment would then be required to increase at the same rate with G.N.P.

The declining productivity of the additional investments is reflected in the rising trend of incremental capital-output ratios shown in Table 18. It is not intended here to enter into the

TABLE 17

GROSS NATIONAL EXPENDITURE PROJECTIONS

(000 million T.L. at 1961 prices)

Years	G.N.P.	Private Consumption.	Current Public Expenditure	Private Investment	Public Investment	Current Account Deficit	Total Investment	Investment financed by Domestic Saving *
	I	II	III	IV	V	VI	VII	VIII
1962	52·7	= 38·6+	7·6+	3·5+	5·1-	2·1	8·6	6·5
1963	56·4	40·5	8·6	3·8	5·8	2·3	9·6	7·3
1964	60·3	43·0	9·0	4·2	6·6	2·5	10·8	8·3
1965	64·5	45·4	9·5	4·7	7·1	2·2	11·8	9·6
1966	69·0	47·6	10·5	5·3	7·8	2·2	13·1	11·9
1967	73·9	50·2	11·5	5·9	8·4	2·1	14·3	12·2
Average Annual Increase (%)								
	7·0	5·4	8·7	11·0	10·6	-	10·7	13·4

Source: S.P.O., Development Plan, 1963-1967, Table 50, p. 116.

* This column does not exist in Table 50 of the Plan.

discussion of the feasibility of these ratios but to make some

remarks only.   In Chapter 1 the incremental capital-output ratio

during the pre-Plan decade or so has been calculated as 2·8[1], which

is higher than that envisaged by the Plan to prevail in the Plan period,

1. See Chapter 1, p. 47

TABLE 18

CUMULATIVE NATURE OF SAVING REQUIREMENTS

Years	G.N.P. (000 million T.L.)	Implied Capital-Output Ratio	Percentage of G.N.P.			Marginal Rate of Saving
			Total Investment = total saving	Foreign Saving	Domestic Saving (A.P.S.)	
	I	II	III	IV	V	VI
1962	52·7	2·33	16·3	4·0	12·3	-
1963	56·4	2·43	17·0	4·1	12·9	·23
1964	60·3	2·56	17·9	4·1	13·8	·253
1965	64·5	2·61	18·3	3·4	14·9	·30
1966	69·0	2·71	19·0	3·2	15·8	·294
1967	73·9	2·77	19·4	2·8	16·6	·255
Average		2·59	18·1	3·3	14·8	·27

Source: calculated on the basis of data given in
Table 17 on page 79.

that is, 2·6.   However, the bottlenecks and shortages caused by

the balance of payments difficulties and the direction of invest-

ments to socially unproductive ventures by inflation, particularly

since 1954, may be considered to have made for a relatively high

capital-output ratio during the 1950's.   The Plan envisages, in

addition to avoiding the bottlenecks and shortages and the infla-

tionary policy, to make use of such existing potential sources of savings as underemployment of labour and capital that tend to lower the incremental capital-output ratio[1]. As the potential sources of savings are gradually exhausted and the capital intensity of the whole economy gradually grows with the intensification of capital formation, it is very likely that the productivity of additional investments will diminish over the plan period.

As the incremental capital-output ratio (v) increases over the Plan period, the maintenance of a constant rate of growth ($\triangle$ Y/Y), that is, 7% p.a., would require that a growing proportion of G.N.P. is invested each year. Table 18 shows that, with the incremental capital-output ratios as given in Column II, the increase of G.N.P. as envisaged in the Plan from 52,700 million T.L. in 1962 to 60,300 million T.L. in 1964 and to 73,900 million T.L. in 1967 would require the proportion of G.N.P. invested to be raised from 16·3% in 1962 to 17·9% in 1964 and to 19·4% in 1967. The proportion of G.N.P. saved must of course be equal to that

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1. The Turkish First Five-Year plan has faced a remarkable para-doxical situation in which underemployment of labour and under-utilization of scarce factor "capital" have been existing simultaneously in the economy. The extent of the underemploy-ment has already been pointed out in Chapter 1, p.5. To give some examples of the underutilization of capital, in 1960 the percentage capacity utilization in the woollen industry was 32 for yarn and 10 for fabric, about 60 in the rubber industry, and 40 in the structural steel industry (S.P.O., Development Plan 1963-1967, p. 245, 252, and 293).

invested if the investment/income ratio of the Plan is to be realized, since real investments can be financed only with real savings.

The cumulative nature of total savings requirements, as percentage of G.N.P. , of the plan is reflected as enhanced in domestic savings ratios of the Plan as shown in Column IV of Table 18.   This is due to the fact that the foreign component of the total savings/income ratio is planned to decline over the Plan period.   Consequently, while the total savings/income ratio by 1967 is required to be 19% above its 1962 level, the increase in the domestic savings/income ratio is expected to be 35% during the same period.   This entails the requirement of a greater rate of increase in domestic savings than in total savings as shown in Table 17 -- 13.4% p.a. versus 10.7% p.a., on average.

The planning of a 13.4% rate of increase in domestic savings against a 7% rate of growth of G.N.P. implies that the Plan expects an income elasticity of 1.9 to be realized in relation to domestic savings.   This high income-elasticity of savings is expected to be realized by holding the rate of growth

of aggregate consumption at 5·9% p.a.[1]   In other words, the
proportion of the incremental G.N.P. saved is envisaged to be
bigger than that of the aggregate G.N.P. saved during the Plan
period.   This is shown by the last two columns of Table 18 which
give the marginal and average rates of savings as implied by the
Plan.

In the past, the domestic saving/income ratio has neither
reached the average ratio envisaged by the Plan nor attained a
cumulative nature except during 1951-55.   Table 19 below shows the
trend of total savings, domestic savings and foreign savings, as
percentages of G.N.P., during the period 1950-62.   In spite of its
deficiencies, Table 19 enables us to have an idea of the trend of
savings in the Turkish economy.   As seen from the table the ratio
of total saving has shown a rising trend throughout the period
1950-62.   While the average rate of total saving was 11·5% of
G.N.P. in the period 1950-53, it attained an average rate of 14·4%

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1.   This is calculated as compound rate of growth of aggregate
     consumption (private plus public) given in Columns II and III
     of Table 17 above.   The rate of growth of private consumption
     is planned to be even lower, that is, 5·4% p.a.   Recalling
     our estimate of the rate of growth of private consumption during
     1950/52 - 1960/62 in page 49 , which has shown that the rate of
     growth in private consumption had been greater than that in
     G.N.P., it is readily seen that the Plan calls forth a substan-
     tial change in the saving behaviour of the Turkish people.

of G.N.P. for the 1950-62 period.   The rising trend becomes more
conspicuous as the 1959-62 average reaches 15·5% against the 13·9%
of 1954-58 and 11·5% of 1950-53.   When we look at the foreign
component of the total saving, we at first glance notice that the
foreign saving ratio had kept rather a high level until the mid-
fifties and then sharply declined, rising again by the end of the
fifties.   It is significant that the period with low level of
foreign assistance, that is, the 1956-58 period, is also the period
in which the level of total savings has somewhat declined after the
high level of the year 1955, recovering again in 1959.   We cannot,
however, explain the rising trend of the total saving ratio by
relying merely on the trend of foreign saving ratio, since the
average rate of foreign savings has shown a decline from 2·6% of
G.N.P. in 1950-53 to 2·4% in 1950-62.   The high average rate of
total savings in 1950-62 as compared with that in 1950-53 can be
explained with the increase in the domestic saving ratio as it
averaged to 12% in 1950-62 but was only 8·9% of G.N.P. in 1950-53.
Nevertheless, the foreign component of the total saving, which
has stood at 3·1% of G.N.P. in 1959-62 and reached the record level
of 4·1% in 1962, has been the main factor accounting for the rising
trend of the total saving ratio during the final quarter of the
period 1950-62 as the domestic saving ratio has almost stagnated
since 1955.

TABLE 19

TOTAL, DOMESTIC AND FOREIGN SAVINGS IN THE
TURKISH ECONOMY, 1950-62. (As % of G.N.P.)

Year	Total Saving	Foreign Saving	Domestic Saving	Average rates of Savings		
				Total	Foreign	Domestic
1950	9·6	1·3	8·3			
1951	10·2	2·1	8·1	11·5	2·6	8·9
1952	12·8	3·8	9·0			
1953	12·4	2·7	9·7			
1954	14·7	2·9	11·8			
1955	15·0	2·5	12·5			
1956	13·4	0·9	12·5	13·9	1·4	12·5
1957	13·1	0·7	12·4			
1958	14·0	1·0	13·0			
1959	15·7	3·1	12·6			
1960	15·9	2·4	13·5			
1961	15·2	2·8	12·4	15·5	3·1	12·4
1962	15·6	4·1	11·5			
Average	14·4	2·4	12·0			

Source: See note about the preparation and shortcomings
of the Table.

Note on Table 19:-

Preparation of the Table: Table 19 was prepared on
the basis of figures given in Table 13 in Chapter 1.
Table 13 gives the figures for G.N.P., total invest-
ment and current account deficit at current prices
for the period 1950-62. From these figures, we have
calculated the total saving ratios and foreign saving
ratios of Table 19 as equal to the rate of capital

Note on Table 19 (contd.).

Preparation of the Table (contd.):-

formation and to the ratio of the current account
deficit to the G.N.P., respectively.   Domestic saving
ratios are the residual of the total saving ratios minus
the foreign saving ratios.   The average rates for each
category of savings have been arrived at by relating the
total of that category saving in a particular period to
the total of (G.N.P.)s in that period.

Shortcomings of the Table:-

1. The table gives us the gross saving as equal to the
    gross capital formation.   The inclusion of depre-
    ciation charges in the saving figures makes them less
    representative of the net saving behaviour of the
    economy since the decisions with respect to the
    depreciation charges reflect the composition of the
    existing real capital rather than the current saving
    behaviour.   It is very much likely that the ratio of
    net to gross saving has not been constant over the
    period 1950-62 as the composition of fixed assets has
    changed.   In fact, while the ratio of gross invest-
    ments in machinery and equipment to that in construc-
    tion was 2/3 in 1950-52, it fell to 1/2 in 1958-60.
    Accordingly, the rate of depreciation has gone up from
    3·8% of G.N.P. in 1950-52 to 4·2% in 1958-60[1,2].   That
    the rate of depreciation allowances in 1962-65 is, on
    average, 4·4% of G.N.P.[3] must be taken into account in
    a comparison of the net saving behaviour of the plan
    period with that of the past if it is made in terms of
    the gross saving figures.

2. The rates of saving in Table 19 correspond to the
    rates of fixed capital formation and do not cover
    those savings used in financing the changes in stocks.
    In view of the fact that investment in inventories has
    probably been considerably higher during the brisk
    activity years - the inflationary period - of 1953-58
    than the periods 1950-52 and 1958-62, the above rates
    somewhat underestimate the actual rates of saving in
    the sub-period 1953-58, relatively speaking.

1. These calculations were made on the basis of figures given in
   Tables 6 & 9 of the S.P.O., "Development Plan, 1963-67".

DIAGRAM 4

TOTAL, DOMESTIC, AND FOREIGN SAVINGS IN THE
TURKISH ECONOMY, 1950-62.
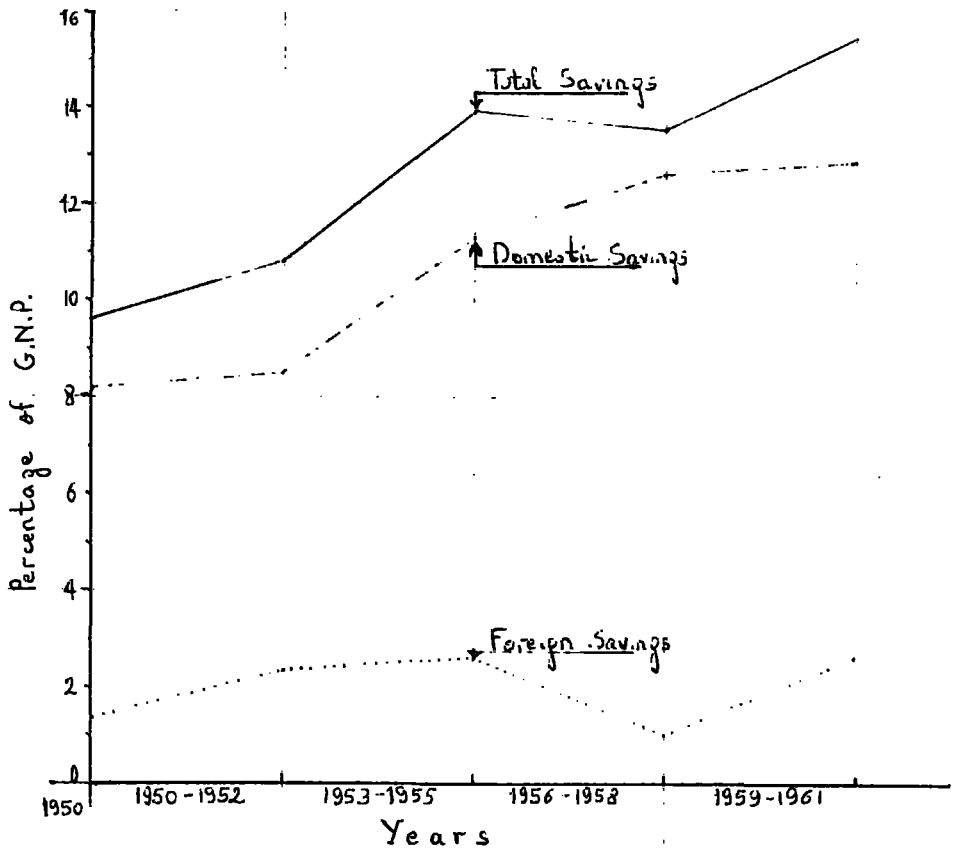
Source: Table 19 on page 85.

(Footnotes contd. from page 86).

2.   The average rate of depreciation in the Turkish economy for the
     period 1950-59 is shown as 4% of gross domestic product in the
     U.N.'s publication, "World Economic Survey, 1960", pp. 61.

3.   This was calculated on the basis of Tables 17 & 2 in the Annual
     Programmes for 1963 and 1965, respectively.

The ratio of domestic saving to the G.N.P. in 1955 was 50%
above the 1950 ratio.   This means that the Turkish public increased
its average propensity to save out of gross national product by 50%
in a six year period.   This is well above the target envisaged by
the Plan with respect to the increase in the domestic saving ratio,
i.e., 35% increase in the period 1962-67.   But, it is undoubtedly
more difficult to achieve a given percentage increase in the
domestic saving ratio when it is already high than when it is low.
In fact, while the 50% increase in the ratio of domestic saving to
G.N.P. in 1950-55 was attained with a marginal propensity to save
of 24·5%[1], the 35% increase in the domestic savings/income ratio
during the Plan period would require a marginal propensity to save
of 27% (see Table 18).

Since 1955 the rate of domestic savings remained around
12·5%.   The average ratio of domestic savings to G.N.P. in 1961-62
was slightly lower than that in 1955-56, though the level of G.N.P.
increased by 25% in the same period.   This means that the Turkish
public increased its consumption at the same pace with the national
income during 1955/56 - 1961/62.

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1.   This was calculated on the basis of the following data given in
     Table 7 of Chapter 1 and Table 19 of this chapter: the index
     of G.N.P. in 1955 was 135, the base year being 1950;   the domes-
     tic savings/income ratio was 8·3% in 1950 and 12·5% in 1955.
     The implicit assumption behind this calculation is that the
     savings/income ratio at current prices corresponds to that at
     constant prices, neglecting the likelihood of changes in
     relative prices.

The stagnation in the domestic saving ratio can better be observed from the last column of Table 19 in which the rates of domestic saving are shown as averages of the three sub-periods, that is, 1950-53, 1954-58 and 1958-62. These periods are marked by the contrasts in the general economic conditions which prevailed in each of them as already explained in Chapter 1. During the stable growth years from 1950 until 1954 the domestic saving ratio, after a pause in 1951, steadily increased and attained an average rate of about 9% of G.N.P. During the inflationary years from 1954 until the mid-1958, it first went up in 1954 and 1955 and then stagnated, giving an average of 12.5% of G.N.P. which is considerably higher than the average rate of the period 1950-53. In the stabilization years from the mid-1958 until the beginning of the plan period, the domestic saving ratio followed a very unsteady path, and, on average, remained slightly below the average rate of the period 1954-58.

The above review of savings in relation to the national income manifests that the realization of the Plan's Targets is dependent upon the taking place of substantial changes in the saving behaviour of the economy. In the following chapters, we shall study in detail the effectiveness of the measures taken to increase savings.

III

The Development Plan foresees no significant transfers of savings in either direction between the public and private sectors[1]. Therefore, the savings problems of the two sectors can be treated separately. In the private sector the proportion of private investment financed by foreign capital was assumed to remain unchanged through the Plan period[2]. Private savings are therefore expected to grow proportionately with private investment[3]. This means that private savings are envisaged to increase at the rate of 11% p.a., which is the target rate of increase of private investment as shown in Table 17 above. In the public sector, total public savings should increase at a greater pace than public investment so that a reduction in dependence on foreign aid as foreseen by the Plan could be achieved.

The Plan does not specify particular targets for savings of the private and public sectors. There are some serious problems which make it impossible to allocate the Plan's estimate of domestic

1. I.B.R.D., Development Performance and Prospects of Turkey, mimeographed report, No. EA-153a, November 1965, paragraph 376.
2. Ibid.
3. This is sometimes misinterpreted as if the Plan foresaw an equality between private savings and investment. For instance, O.E.C.D., Turkey 1962/63, makes this mistake in pages 16 and 17, and in Table 16.

saving requirements between the public and private sectors[1]. The requirements of the Plan with respect to savings of the public and private sectors from domestic sources could have been estimated from investment targets had we had the data on the proposed allocation of foreign aid between the two sectors and on the transfer of savings between them.

The Plan gives projections about the public revenue and expenditure during the Plan period. The difference between the public revenue and public current expenditure is to be equal to the public savings. But this method also is rendered inaccurate by the following factors. First, there are inconsistencies in the data on the public revenue and current expenditure estimates which are given in Tables 50, 51, 52 and 53 of the Plan. Secondly, at the time the Plan was prepared Central Government expenditures were classified under the heads of only current and investment. This means that both headings contained important financial transfers such as internal and external debt servicing, allocations to the S.E.E. and grants to municipal and local governments.

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1. The I.B.R.D. mission to Turkey in 1965 found itself unable to obtain a breakdown of the Plan's saving requirements between the two sectors. (I.B.R.D., op.cit., paragraph 376 and 377).

Although an accurate breakdown of the domestic saving

estimate of the Plan between the public and private sectors is not

possible, Table 20 below may be useful to observe, even if roughly,

the relative order of the public and private savings from domestic

sources as foreseen by the Plan.   Savings of the private sector in

the table are calculated as residuals of total domestic savings

less savings of the public sector.   The Plan expects savings of

the Private sector to grow at the same rate with the private

investment[1], that is, 11% p.a.   But the corresponding rate in

TABLE 20

TARGETS FOR THE PUBLIC AND PRIVATE SAVINGS IN THE PLAN,
1963-67.   (At 1961 prices, 000 million T.L.)

Years	Total Domestic Saving	Public Revenue	Public Current Expenditure	Public Saving	Private Sector Saving	Percentage of G.N.P.	
						Public Saving	Private Saving
1962	6·5	11·02	7·96	3·06	2·90	5·8	5·5
1963	7·3	13·46	9·07	4·39	2·91	7·8	5·1
1964	8·3	14·38	9·35	5·03	3·27	8·4	5·4
1965	9·6	15·72	10·01	5·71	3·89	8·8	6·0
1966	10·9	17·31	11·00	6·31	4·59	9·2	6·6
1967	12·2	18·91	11·90	7·01	5·19	9·5	7·0

Sources: S.P.O., "First Five-Year Development Plan,
1963-1967", Tables 50, 52 and 53.

1. S.P.O., Development Plan 1963-1967, p.456.

Table 20 is 12·3%.   This shows that the breakdown of domestic saving estimates of the Plan between the public and private sectors as revealed in Table 20 is not exactly what the Plan aims at.   As percentages of G.N.P., the public and private savings are expected to be about of the same order in 1962, but thereafter public savings are getting larger.

As for the public savings, the Plan specifies the targets for the public revenues and expenditures for each year of the plan period, which have already been shown in Table 20.   In this dissertation we shall not deal with the saving of the local administrations because of the lack of adequate information about their revenues and expenditures, on the one hand, and of their relatively small share in the total savings, on the other hand.   The revenues by sources and current expenditures of the central Government[1], as foreseen by the Plan, are shown in Table 21.   The difficulties and possibilities with respect to the attainment of these targets will be discussed in detail in Chapters 5 and 6.   We shall here confine ourselves to some overall remarks.   As seen from the table, the major part, i.e., around three quarters, of the total government revenue is to come from taxation.   The share of the tax revenue in

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1. All revenues and expenditures of the central government are
    included in the General and Annex Budgets.   From now on the
    word "government" will refer to the central government and
    will not include local administrations.

the total revenue is planned to remain almost unchanged during the
1963-67 period.   But the share of the tax revenue in G.N.P.,
parallel to the share of the total government revenue in G.N.P.,
is proposed to increase from 14·61% in 1962 to 17·32% in 1967.
This requires an average rate of increase of 10·8% per annum
against a 7% target rate of growth in G.N.P.   In other words,
the income elasticity of the tax system during the plan period is
envisaged to be 1·5.

During the period 1950-62 the government's share in G.N.P.
was, on average, about 14% against about 22% of G.N.P. which is
envisaged by the Plan.   Thus, the average share of government
revenues in G.N.P. during 1963-1967 is expected to record an
increase of more than 50% over the 1950-62 average (or over the
1959-62 average, see Table 22).   The tax system, providing the
largest part of the public revenue, stands as the main instrument
for the attainment of this increase.   In fact, the Plan proposes
many reforms in the tax system, which will be studied in Chapter 5,
in order to gain the control of an increasing share of G.N.P.
According to the Plan, the share of the tax revenue in G.N.P.
will, on average, be 17% during the period 1963-67, which is more
than 40% above the 1959-62 average.   The scope of the required
reforms in the tax system will be more conspicuous when we notice
that the share of the tax revenue in G.N.P. during the 1950-58

period stagnated at 11% and, after the 1958 devaluation, reached only 12% in 1959-62.   This points out the fact that during most of the fifties the income elasticity of the Turkish tax system had been around unity and only in 1959-62 was slightly greater than unity against the Plan's proposal of an income elasticity equal to 1·5.

Although the share of tax revenue in G.N.P. has almost stagnated in the 1950-62 period, the proportion of the government revenue coming from taxation has grown from 73% in 1950-53 to 85% in 1959-62. This was due to the failure of the public revenues other than taxes to keep pace with the growth in G.N.P.   In fact, while the Turkish government had been appropriating 15% of G.N.P. through the General and Annexed Budget revenues in the period 1950-53, this proportion fell to 13·4% in 1954-58 and then slightly rose to 14·1% in 1959-62. In order to reduce the share of tax revenue in the total revenue from 85% in 1959-62 to about 75% in the plan period, the public revenues other than taxes must increase at a greater rate than the tax revenue.   The tax revenue index is envisaged to reach 166 in 1967 while the index for other revenues is expected to hit 213 in 1967, the base year for these indexes being 1962.

The public revenues other than taxes are composed mainly of the surplus funds of the state economic enterprises (S.E.E.), fees

TABLE 21 - TARGETS FOR THE PUBLIC REVENUES, CURRENT EXPENDITURE & SAVING IN THE PLAN, 1962-67.
(General & Annexed Budgets).   (000 million T.L. at 1961 prices).

Years	Tax Revenue	Other Public Revenues	Saving Bonds	Surplus Funds of the S.E.E.	Funds From Unidentified Sources	Total Public Revenue	Total Public Current Expenditure	Public Saving	Percentages of G.N.P.		
									Tax Revenue	Total Public Revenue	Total Public Current Expenditure
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI
1962	7·70	0·93	0·50	0·55	–	9·68	7·00	2·68	14·61	18·36	13·30
1963	9·00	0·98	0·53	0·67	0·84	12·02	8·10	3·82	15·95	21·34	14·36
1964	10·10	1·03	0·57	0·96	0·18	12·84	8·30	4·54	16·74	21·30	13·76
1965	10·92	1·08	0·61	1·01	0·45	14·07	8·86	5·21	16·93	21·82	13·74
1966	11·80	1·13	0·65	1·08	0·89	15·55	9·75	5·80	17·10	22·54	14·13
1967	12·80	1·19	0·70	1·23	1·11	17·03	10·50	6·53	17·32	23·04	14·21

Sources: The S.P.O., First Five-Year Development Plan 1963-1967.   Columns I to VI are from Table 53, excluding revenues from counterpart funds and from Local Administrations; Column VII from Table 52 excluding current expenditures of the Local Administrations. Column VIII is the difference between Columns VI and VII.   G.N.P. figures used in the calculations in columns IX to XI are from Table 50.

TABLE 22 - SOME INDICATORS OF THE DEVELOPMENT OF REVENUE, CURRENT EXPENDITURE & SAVING IN THE GENERAL AND ANNEXED BUDGETS.

Year	Tax Revenue		Percentages of G.N.P.			Average Propensity to save of the Government
	% of G.N.P.	% of Total Revenue	Total Revenue	Total Current Expenditure	Total Public Saving	
1950-53	11·0	73	15·0	13·2	1·8	12
1954-58	11·2	84	13·4	10·6	2·8	21
1959-62	12·0	85	14·1	10·9	3·2	23
1963-67	16·8	76	22·0	14·0	8·0	36

Sources: 1. The S.P.O., First Five-Year Development Plan 1963-1967.
2. The Ministry of Finance, Budget Revenues Bulletin, No. 14, pp. 14 and 15.
3. The S.P.O., A Summary of the Progress Report on the Implementation of the 1963 Annual Program, p. 32.

Note on the Preparation of Table: G.N.P. figures were taken from Table 6 of the Plan;   The tax revenue figures for 1950-61 from Table 12, the current expenditure figures for 1950-1961 from Table 13 of the Plan.   The total revenue figures were taken from Table 12 of the Plan with the additions of Petroleum Import Treasury share from 1957 on and Saving Bonds from 1961 on, which were taken from the Revenue Bulletin.   These additions were made in order to make the total revenue figures of Table 22 comparable with those of Table 21 which appears to have included these two items.   Tax revenue figures and Total Revenue figures for 1962 were taken from the Revenue Bulletin.   Total current expenditure figures for 1962 were from the Source No. 3 above.   For 1963-67 figures, which are the estimates of the Plan, see Table 21 of the present chapter.

collected by agencies included in the Annexed Budget, the revenue

on state property which is not in the nature of taxes and revenue

from savings bonds.   The fees collected by the annexed budget

agencies and the revenue on state property have increased at an

average rate of 5% per annum in the past[1] and are expected to

continue increasing at the same rate during the plan period also.

Savings bonds were first issued in 1961 and, therefore, the revenue

from them could not be estimated on the basis of past trends.   It

has been assumed that a 7% annual increase, similar to the rate of

growth, could be obtained in the revenue from this source.   Among

the public revenues other than taxes, the surplus funds of the

S.E.E. are expected to attain the highest rate of increase,

reaching an index of 244 in 1967 if the surplus funds in 1962 is

taken as 100.

In order to gain a complete perspective of the Plan's

strategy with respect to the public savings we have to consider

public current expenditures as well, since the public saving is

the surplus of the public revenue over the public current expenditure.

Table 21 shows the estimates by the Plan of the current public expen-

ditures both as absolute amounts and as percentages of G.N.P.   The

1. S.P.O., Development Plan, p. 123.

total of current expenditures from the General and Annexed Budgets
is expected to increase by 50% in 1967 compared with 1962, growing
at a rate just above 8% per annum.   This would result in increasing
the share of total public current expenditures in G.N.P. from, on
average, about 11% in 1959-62 to 14% in the plan period.

The plan envisages that the ratio of total public savings
out of the General and Annexed Budgets to G.N.P. will increase, on
average, from 3·2% in 1959-62 to 8% in 1963-67, recording a 150%
increase.   This could be achieved with an increase in the average
propensity to save of the government from ·23 in 1959-62 to ·36 in
1963-67.   Taking into account that in the pre-plan period the
total public saving ratio has increased only by 77% in a decade or
so -- from 1·8% of G.N.P. in 1950-53 to 3·2% in 1959-62 -- the
degree of the effort and skill required from the fiscal authorities
in order to realize the financial targets of the plan should no
doubt be regarded as quite difficult to achieve.

IV

The chapter on financing in Section IX of the Plan starts
with an introduction of the principles which would govern the
financing of the Plan.   These principles are as follows:-
    a. "Non-inflationary financing.
    Investments will be financed from real savings and deficit

financing will not be resorted to during the Plan period. There will be equality between annual saving and annual investments".

    b. "Physical Equilibrium in Financing.

The volume and pattern of savings was determined in the light of the physical resources required for the realization of the proposed investments. Consideration was further given to the action to be taken in order to prevent the emergence of bottlenecks due to the likely demand for these physical resources during the Plan period".

    c. "Monetary equilibrium between total volume of savings and financing needs".

Although enumerated as three separate principles, they in effect emerge as a single principle: non-inflationary financing. However, it seems that the Plan does not have a clear-cut view on the relationship between deficit financing and inflation.

Inflation is generated at three points of the economy. This may be expressed through a formula as this[1]:-

$$(X-M) + (I-S) + (G-R) = 0$$

where X stands for exports; M for imports; I and S for investment.

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1. UNITED NATIONS, E.C.A.F.E., Economic Bulletin for Asia and the Far East, Vol. III, Nos. 1-2, p. 5.

and savings respectively, of the private sector; G and R for
expenditure and revenue respectively, of the public sector.   One
cannot argue that the inflationary pressure exists simply by
looking at, say, the budget alone but at the three points simul-
taneously.   X, M, G, R may be known in advance.   I is known with
greater or lesser accuracy after it has taken place, whereas, from
the policy point of view, it ought to be known in advance.   S is
not known at all because S represents the total which people expect
to save.

Considering that $G = I_g + E$ and $R - E = S_g$, where I_g
and S_g denote the public sector's investment and savings, respectively,
and E public consumption (current expenditure), the public sector's
budget (G-R) may be stated as $I_g - S_g$.   Thus, the above formula
becomes as follows:-

$$(X-M) + (I_p - S_p) + (I_g - S_g) = 0 \text{ , where } p \text{ and } g$$

indicate the private and public sectors, respectively.

The three sectors of the economy, namely, the foreign trade,
the private and public sectors, may individually show an excess or
deficit.   But as long as they cancel each other in total, no infla-
tionary or deflationary pressures would develop in the economy.
Putting it differently, a non-inflationary financing of economic
development in a country requires that the excess of the total

(public plus private) expected investment over the total expected

savings must not be larger than the expected current account

deficit[1].

The first of the above-mentioned three principles of

financing of the Plan states that there will be equality between

annual savings and annual investments. Since, in the national

income accounting, realized savings/are always equal to realized invest-

ments, it is reasonable to assume that the Plan aims at an equality

between expected savings and investments.

The other two principles seem rather to be connected with

the realization of expected investments. The emergence of bottle-

necks and the failure of the monetary and fiscal institutions to

provide funds for investment to the extent of expected savings

would cause investors to alter their investment plans, thus leading

to a discrepancy between expected savings and investments.

The inclusion in the first principle of the clause that

deficit financing will not be resorted to during the Plan period

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1. See, R. F. Harrod, Economic Planning and Capital Investment, in
   Capital Formation, op.cit., p. 313; H. W. Singer, "Deficit
   Financing of Public Capital Formation", Social and Economic
   Studies, Vol. VII, No. 3, pp. 85-96. UNITED NATIONS, "Some
   Financial Aspects of Development Programmes in Asian Countries",
   Economic Bulletin for Asia and the Far East, Vol. III, Nos. 1-2,
   p. 5.

suggests that the Plan considers deficit financing as always inflationary. As a matter of fact, deficit financing in the public or private or in the both sectors may take place without resulting in inflation, provided that the ex-ante equilibrium condition is fulfilled and that bottlenecks do not emerge in the supply of goods and services and of investible funds.

Whether the method of deficit financing always leads to inflation and whether some justification may exist for the use of deficit financing in the public sector will be studied in detail in Chapter 6.

CHAPTER 4

SAVINGS OF THE PRIVATE SECTOR

It has been shown in the last chapter that the Plan's
strategy for domestic financing envisages that a considerable
part of total saving requirements will be met by the private
sector.   It is therefore of the utmost importance to examine
carefully the saving behaviour of the private sector and to
search for methods of increasing and mobilizing private savings.
Accordingly, in the first section of the present chapter, an
estimate of the rate of private savings will be made, and this
rate will be compared with those in the advanced and under-
developed countries.   Section II will survey the factors
accounting for the low rate of private savings in Turkey rela-
tive to the advanced countries.   Finally, in section III, we
shall have a look at the financial assets which are available
as saving means to the private sector.

I

ESTIMATE OF THE PRIVATE SAVINGS

Domestic savings originate at three levels: households,
businesses, and government.   In this chapter we shall be con-
cerned in savings arising from the first two sources.   It is
desirable to estimate savings through their sectoral forms as

this would provide a deeper insight for the policy measures. Unfortunately, no work has hitherto been done in this field in Turkey. Although Dr. Oktay Yenal of the University of Istanbul, has come out with an estimation of sectoral savings on the basis of his investigation of the development of a capital market in Turkey, his underlying assumptions are too arbitrary to deduce the saving behaviour by sectors of the economy.[1]

Estimates of savings through their sectoral forms could be derived from such data as income tax returns, balance sheets of

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1. Dr. Yenal has divided the economy into six sectors particularly from the viewpoint of investments. These are Agriculture, Households, Businesses, Public, Commercial Banks and the Cental Bank. The Public Sector makes all the public investments and receives all the credit classified as official credit. The Agricultural sector makes all the investments in rural housing and in other agricultural buildings and receives all the credit classified as agricultural credit. The Business Sector undertakes all the investment in industrial and commercial construction and machinery and equipment and receives all the industrial and commercial credits. The household sector invests in urban housing and receives all housing credit from the financial institutions. All saving deposits have been assumed as coming from the household sector, all commercial deposits from the business sector, and official deposits from the Public sector. Further, all the increases in the currency have been assumed as being held by the household sector. Under these assumptions, he estimated sectoral savings as a residual of the sector's investment plus increase in financial assets (deposits, and currency as well in the case of household sector) minus increase in financial liabilities (credit). He used the investment figures of the "Report About the Project Studies on the Correction and Integration of Investment figures" submitted to the S.P.O. by Dr. Kenan Gürtan, of the Istanbul University. Dr. Yenal's study covers the 1950-1960 period and was published in the "Necessary Measures for the development of Capital Market in Turkey" edited by the Committee conducting the seminar on Capital Market, Ankara 1964, pp. 7-38.

companies, changes in funds of financial institutions, and consumer expenditure[1]. These statistics either are not available in Turkey or are available in such forms that they could not be of much use to a study of savings. It is therefore attempted here to estimate private savings as a whole without any regard to the division of it between households and businesses.

Savings of an economic unit, whether a household, a firm, a sector or a whole economy, can be calculated either from its income account by subtracting current expenditures from current income or through its balance sheet by subtracting changes in liabilities from changes in assets. The former approach will be used here in estimating the saving of private sector in Turkey[2]. In Table 23 the private current income (disposable income) for

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1. For the use of such data in the estimation of savings in a country with advanced statistics, see, for instance, R. W. Goldsmith, A Study of Savings in the U.S., Princeton 1955; and Bank of Japan & Rissho University, "Savings in the Economic Growth of Postwar Japan" in the U.N., Econ. Bull. for Asia & the F. East, September 1960, pp. 1-43. On the other hand, Saving of the Federation of Malaya, 1954-1958 in the U.N., Econ. Bull. for Asia & the F. East, June 1962, pp. 17-34, constitutes an example of the limited use of those data as supplemented by some presumptive methods.

2. This approach has been used by B. Hansen in studying income-consumption behaviour of the private sector in his report to the S.P.O., "Some Comments on the 1965 Program and the Policy Problems 1964 and 1965", Sept. 1964, mimeographed, pp. 7-9. His work covered 1963-1965, of which only for 1963 he had the figures of actual outcome, while Table 23 in this work is based on the figures for actual outcome of the years 1962-1964.

1962-1964 is calculated as the difference between the G.N.P. at
current prices and net income transfers to the Public Sector.
The latter is computed as total taxes and government revenue
proper minus income transfers from the General and Annexed Budgets
to the private sector and the government interest payments abroad.
The reason for the deduction of the interest payments is that these
payments have been deducted from G.D.P. to reach G.N.P., while
obviously they do not reduce domestic private income.   The private
saving in the table is the retained income found as the difference
between the private disposable income and private consumption.   The
figures on private consumption as such are not available.   Although
the Annual Programmes have the tables of balance of resources, they
include the private consumption into the residual item called "Other
Expenditures" which is defined as private consumption plus stock
changes in the public and private sectors minus capital and income
transfers from the General and Annexed Budgets[1].   Consequently, we
also have to estimate private consumption.   This is done for 1962-
1964 in Table 24 in which private consumption is estimated as a
residual[2].

1.   S.P.O., 1965 Annual Programme, Ankara 1964, pp. 12.

2.   In both Table 23 and Table 24, recourse has been had to a good
     many sources for statistical data.   But the heterogeneity in
     sources has been avoided by confining ourselves to the S.P.O.
     figures.   O.E.C.D. and Hansen rely on the S.P.O. figures.
     The tax figures are undisputed.   Only for the government interest
     payments abroad in 1964 and 1965 has recourse been had to the
     State Institute of Statistics, whose figures in almost every field
     differ from those of the S.P.O.

TABLE 23

ESTIMATES OF PRIVATE SAVINGS, 1962-1964

(000 million T.L. at current prices)

	1962	1963	1964
G.N.P.	55·24	62·76	66·82
Taxes & Government Revenue Proper:			
General Budget:			
Direct Taxes	2·33	2·75	3·02
Indirect Taxes	5·52	6·95	7·50
Annexed Budget Revenue	0·36	0·39	0·40
Revolving Funds	0·12	0·24	0·21
S.E.E. Resources Proper	0·33	0·87	1·03
Local Administrations	1·27	1·22	1·47
Total Taxes & Government Revenue Proper	9·93	12·42	13·63
Minus Income Transfers from General & Annexed Budgets to Private Sector	0·30	0·56	0·73
Minus Government Interest Payments Abroad	0·24	0·24	0·24
Net Income Transfers to Public Sector	9·39	11·62	12·66
Private Disposable Income	45·85	51·14	54·16
Private Consumption	42·60	46·89	49·10
Private Saving	3·25	4·25	5·06
Ratios: (as percentages)			
$S_{Private}$/G.N.P.	5·9	6·7	7·4
$S_{Private}$/$Y_{Private}$ (APS)	7·1	8·3	9·3
$\triangle S_{Private}$/$\triangle Y_{Private}$ (MPS)	-	19·0	27·0

Note on the sources of Table 23.

        The G.N.P. figure for 1962 was taken from
O.E.C.D., Turkey, Paris 1964, p. 43; those for 1963-
65 were from S.P.O. A Summary of 1966 Annual Pro-
gramme, p. 64.

        For the sources of data about the General and
Annexed Budgets revenues see Table 35, and for the
S.E.E. Resources Table 37 of this essay. The data
for Revolving Funds and Local Administrations were
taken from S.P.O. A Summary of 1966 Annual
Programme, p. 70.

        I have been unable to trace the part of the
total transfers from the consolidated budget going
to the private sector. The figures of the income
transfers to the private sector for 1963 and 1964
were taken from Prof. Bent Hansen, op. cit., p. 8
Table 4, the 1963 figure being actual outcome and
1964 figure expected outcome. The 1962 figure
was estimated as follows: Transfers to local
authorities and private sector together in 1961-
1963 are shown in O.E.C.D., op. cit., p. 27.
Transfers to the local authorities in 1960-1963
are given in S.P.O., 1964 Annual Programme, p. 278,
Table 158. From these data, the income transfers
to the private sector in 1962 have been found to
be about 300 million T.L. The same estimation
for 1963 gives a figure corresponding to the
Hansen figure for 1963.

        The figures of government interest payments
abroad for 1962 and 1963 have been taken from
O.E.C.D., op. cit., p. 43, Table 1; and that for
1964 from the Budget Preamble for the 1966 Fiscal
Year, p. 54, Table 1, which quotes the State
Institute of Statistics.

        The basis of the estimation of private
consumption are explained in the note on Table 24.

TABLE   24

UTILIZATION OF RESOURCES IN 1962-1964.

(000 million T.L. at current prices)

	1962	1963	1964
G.N.P.	55·25	62·76	66·82
Foreign Deficit	2·18	2·70	0·95
Available Resources	57·43	65·46	67·77
Private Consumption	42·60	46·89	49·10
Public Current Expenditure	6·50	7·34	7·79
Public Fixed Investment	4·23	5·14	5·66
Private Fixed Investment	3·60	4·69	4·72
Stock Changes	0·50	1·40	0·50
Total Uses	57·43	65·46	67·77

Note on Table 24:-

The G.N.P. figures have been taken from Table 23 above.

The data on the current account deficit have been taken from O.E.C.D., Turkey 1965/66, p. 22, Table 8, where they are expressed in terms of U.S.$.   The conversion to the Turkish Lira in Table 24 has been made according to that per U.S.$ = T.L. 9.

The figures for Public Current Expenditures in 1964 has been taken from S.P.O., op. cit., pp. 69, Table 11, and the figure for that in 1962 has been arrived at by adding the current expenditures of the

Note on Table 24 (contd.):-

 local authorities given in S.P.O., 1965 Annual Programme,
pp. 310, Table 224, to the current expenditure from the
General and Annexed Budgets given in O.E.C.D., Turkey
1963/64, p. 27.

 For the sources of the data about the public invest-
ment, see Table 39 of this essay.

 The 1962 Private Investment figure was taken from
O.E.C.D., Turkey 1963/64, p. 38, Table 10.   The Private
Investment figures for 1963 and 1964 are arrived at
thus: 1963 and 1964 private investments can be calculated
as 4,400 million T.L. and 4,264 million T.L. at 1961
prices respectively from the data given in S.P.O., A
Summary of 1966 Annual Programme, pp. 48-49, Tables 5 and
6.   These figures can be converted to those at current
prices by means of a special price index for investment
goods which I have arranged according to the information
given in S.P.O., 1964 Annual Programme, p. 35;   1965
Annual Programme, p. 10;   A Summary of 1966 Annual Pro-
gramme, p. 2.   The index is this: 1961 = 100;   1962 =
104·4;   1963 = 106·7;   1964 = 110·7.

 There are no official data on stock changes in the
Turkish economy.   Those given in the table are the
estimates by B. Hansen in his report.

 As seen from Table 23, private savings have increased from

3,250 million T.L. in 1962 to 5,060 million T.L. in 1964.   Its

share in G.N.P. has gone up from 5·9% in 1962 to 7·4% in 1964.

The per capita private saving in real terms increased from 111 T.L.

in 1962 to 160 T.L. in 1964, i.e. a 44% increase during three years[1].

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1.   The saving figure for 1964 in Table 23 was deflated to 1962
constant prices according to the wholesale price index, given in
the Ministry of Finance, Budget Preamble for 1966 Fiscal Year,
p. 86, which is this: 1953 = 100;   1961 = 246;   1962 = 260;
1963 = 271;   1964 = 269;   1965 = 290.   The population of Turkey
has been estimated as 29·18 million in 1962 and 31·39 million in
1964 by means of interpolation of the results of the 1960 and
1965 population census.

The considerable increase in private savings reflects the fact that private consumption has increased at a much slower pace than private disposable income, i.e., 7·3% p.a. versus 8·6% p.a.[1]. The average propensity-to-save (A.P.S.) of the private sector rose from 7·1% in 1962 to 8·3% in 1963 and 9·3% in 1964. The increasing A.P.S. has been achieved through maintaining a marginal propensity-to-save (M.P.S.) well above the A.P.S. (see Table 23).

It is significant to note that the average as well as the marginal propensity-to-save in 1964 were higher than in 1963 in spite of the fact that G.N.P. in real terms grew by only 4·2% in 1964 against by 7·5% in 1963. This may be taken as an indicator that there is no immediate relationship between the rate of growth of national income and the saving behaviour of the private sector in the very short-run.

Despite the above-mentioned favourable developments, the rate of private saving in Turkey is still much lower than in the advanced countries and many underdeveloped countries. Although the statistical shortcomings lessen the accuracy of the comparison

---

1. The discrepancy between the average rate of growth of G.N.P. in money terms during 1962-1964, that is, about 10% p.a. and that of private disposable income, that is, 8·6% p.a., reflects the fact that net income transfers to Public Sector have increased at a greater rate than G.N.P. during that period.

TABLE 25

RATE OF GROSS PRIVATE SAVING IN SELECTED COUNTRIES[a]
(percentage of gross domestic product)

Advanced Countries	Gross Domestic Saving	Private Saving	Underdeveloped Countries	Gross Domestic Saving	Private[b] Saving
Australia	26·1	19·6	Burma	14	11
Japan	28·7	21·0	South Africa	14	10
Canada	22·5	18·2	Morocco	11	7
Netherlands	25·7	17·0	Brazil	10	7
United States	18·6	15·2	Ceylon	9	7
Belgium	17·6	17·3	Turkey	14	7·5
United Kingdom	15·2	11·5	India	7	6
			Spain	8	6
			Greece	4	3
			Portugal	6	3

a. The data refer to the averages for 1950-59, except for
Belgium and Turkey for which the data refer to the
averages for 1950-58 and 1962-64 respectively.

b. Public corporations included, except in Turkey.

Sources: For Turkey, G.D.P. figures have been calculated from
Table 23 as G.N.P. minus indirect taxes plus income
from rest of the world which equals to the government
interest payments abroad in the case of Turkey.
Private saving figures have been taken from Table 23.
Domestic saving figures have been calculated from
Table 24 as total capital formation minus foreign
deficit. With these information the ratios given
in the above table have been computed.

For other countries; U.N., World Economic Survey
1960, New York 1961, pp. 20 & 62.

provided by Table 25, it no doubt gives an idea about the relative

position of the countries with respect to the rate of private

saving.   The rate of private saving in Turkey compares favourably

with that in other underdeveloped countries[1].   But when compared

with the private saving ratios in advanced countries, the extent

of the task confronting the Turkish private sector in increasing

the share of its saving in G.D.P. can be envisaged better.   Indeed,

the plan projects that the share of the private sector in the

increasing total investment would grow bigger in the course of the

fifteen-year perspective plan and that the private savings would

grow at the same rate as the private investment.   This means that

not only the share of private savings in G.D.P. but that in total

domestic saving must also approach towards those observed in

advanced countries.   The share of the private sector in the total

domestic savings in Turkey is smaller than in all the countries

included in Table 25, except Portugal.   This might at first sight

give the impression that the efforts to maintain a large share of

domestic savings by the government must have been responsible for

1. It must be noted that the private saving ratios in the under-
    developed countries other than Turkey shown in the table include
    the saving of public enterprises.   In the advanced countries of
    the table, the level of saving of public enterprises, which is
    not included in the private saving, differs between 0·8% and
    1·5% of G.D.P.

the low rate of private saving.   This is, however, contradicted

by the fact that both public and private savings have increased

substantially in the period 1962-1965.

II

OBSTACLES TO A HIGHER RATE OF PRIVATE SAVINGS

The relatively low level of private saving in Turkey as

compared with advanced countries is usually explained by the low

level of per capita incomes in Turkey[1].   A generalization of what

might be correct for an individual when applied to a group may

lead to such an incorrect deduction.   Various studies have shown

that there is no systematic relationship between the proportion

of national income saved and the level of per capita national

income[2].   A similar argument can be put forward with respect to

the relationship between the private disposable income and the

rate of private saving.   As for the private corporate saving,

the fiscal policies of governments and dividend and depreciation

policies of corporations are as effective determinants of the

level of corporate saving as their current revenues[3].   Therefore,

the bigger the share of corporations in total private saving the

1. For example, K. Kurdaş, op. cit., p. 25; and B. Üstünel,
    op. cit., p. 16.

2. S. Kuznets, "International Differences in Capital Formation
    and Financing" in Six Lectures on Economic Growth, New York
    1955, pp.   ; and "Economic Growth and Income Inequality"
    in American Economic Review, March 1955; also, various U.N.
    publications referred to in this chapter.

3. U.N., World Economic Survey 1960, New York 1961, pp.

weaker the relation between private disposable income and private

saving.   No statistical data are available in relation to the

size of revenues and savings of the corporation sector in Turkey.   It

is, nevertheless, possible to have a rough idea of them by means of

some relevant indicators.   According to the Corporation Tax

statistics, the net revenue after direct taxes of the corporations

subject to the Corporation Tax was 2 per cent of G.N.P. and 2·5% of

the private disposable income in 1962[1].   Of this, however, only a

little more ·than $\frac{1}{4}$ was the net revenue after taxes of the Turkish

---

1.   These ratios have been calculated on the basis of the data
     given in Institut National de la Statistique, Annuaire
     Statistique 1960-62, Pub. No. 460, pp. 397-404, and Table 23
     of this essay.

     Turkish Corporations:-

     A total of 2,692 corporations declared a net
                                        revenue of   1,323 million T.L.
              121 S.E.E.,   "   "   "   -   348   "   "
                                                          977   "   "
     Corporation Tax   192   "   "

          Total   310 million T.L.
        - S.E.Es 128   "   "
                 192   "   "   -
                                                         785 million T.L.
     20% withholding Income Tax . . . .-   157   "   "
                                                          628   "   "
     1400 corporations declared a net loss of . .   386
     A total of 1,523 corporations 565 million T.L.
              123 S.E.E.   - 179   "   "
              1,400 corporations 386   "   " -
     Net Revenue after·Taxes . . . .   242 million T.L.

corporations and the remaining belonged to the foreign corporations[1].

Dr. İbrahim Öngüt has estimated that the ratio of undistributed

profits to total profits after taxes in Turkish corporate enter-

prises has increased from 44% in 1952 to 71% in 1960[2].   Assuming

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1. In order not to cause an exaggerated impression of the role of
    private foreign capital in the Turkish economy the following
    clarification seems to be helpful: The Corporation Tax
    classifies the corporations into two groups: those which are
    subject to the tax with their whole income, and those which have
    their headquarters abroad and which are subject to the tax with
    their earnings in Turkey.   It is these latter corporations
    that have been considered foreign corporations in this text.
    According to a recent survey made by the S.P.O. about the
    private foreign investment in Turkey, private foreign capital
    uses domestic credit facilities and colloborates with domestic
    capital to such an extent that it practically loses its foreign
    character, though maintains its status of foreign corporation.
    For example, the foreign corporations included in the survey
    altogether have brought in a foreign capital of 271 million T.L.
    but they obtained the collaboration of 468 million T.L. domestic
    capital; 38 of them have altogether obtained a total domestic
    credit equal to 116% of their total capital.

2. Dr. İ. Öngüt, "The Development of a Capital Market in Turkey"
    in Capital Formation...., op. cit., pp. 142.   He only mentions
    of a few results of his estimation and does not give details
    about it.   However, he states that he has based his estimate
    on the tax returns by the corporations and stockholders.

    The ratio of net corporate saving to corporate disposable
    income is, as 1950-59 averages, 88% in Norway, 79% in Japan,
    74% in Finland, 68% in W. Germany, 54% in the U.K., 41% in the
    U.S., 63% in Puerto Rica, 57% in Brazil. (U.N., World Economic
    Survey 1960, New York 1961, pp. 31 and 71).

Foreign Corporations: Revenue before taxes   1,400 million T.L.
                        Corporation Tax   - 282   "   "
                                                 ‾‾‾‾‾
                                                 1,118   "   "
                        20% withholding tax   - 223
                        Net Revenue after taxes   895   "   "

Total Net Revenue after Taxes of the Private Corporation Sector:
242 million T.L. + 895 million T.L. = 1,137 million T.L.   This
amount may slightly differ from the actual amount since we have
not considered various exemptions from the withholding Income Tax.

that the latter ratio holds good for 1962, the contribution by
Turkish private corporations to the total private saving in 1962
is calculated as 6%[1].   We have no data at our disposal with
respect to the savings by foreign corporations operating in
Turkey.   However, from the "profit transfers" item ($2 million =
18 million T.L.) in the Balance of Payments it can be computed
that only a small fraction, that is, about 2%, of the net revenues
of foreign corporations was remitted abroad in 1962.   Furthermore,
a survey by the S.P.O. of a sample of foreign corporations has
revealed that the profits of such corporations are to a great extent
reinvested.   From these two indications it could be reasonably
supposed that the retention ratio in the foreign corporations
operating in Turkey is similar to that in the Turkish private
corporations.   Hence, the total corporate saving may be put at
something around one-quarter of the total private saving[2].

Production in the private sector is dominated by unincor-
porated and small enterprises.   To illustrate this matter, in
industry only the production of the small units employing less
than ten workers or machines of less than 10 H.P., which are about

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1. (71% x 242 million T.L.)/2,900 million T.L. = 0·06.

2. In India, corporate income after tax comprised less than 1% of
    national income and corporate saving accounted for 5·8% of
    total private saving in 1950's.   In Japan these percentages
    are 13 and 53, respectively.   (U.N., "Financing of Economic
    Growth" in the Economic Survey of Asia & the Far East 1961,
    Bangkok 1962, pp. 41-65).

60,000 in number, constitutes 34% of the income that private enter-
prise creates in industry. The number of enterprises employing
more than ten workers or machines of more than 10 H.P. is about
5,200, only about one-third of which are of incorporated form[1].
No study, to my knowledge, has been undertaken to estimate the
saving of the unincorporated business sector in Turkey. It may
be argued that the rate of saving in this sector is likely to be
higher than in the incorporated business sector because of the
greater difficulties encountered by the former in obtaining external
finance. This favourable factor, however, might be more than
outweighed by some other considerations. First of all, the high
ratio of undistributed to total profits in the corporations is due,
as pointed out by Dr. Öngüt, to the inclusion of banks and insurance
companies among the incorporated enterprises. Secondly, the system
of taxation of corporation discriminates in favour of undistributed
profits[2], whereas no such an inducement exists for unincorporated
enterprises. Furthermore, today the small businessmen in Turkey
are not characterized by the acquisitiveness of capitalism, and,
hence, do not endeavour to create an ever growing expansion.
Their narrow-horizons coupled with the difficulties in financing

1. S.P.O., Development Plan 1963-1967, pp. 70; and, I.N.S.,
   Annuaire Statistique 1960-1962, pp. 400.
2. See Chapter 5, pp.184-194 of this dissertation. The conditions
   of the enjoyment of various incentives in the income tax
   may be fulfilled more easily by big corporations than by
   individuals and small unincorporated enterprises.

and marketing make them rather content with a comfortable living.
While these factors work so as to result in a somewhat lower rate
of saving by unincorporated as compared with incorporated enter-
prises, the greater identity between ownership and management in
the former also makes for a similarity between the saving behaviour
of the small businesses and households.

While the contribution of the corporate sector to the total
domestic saving is limited with its small share in the national
income, the same cannot be argued for the households sector as a
whole, including unincorporated enterprises.   Nor could the low
level of average per capita income be the cause of the low rate of
households saving.   In fact, several U.N. studies[1] have demonstrated
that the range of variation in the saving propensity of households
in various countries is not related to either the absolute level or
to the share of households income in national income.   Notwith-
standing great disparities of households income both Burma and
Japan saved more than ten per cent of it;   whereas in Taiwan, where
personal disposable income is higher than in Burma, the rate of
households saving was only one-half as high[2].

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1. World Economic Survey 1960, New York 1961; Economic Survey of
    Asia and the Far East 1961, Bangkok 1962; World Economic Survey
    1965, New York 1966.
2. U.N., "Financing of Economic Growth" in the Economic Survey of
    Asia and the Far East 1961, pp. 41-65.

It is therefore more reasonable to explain the low rate of private saving in Turkey by the lack of adequate desire for saving. Unless the factors accounting for the lack of adequate desire for saving are removed the increasing of national income could hardly lead automatically to a higher rate of private saving[1]. Such factors need, of course, be sought in relation to those income classes which have income surpluses over their essential consumption, since only they can afford saving. As manifested by the study of the distribution of income and wealth in Chapter 1, the distributional inequalities in Turkey are, at least, as great as in the advanced countries. It seems, however, that the very existence in Turkey of the highly unequal income and wealth distribution has not been sufficient to secure a high rate of private savings, particularly, of households savings. This means that the great distributional inequality in Turkey does not coincide with the concentration of income and wealth in the hands of those income groups with strong propensities to save[2]. The main factors

1. As Keynes thought the proportion of consumption to income can be expected to decline as income rises. But consumption function cannot be linear, non-proportional and stable in a developing country like Turkey, where the scope for the development of wants and needs is immense and where a swift development is projected. This has been proved empirically by S. Kuznet in relation to the U.S., and provoked new consumption theories by A. Smithies, Dusenberry and Friedman, etc. (G. Ackley, Macroeconomic Theory, New York 1961, The MacMillan Comp., pp. 236-246).

2. "The ratio of savings to national income is a function not just of inequality, but more precisely, of the ratio of profits to national income" (W. A. Lewis, op.cit., pp. 227). In Ceylon 46% and in the Philippines 56% of households income is classified as enterpreneurial income from property; but the households in the

accounting for the weakness of the saving propensity of the well-to-do class in Turkey are particularly related to three structural defects which are:-

(1) the prevalence of a strong demonstration effect and of the popular habit of conspicuous consumption;

(2) the static character of the wealth structure;   and

(3) the lack of a financial superstructure to provide attractive saving means[1].

It is not possible to describe in measurable terms the effect of emulative consumption on the rate of private saving. However, the enormous waste of resources in luxury consumption is conspicuous to anyone travelling around the country or going through the modern Turkish literature, even daily newspapers. The present state of advanced international co-operation embracing Turkey in every field, the advanced techniques of communication and the democratic system of government make it impossible for Turkey to repeat the Japanese experience of containing the consumption of the masses to the traditional patterns.   The

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1.   These are of course inter-related factors;   the inter-relation is particularly strong between (2) and (1), and (2) and (3).

(contd. from page 120):-

Philippines have been dissaving.   In Japan the proportion of households income appropriated by enterprise and property income has been the same as in Ceylon, but the rate of household saving there has been $2\frac{1}{2}$ times as high as in Ceylon.(U.N., Financing of Economic Growth, op.cit.).

American way of life is, through the high-income classes, permeating

even among the masses, but with its attitudes towards consumption

and not towards investment, savings and working[1].   The political

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1. P. T. Bauer and B. S. Yamey write in their "The Economics of
    Underdeveloped Countries", Camb. Univ. Press. Camb. 1963,
    p. 139:   "It is not obvious why the high standards of consump-
    tion in richer countries alone should arouse interest.
    Accumulation and investment as means to an improved standard
    of living may be imitated; .....It is of interest, for example,
    that immigrants in rich countries not only gradually assimilate
    the local habits of consumption but also that many of them save
    a very high proportion of their income......".   I think Bauer
    & Yamey are led to a mistaken view with respect to international
    demonstration effect by their belief in unhampered trade
    between developed and poor countries.   First of all, it is
    obvious that consumption patterns, and not saving and invest-
    ment habits, of rich countries will be imitated because (a) it
    is more appealing to human nature, particularly in under-
    developed countries: (b) consumption pattern of rich countries
    is more conspicuous to the people of underdeveloped countries
    than their saving and investment patterns;   (c) Today, every
    effort is made to expand markets for the commodities which may
    be deemed as luxury for poor countries while no such effort is
    made to develop the saving and investment habits of the people
    of poor countries.   In the second place, the example given by
    the authors is not relevant to the issue for these reasons:
    (a) It is attitudes of the society in underdeveloped countries
    that induce the individual to indulge in emulative consumption.
    To observe the behaviour of an immigrant in an advanced country
    and then to reach a judgement from this observation about the
    behaviour of the poor country's people is not convincing at
    all.   (b) An immigrant is not the typical representative of
    the people of his native country simply because being an
    immigrant proves that he is dissatisfied with the status quo
    and showing enterpreneurial habit to take risks.

struggle for power has been proved to lead to success through the
promises for higher consumption without mentioning the sacrifices
necessary for it.   The politicians' slogan that Turkey is a state
of non-strata is endeavoured to be proved true by low- and,
particularly, middle-income classes indulging in conspicuous
consumption.   This process is fed by the continuous incorporation
of new wants and needs in the living standard of high-income classes.

The Development Plan envisages fiscal and credit policy
measures in order to cope with luxury consumption.   In this
connexion, the tougher rules of taxation on buildings introduced
from the beginning of 1963 and the tighter credit market since the
end of 1963, coupled, in both cases, with a discrimination against
luxury buildings, have checked the increases in the construction
of luxury buildings[1].   According to the license-statistics, the
share of blocks of flats in both the total value of, and total area
covered by, new construction has been declining since 1962 in favour
of tenement houses, industrial and commercial buildings, and,
particularly, cultural and social constructions[2].   The introduction
of a new tax on private cars and taxation of non-basic commodities

1.   O.E.C.D., Turkey, 1965/66, Paris 1966, p. 40.

2.   Ministry of Finance, Budget Preamble for 1966 Fiscal Year,
      Ankara 1965, p. 72.

at higher rates than the necessities, etc., have no doubt served
as curbs on emulative consumption.   But the problem is so deeply
rooted in the social value pattern and wealth structure that it
cannot be solved with incentive measures such as of the monetary
and fiscal policy.   In the long run, education can do much good
in incorporating the "rationale" element into the value patterns.
However, the close interaction between the value pattern and
wealth structure of any community suggests that the adverse effects
of emulative consumption on the rate of saving could not be reduced
to a minimum unless the wealth structure is revised.

In Turkey, the effects of the present wealth structure go,
indeed, well beyond a mere inducement of consumption through
demonstration effect.   As will be seen shortly, its static character
is the crucial obstacle to raising the rate of private saving[1].
In Turkey, only a fraction of total real wealth is produced wealth;
the major part of total wealth consists of natural resources such
as farm land; mineral resources, forests, fisheries, etc., the

1. The following analysis of the relationship between the static
    wealth structure and the low rate of private saving in Turkey
    is based on a study by Prof. Anders Östlind, of UNTAO, who has
    been requested by the S.P.O. to prepare it as the basis of the
    chapters dealing with monetary policy, wages and price policies
    of the First Five-Year Development Plan: "Scope for Non-
    inflationary Economic Expansion in Turkey", Ankara May 1962,
    mimeographed, pp. 107.

remainder being dwellings, farm buildings, simple tools and means of transportation, animals, seed, inventories and the like. The sum total of real wealth does not change much. Putting it differently, net real investments are low relative to the total wealth. Most individual fortunes are made up predominantly of real assets, the financial components being meagre. The preferences of individual wealth-owners are oriented rather towards existing property objects. Some transactions in real wealth objects may take place but without anything being added to the total real wealth. This general static frame characterizes predominantly the wealth structure in the rural economy of Turkey but less so in the urban sector where the dynamic-wealth-owners are more frequently met. Dynamic-wealth-owners, compared with static-wealth-owners, have a wider register of investment alternatives and wider knowledge and better competence in appraising capital values. They are the potential force for industrial and commercial development. Yet, the majority of dynamic-wealth-owners do not at present give priority on their preference scales to investments in modern industrial and commercial enterprises but to traditional investment in land, particularly urban and potentially urban land. In this inclination towards investment in land dynamic-wealth-owners are attracted by the prospects for big capital gains, while the static-wealth-

owners hang on investments in land for such reasons as prestige, ignorance of alternative investment outlets and lack of knowledge and skill necessary to deal with investments in assets other than land.   It is, however, understandable that as long as the dynamic-wealth-owners are still very few and as long as they have only limited access to credits at moderate rates of interest there will be much land that will stand out as undervalued in the opinion of dynamic-wealth-owners.

It can be seen that the above-described wealth pattern in Turkey offers a number of obstacles to increasing the rate of private saving.   Firstly, as long as the static-wealth-owners dominate over the major part of wealth the rate of investment in private sector is bound to be low.   In Turkey, saving and investing units in most cases are the same.   Therefore, the domination of the wealth-owners with narrow-horizons as regards investment alternatives result in lack of inducement for saving.   Secondly, it is apparent that in a country with a wealth structure of the type observed above profits cannot constitute a significant part of the private sector's income.   In Turkey, most incomes out of which some saving could be afforded are in the form of rental incomes and capital gains on real estate;   and, these are known as flowing in large part towards lavish consumption expenditures.

Thirdly, the orientation of the most wealth-owners towards investments in existing assets, is the main obstacle for the growth of the private sector in Turkey, though it is sometimes argued that it is the lack of adequate saving that holds back growth in the private sector. As a matter of fact, capital formation and saving can escalate each other if only a dynamic character can be infused into the present wealth structure in Turkey. Finally, the prevailing pattern of wealth structure in Turkey is certainly not conducive to the flourishing of a financial superstructure which would stimulate private savings by providing saving means of various types and which would secure the using of available savings in the most productive fields.

The Development Plan contemplates various Government action to change the composition of private wealth so as to accord a dynamism to it. Of these, the following are of vital importance:-

1. A progressive land policy;

2. To induce the preferences of dynamic-wealth-owners in favour of the creation of real industrial and commercial capital and stimulate the growth of private corporations by introducing new legislation, especially tax reforms;

As it is stated in the 1963 Annual Programme[1], a land reform is the precondition for the success of the measures envisaged in the Development Plan as regards the Agricultural Sector. Attention here will, however, be focused only on the possible effects of the land reform proposed by the Plan on the wealth pattern and saving propensities; and, it will be assumed that the safeguards in such a reform will be effective in maintaining and, perhaps, raising, the agricultural productivity.

The studies for a comprehensive Land Reform Bill started as early as in 1961. The main features of the proposed Reform were the limitation of maximum and minimum size of holdings according to the types of farming and varying from one district to another, and the protection of the rights of share-croppers and tenant farmers by the special legislation[2]. The expropriation of land-holdings above the maximum size would serve two important purposes. First, it would wither away the absentee landlordism and the holding of land with non-commercial purposes. Secondly, the ex-landlords would be endowed with financial assets which are likely, if adequate incentives are given, to be placed

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1. S.P.O., 1963 Annual Programme, pp. 303.
2. Ibid, pp. 303-304.

under the disposal of entrepreneurs. These changes in the wealth

pattern of the well-to-do agrarian class would stimulate them to

curb their lavish consumption expenditures and to put their

resources into profitable uses[1], since only in this way they could

maintain their higher status in the society. As for the rest of

farmers, those who would become owners would have an incentive to

save and invest more on their own land. Moreover, thefixing of

rents and also fixing the share of landowner in the crop-sharing-

system would make secure the small peasant, thus encouraging him

to save and invest in the land. It is, however, likely that the

land reform would create tendencies towards increasing consumption.

Although the part of the increased consumption directed towards

the manufactured goods could help in expanding the limited market,

the other part directed towards food crops might result in a

reduction of the supply of foods to the market and in a reduction

in the cultivation of cash crops and export crops. It would

therefore be necessary to give more positive inducement to the

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1. Since the ex-landlords are neither accustomed nor willing to
   keep substantial financial assets they may try to re-invest in
   urban land and buildings. But the market would then be so
   narrow that even a marginal increase in demand will force urban
   land and building prices up to a level that makes them unattrac-
   tive investment alternatives. The scope for residential house
   building is also limited by demand factors. There is then no
   course open to ex-landlords who are anxious to get rid of their
   "excessive" financial assets other than to look more to new
   investments in industrial and commercial ventures.

farmer to invest than the mere ownership spirit.

Despite the great emphasis placed on a land reform in
the Development Plan and Annual Programmes, the landed interests
have so far succeeded in obstructing the progress of the Bill in
the Parliament.   Following the change in power in the October
1965 election, the hopes for a radical land reform have to be
deferred till the next election in 1969.

The tax measures which are designated to affect the
investment preferences of the wealth-owners are studied in the
next chapter.   The conclusion arrived at there is that the
incentive measures in the present tax system are incompatible
with the Plan's objectives, i.e., they favour the use of resources
in agriculture and in speculative investments.

III

PRIVATE SAVINGS THROUGH FINANCIAL
ASSETS

The kinds of assets through which savings are held do not
have much significance from the viewpoint of this dissertation.
The attention in this dissertation is concentrated on the level of,
and changes in, the aggregate level of domestic savings in relation
to G.N.P.   Whether savings are largely held in the form of physical

assets or in the form of financial assets does not have any direct relationship with the level of savings/G.N.P. ratio. Similarly, whether people hoard in cash or purchase saving bonds has nothing to do directly with the level of savings/G.N.P. ratio. For the act of saving is essentially an act of restraint from current consumption.

The kinds of assets through which savings are held constitute a problem which is more relevant to the investment side rather than to the savings side of the financing process. If savings are largely directed towards saving institutions the authorities will have greater control over the allocation of savings to various uses than they will have if savings are held in cash hoards, jewelry, or the like. It is true, the authorities can extend credit for development projects, without inflationary effect, to the amount of money withdrawn from circulation into cash hoards[1]; but, money in hoards may be "hot" in the sense that it may suddenly be spent.

The private savings through financial assets are shown in Table 26. In Turkey, as in all underdeveloped countries, the

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1. B. Higgins, Economic Development, London 1959, p. 484.

financial assets which serve as saving media are of very limited
types.   The most important of them is the bank deposits.   In
the second place, currency, saving bonds and contributions to the
Pensions Fund can be counted.   Finally, the contributions to the
Workers' Insurance Fund may be expected to develop as an efficient
medium of saving in future as the industrialization and the
organisation of workers gain momentum.

TABLE 26

PRIVATE SAVINGS THROUGH FINANCIAL ASSETS, 1960-1964.

Million T.L.

Changes in:	1960	1961	1962	1963	1964
1. Currency	422	312	387	399	909
2. Demand deposits with banks	111	369	579	813	1094
3. Time deposits with banks	255	305	68	410	227
4. Saving bonds	-	407	407	478	542
5. Pensions Fund	375	459	497	580	627
6. Workers' Insurance Fund	43	48	54	61	71

Sources: Banque Centrale de la Republique de Turquie S.A.,
Bulletin Mensuel, Avril-Mai, No. 4-5, Ankara 1965.
Institut Nationale de la Statistique, Annuaire
Statistique 1960-1962, Pub. No. 460, Ankara 1964.

The first item in Table 26 shows the changes in the volume of currency (banknotes plus coins) circulating outside the banks. The fact is sometimes missed that the currency held by the public represents a part of the total savings in the sense that the current consumption of goods and services is foregone in order to acquire it[1]. Since the Turkish Lira is not convertible it is not necessary for the authorities to ensure that a substantial fraction of the resources handed over to them in return for currency is held in the form of gold, or of foreign exchange easily convertible into gold[2]. The increase in the currency in circulation is backed mainly by Government Bonds. This means that the Government may obtain command over a part of private savings by increasing the currency. There are, however, some limitations over this method of financing the Public sector, which will be explained in Chapter 6.

The Commercial banks and the Agricultural Bank, which is a State Economic Enterprise, play a widespread role all over the country in the collection of small savings. With their branches

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1. E. Nevin, Capital Funds in Underdeveloped Countries, London 1961, p. 4.

2. If a part of the currency increase is backed by foreign exchange, this means that foreign governments acquire command over resources foregone by the Turkish public in order to hold more currency. The same explanation holds good for use of gold as backing, since gold is not extracted in Turkey.

extending to the remote parts of the country and with their
various schemes to attract deposits from the public, they may be
considered as inducing the public to save more and as mobilizing
the private savings.   However, a study by Dr. O. Yenal has shown
that the volume of total deposits in Turkey is closely related to
the volume of currency in circulation[1].   In other words, the
people have deposits with banks mainly for liquidity purposes.
This, of course, does not alter the fact that deposits constitute
a part of total private savings; but it does make deposits a
very volatile part of private savings.   Consequently, the
commercial banks and the Agricultural Bank cannot use their
resources to a great extent for financing the capital formation.

Saving Bonds are a recently introduced device of compul-
sory saving.   Those who are subject to Income Tax are bound to
accept saving bonds to the value of a certain percentage of their
income.   This percentage, which is a flat rate for all taxpayers
and which cannot be higher than 3%, is determined by the Ministry
of Finance.   Varying exemption limits are considered for different
kinds of incomes.   Saving Bonds are not transferable for ten years[2].

1. During 1953-1962 the ratio of deposits to currency stood around
   2.   O. Yenal, op. cit., pp. 22-23.
2. These particulars were those prevailing by the mid-1965. Some
   changes in them had taken place and substantial alterations were
   being proposed by then. For a detailed account of the practice
   of Saving Bonds in Turkey, one may be referred to these studies:
   Articles by Alpaslan Onay in the newspaper "Ulus", 13-14 June,
   1964, 8 December 1964, and 15 July 1965; H. Kizilyalli, op. cit.,
   92-102.

Saving Bonds may cause an increase in total domestic savings if they entail a reduction in the consumption by the Bond owners. As for the low-income groups, Saving Bonds may be regarded as contributing to the increase in domestic savings since the low-income earners would not have probably saved voluntarily. As for the middle and high income classes, Saving Bonds may partly cause an increase in total savings and partly give rise to a transfer of some private savings to the public sector. This is because some individuals in these income classes may reduce their voluntary savings as they are forced to save through Saving Bonds.

Turkey does not have a well-developed social security system. Social security services are performed on a limited scale by the Pensions Fund and Workers' Insurance Fund, which have status as State Economic Enterprises. The former covers all civil servants and military officers, while the latter is concerned with the employees of the S.E.E., and the large private enterprises but is very limited in its coverage.

A social security system based on the principle of actuarial reserves will accumulate large savings, at least for a time, because future benefits (especially retirement and death benefits) must be

preceded by a period of building up reserves[1].   In a mature system,

payments would on an average equal receipts, except to the extent

that the working population grows.   However, in Turkey, where the

coverage of the social security system is expected to extend

steadily as the area of the "business economy" grows relative to

the "non-business economy", the period of accumulation may be very

long.

The proliferation of financial institutions in Turkey cannot

be expected to take place in a short time.   For the development of

the financial institutions of the types observed in today's advanced

countries, it is not sufficient to have funds willing to flow into

them but also there must be a steady demand for these funds by the

business sector through the issue of bonds and shares.   This

requires that the capitalist class in Turkey must change their

scale of preferences in relation to investment and their methods of

financing.   This is a time-consuming process.   However, there is

a whole range of savings institutions that can be developed at the

present time in Turkey.   For instance, post office savings,

friendly societies, co-operative credit societies, co-operative

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1.   E. M. Bernstein, "Financing Economic Growth in Underdeveloped
     Economies", in Savings in the Modern Economy, (ed.) W. W. Heller,
     The Univ. of Minnesota Press, Minneapolis 1953, p. 299.

retail societies, building societies and the like do not require any great specialization within the financial system. These institutions have proved to be effective in mobilizing the small savings in many underdeveloped countries[1]. "If they are pushed right under the individual's nose, to the extent of having street savings groups, or factory groups, or even deductions from earnings at source, people save more than if the nearest savings institution is some distance away"[2].

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1. United Nations (EGAFE), Mobilisation of Domestic Capital, Reports and Documents of the Second Working Party of Experts, Bangkok 1953.
2. W.A.Lewis, op.cit., p. 229.

CHAPTER 5

TAXATION.

In the previous chapter we have seen that the private
sector could not provide even half of the savings required from
the domestic sources for the realisation of the plan targets.
The major part of the efforts to mobilise the real resources
for development purposes, therefore, falls upon the public sector.
The public sector has at its disposal many instruments to obtain
command over a particular proportion of the national income.
The present chapter will deal with taxation, which is of the
foremost importance compared with other instruments, leaving non-
tax instruments to the next chapters.   In the first section
below, the taxation structure of Turkey will be introduced.
This will be followed by a study of the main problems of the
tax system.   In this connection, Section II will be devoted to
the problems of direct taxation of the agricultural sector;
section III to the taxation of incomes and profits; and section
IV to the taxation of commodities.   Finally, the study of
taxation will be concluded with an analysis of the taxation
policy followed in the first years of the plan implementation
and with some suggestions with respect to the policy to be
followed in the rest of the plan period.

I

THE TAXATION STRUCTURE IN TURKEY

The structure of taxation in Turkey bears many characteristics common to all underdeveloped countries. We have already seen in chapter 3 that the ratio of tax revenue to G.N.P. is around 12% in Turkey. On the other hand, in many advanced countries, this ratio is twice as high as it is in Turkey. As seen from Table 27, the ratio of tax revenue to G.N.P. in Turkey is considerably smaller than in all the developed countries, except Japan and Switzerland, and is even lower than in some underdeveloped countries such as Brazil, Ceylon, Burma, the Federation of Malaya, and Greece.

Only about one-third of total tax revenue in Turkey comes from direct taxes (taxes on income and property), whereas direct taxes constitute the major source of revenue in most of the developed countries. Indeed, the share of direct taxes in total tax revenue in Turkey is smaller than in ten out of the thirteen developed countries listed in Table 27. On the other hand, only four out of the fifteen underdeveloped countries in the table obtain through direct taxes a larger share of their total tax revenue than Turkey can do.

TABLE 27

TAX REVENUE AND DIRECT TAXES
in Developed and Underdeveloped Countries

Country	Year	Tax revenue as % of G.N.P.	Direct Taxes as % of total tax revenue
I. Developed Countries:			
1. Australia............	1961	24·1	53·5
2. Austria..............	1961	23·3	48·0
3. Belgium.............	1961	19·0	38·0
4. Canada..............	1961	13·6	63·0
5. France..............	1961	20·1	29·7
6. Germany (Fed. Rep.)..	1961	34·8	58·9
7. Italy...............	1961	19·3	21·5
8. Japan...............	1961	10·6	52·9
9. Netherlands.........	1961	23·1	60·6
10. Sweden..............	1961	21·9	52·0
11. Switzerland.........	1961	7·3	22·3
12. United Kingdom.......	1961	30·0	54·8
13. United States........	1961	24·7	76·2

Table 27 (contd.)

Country	Year	Tax revenue as % of G.N.P.	Direct Taxes as % of total tax revenue
II. Underdeveloped Countries:			
1. Argentina............	1961	10·2	28·0
2. Brazil..............	1960	16·9	23·8
3. Burma...............	1961	13·3	34·6
4. Ceylon...............	1961	19·0	25·2
5. Colombia............	1960	7·4	57·8
6. Federation of Malaya..	1960	20·1	22·1
7. Greece..............	1961	13·1	20·2
8. India[1].............	1961	9·2	29·7
9. Indonesia[1]..........	1959	6·4	42·2
10. Israel..............	1961	18·7	41·5
11. Mexico..............	1960	7·6	25·8
12. Pakistan[2]...........	1961	11·6	25·0
13. Philippines..........	1961	7·5	27·9
14. Spain...............	1960	11·3	40·9
15. Thailand............	1959	8·7	10·0
16. Turkey..............	1961	11·6	34·1

1. As percent of national income.
2. As percent of net national product at 1949-52 prices.

Sources: as taken from K. S. Krishnaswamy, "The Evolution of tax structure in a Development Policy" in the Government Finance and Economic Development, edited by A. T. Peacock and G. Hauser, Paris 1965, pp. 75-90.

1. G.N.P. figures are as given in the International Financial Statistics, July 1963.
2. Figures relating to taxes are as given in the U.N. Statistical Year Book, 1962.

Note: Receipts from fiscal monopolies are considered as non-tax revenue.

The total tax revenue has increased rapidly since 1952. A great proportion of the increase in money terms, however, is accounted for by rising prices. As seen in Table 28, although total tax revenue in 1964 was almost six times as great as that in 1952 in money terms, the increase in real terms was only slightly more than twice. If we take account of the population factor as well, it is understood that the increase in per capita tax has been only 56% in a twelve-year period, most of which has occurred after 1962. The increases in per capita tax during 1952-1960 have been only slightly more than proportional with the increases in per capita national income. This is observed from the ratio of total tax revenue to national income which increased from 11% in 1952 only to 11·6% in 1956 and kept the same level in 1960. In other words, as already shown in Chapter 3, income elasticity of the Turkish tax system has been around one (unit elasticity) during the 1950's. Only with the beginning of economic planning, attempts have been made to increase the share of tax revenue in G.N.P. (see Table 28).

As for the composition of the taxation, the income tax has the largest share in total tax revenue. Since its first application in 1949 its importance has grown steadily with its share in total tax revenue rising from 19% in 1952 to about 30% in 1956, and to 32·6% in 1960. In recent years its importance

TABLE 28

CERTAIN TAX INDICATORS

	1952	1956	1960	1962	1963	1964
1. Total Tax Revenue (mill. T.L. money terms)	1,580	2,816	5,671	7,114	8,424	9,258
2. Index of (1)	100	178	360	450	533	586
3. Wholesale Price Index	100	141	243	265	276	272
4. Total Tax Revenue in real terms (mill. T.L.)	1,580	1,928	2,334	2,685	3.056	3,404
5. Index of (4)	100	122	148	170	193	215
6. Per Capita Tax in real terms (T.L.)	71	78	84	92	102	111
7. Index of (6)	100	110	118	120	143	156
8. Total Tax Revenue as % of G.N.P.	11	11·6	11·6	13·0	13·4	13·0

Sources: for (1) see Table 29.

for (3) see Chapter 1, Table 8; and Chapter 4; p. 110n.

for population figures, see Chapter 1, Table 9; and Chapter 4, p. 110n.

for G.N.P. figures, S.P.O., Development Plan, and Annual Programmes
for 1964 and 1965.

TABLE 29

REVENUES FROM THE TAXES IN THE GENERAL & ANNEXED BUDGETS

(Million T.L.)

Kind of Tax	1952	1956	1960	1962	1963	1964
Income Tax	299	840	1851	1911	2240	2419
Corporation Tax	50	129	238	359	415	443
Defence Tax on Buildings	5	10	24	31	36	92
Inheritance and Gift Tax	3	10	10	13	14	16
Motor Vehicle Tax	-	-	-	-	41	51
Revenue from Abolished Direct Taxes*	57	58	50	22	5	2
TOTAL DIRECT TAXES	414	1047	2173	2336	2752	3024
Import Production Tax**	225	170	681	837	883	744
Domestic Production and Expenditure Tax**	162	343	506	618	705	744
Petroleum Production Tax***	81	96	187	283	336	554
Petroleum Import Treasury Share	-	-	128	180	169	182
Banking & Insurance Transaction T.	27	95	227	237	342	366
Transportation Tax	18	35	27	62	64	69
P.T.T. Service Tax	5	7	25	27	36	40
Customs Duty	191	193	551	737	796	948
Defence Tax & Monopoly Rev.	209	417	634	941	1072	1193
Sugar Consumption Tax	137	222	110	330	361	408
Foreign Travel Expenditures Tax	-	-	-	-	98	110
Revenue from Abolished Indirect Tax	5	6	9	7	6	20
Stamp Duty	50	84	231	276	545	565
Real Estate Regn.Fees	23	48	83	106	134	152
Other Duties and Fees	33	53	99	137	118	132
TOTAL INDIRECT TAXES	1166	1769	3498	4778	5672	6233
TOTAL TAX REVENUE	1580	2816	5671	7114	8424	9258

 * Livestock tax till 1961, the tax on artisans and shopkeepers
   till 1956 and the tax on private cars till 1962.
 ** Till 1956 it shows the revenue collections from the "import
   and production transactions tax".
*** Till 1956 it shows Revenue collection from the Petroleum Road
   Tax and Petroleum Consumption Tax.

TABLE 29a.

THE SHARES OF SOME IMPORTANT TAXES IN TOTAL TAX REVENUE

(as %)

Kind of Tax	1952	1956	1960	1962	1963	1964
Income Tax	19·0	29·8	32·6	26·8	26·6	26·1
Corporation Tax	3·2	4·6	4·2	5·0	4·9	4·8
TOTAL DIRECT TAXES	26·3	37·2	38·3	32·8	32·6	32·6
Import Production Tax	14·2	6·0	12·0	11·7	10·5	8·0
Domestic Production T.	10·2	12·2	9·0	8·7	8·4	8·0
Petroleum Production T.	5·1	3·4	3·3	4·0	4·0	6·0
Banking & Insurance T.T.	1·7	3·3	4·0	3·3	4·0	4·0
Customs Duty	12·0	7·0	10·0	10·3	9·4	10·2
Defence Tax & Monopoly Rev.	13·2	14·8	11·2	13·2	12·7	12·9
Sugar Consumption T.	8·6	8·0	2·0	4·6	4·3	4·4
Stamp Duty	3·1	3·0	4·0	3·8	6·4	6·1

Source for Tables 29 and 29a.

Ministry of Finance, "Budget Revenues Bull., 1964"
Ist. 1965, pp. 14-15.
The 1964 figures are provisional.

has somewhat declined and its share now stands at slightly above a

quarter of the total tax revenue.   The tax on the profits of

corporations, namely, the Corporation Tax provides something of

the order of 5% of total tax revenue.   Thus the taxes on incomes

and profits together account for in recent years around 31% of total tax revenue while their share was 34·4% in 1956 and 36·8% in 1960. The other direct taxes, i.e., defence tax on buildings, inheritance and gift tax and the recently levied motor vehicles tax are insignificant from the revenue point of view. They altogether amounted to only 1·7% of total tax revenue in 1964.

Among the various indirect taxes the largest revenue is raised by the defence tax on, and the profits from the sale of, the products of the State Monopoly Administration which are the most widely consumed commodities, such as cigarettes, alcoholic drinks, tea, table salt, etc. This is followed by the import production tax and customs duty. They fluctuate in accordance with the external payments situation, and together provided 18·2% of the total tax revenue in 1964. When taken together, their share appears to have continually diminished from 26·2% in 1952 to 22·0% in 1960 and to 19·9% in 1963. In view of the intention of Turkey to join the Common Market it is reasonable to expect that the diminishing trend of revenue from the taxation of commodities of foreign-origin will continue in the coming years. The domestic Production Tax, which is an excise tax levied on raw materials and primary products, provided 8% of total tax revenue in 1964 against 12% in 1956. With the increasing

consumption of petroleum, the share of the petroleum production
tax in total tax revenue has increased from 3·3% in 1960 to 6% in
1964.   Taxation of the consumption of sugar constituted an
important source of revenue in the 1950's but in the 1960's its
contribution to the total tax revenue has been only slightly above
4% against 8·6% in 1952 and 8% in 1956.   Banking and Insurance
Transactions Tax and Stamp Duty, which fall in the main upon
businesses and property owners, each contributes around 3-4% of the
total tax revenue.   However, the recent changes in the stamp duty
rates raised its share to over 6% in 1963 and 1964.

II

TAXATION OF THE AGRICULTURAL SECTOR

In the days of the Ottoman Empire, both agricultural land
and agricultural income were subject to taxation.   The tax levied
on agricultural income, namely, the tithe, constituted the most
important source of revenue of the Empire.   However, since it had
become an instrument of force and source of injustice, it was
abolished by the Republican Administration in 1925.   Agricultural
incomes had not since then been directly taxed till 1963, except
during the Second World War when the agricultural income was taxed
both directly by the Agricultural Produce Tax and indirectly by
the tax on exports.   The taxation of agricultural land, on the

other hand, continues being in effect at the present time; but, owing to the absence of any reassessment of land values since 1936, it has been largely eroded. According to the 1936 cadastral survey and to a sample survey recently made by the University of Ankara, the land values in 1960 were on average 50 times the 1936 values, whereas the increase in the land tax revenue in the same period has been only 2·7 fold. Accordingly, the share of the land tax in total tax revenue fell from 4% in 1936 to 0·3% in 1960[1].

Although, according to the S.P.O. estimates, the net income of the agricultural sector in 1961, that is, 17·6 billion T.L., accounted for 42·5% of the net domestic product of 41·3 billion T.L., agriculture contributed 0·8% of all direct taxation[2]. As regards the indirect tax burden of the agricultural sector, Mr. Kaldor estimates that, in view of the high ratio of income consumed directly by the producers, its contribution could hardly exceed 20-25% of the total revenue from indirect taxes, though he points to the impossibility of allocating the incidence of indirect taxation with any precision[3]. Thus, it becomes apparent that the burden of all kinds of taxes

1. Nicholas Kaldor, Report on the Turkish Tax System, April 1962, mimeographed.
2. Ibid.
3. N. Kaldor, op. cit.

falling on the agricultural sector is around 5% of its income[1]

against a burden of 20-25% on the rest of the economy[2].

Throwing a disproportionate share of the burden of taxation
on the non-agricultural sectors does not seem to be compatible with
the objectives and strategy of the Development Plan.   It does not
seem feasible, quite apart from the need of increasing public
savings, to plan a growing share for the non-agricultural activi-
ties in the national income and in the total active population, on
the one hand, and to follow a taxation policy giving every induce-
ment to the agricultural activities to expand at the expense of
non-agricultural activities, on the other.   Taking into account
that about 15% of total investment expenditures is planned to go
directly into agricultural sector and that considerable benefits
will accrue to the agricultural sector from the investments in

1. This has been calculated on the basis of the following data: In
   1961 the revenue from direct taxation was 2626 million T.L. and
   from indirect taxation 4073 million T.L. (Ministry of Finance,
   "Budget Revenues Bulletin, Fiscal Year 1964", Istanbul 1965,
   pp. 14-15.
2. Mr. Kaldor's estimates are somewhat different from the following
   estimates quoted in Hüsnü Kızilyalli, Economic effects of the
   Turkish Tax system (in Turkish), mimeographed by the S.P.O.,
   1965, pp. 31. : Nazif Oker estimated that in the early 1950's
   the agricultural sector contributed 8·15% of its income to the
   total tax revenue and the other sectors 22·83% of their incomes.
   The estimates made by Professors O. Dikmen and M. Yaşa, of the
   Istanbul Univ., in 1963 give the former ratio as 8% and the
   latter as over 25%.   These estimates differ from those of
   Mr. Kaldor particularly with respect to the burden of the agric-
   ultural sector, though the difference is not as great as to alter
   the main conclusion that agricultural sector is taxed more
   lightly than the other sectors.

energy, transport and communication and housing, which altogether amount to the 40% of total investment expenditures, the prevalence of the pre-plan state of agricultural taxation in the plan period would in effect mean the subsidization of the primary sector (agriculture) by the secondary (industry) and tertiary (services) sectors.

Since economic development invariably entails a growing proportion of the population to be employed in non-agricultural sectors, the "agricultural surplus"[1] must steadily increase in order to make a balanced growth possible. Our study, in chapter 1, of the characteristics of the agricultural sector has shown that the production in that sector is held back by some basic structural defects. Hence, it seems that an expansion of the agricultural surplus cannot be relied on to occur automatically as a result of the economic incentives which may be expected to arise from the overall process of growth. Besides, the economic incentives do not operate in the same way in agriculture as in the case of industry and commerce. An excess demand for food may, through the rising prices of basic foodstuffs, lead to a decrease in the supply of food as the farmers receiving higher prices may tend to

1. By "agricultural surplus" we mean the excess of agricultural production over the food consumption of the agricultural sector.

increase their own consumption and/or to work less. The imposition
of compulsory levies on the agricultural sector which will penalize
the unproductive farming units may therefore be the only sure way
of compelling this sector to expand its surplus.

Manifestly, there is every good reason to throw on the
agricultural sector a tax burden much heavier than it has so far
carried. Although the attempts made in the 1950's to subject
agricultural incomes to the income tax law seem to have been
frustrated with such arguments as that the low levels of per capita
incomes in the agricultural sector do not permit levying any tax
and that administrative difficulties involved in such a taxation
are formidable, the real factor behind this failure has always been
the political rather than any other considerations.[1]

The fact that, on average, the farmers in Turkey are poorer
than the rest of the community does not justify the farmers' paying
less tax[2]. The averages may be misleading in the assessment of

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1. M. Yaşa, "The Taxation of Agricultural Income and Land" in the
   Agricultural Aspects of Economic Development, edited by the
   Economic and Social Studies Conference Board, Istanbul 1964,
   p. 190.

2. For the relative income of farmers, on average, see chapter 1,
   page 9.

the tax potential of an economy or any sector of it. The degree

of inequality in the distribution of wealth and income and the

amount of income in the each income range ought to be considered

as well. In the Turkish agriculture the land tenure situation

is the best indicator of the degree of inequality in the distribu-

tion of wealth and income. We have already explained in

chapter 1 how great is the inequality in the distribution of

landholdings among farm families[1]. By classifying all the farm

families into ten percentile according to the size of their land-

holdings we see that on the average the farmers in the first three

percentiles own farm units of 11 decares while the farm families

in the top percentile own farm units of about 400 decares. The

degree of concentration in the ownership of land is also very

great. While the first three percentiles of the farm families

own only 4·3% of the total cultivated area and the following three

percentiles 14·3% of the area, the families forming the top percen-

tile own more than half the total cultivated area. Despite the

existence of such a substantial inequality between the agricultural

income groups, it is estimated that under the tax system of the

pre-plan period the lowest income category in agriculture pays

6·7% of its income in taxes, the middle category 9·7% and the highest

1. See Chapter 1, pages 10-13.

income category only 12.5% of its income[1].   It thus becomes

obvious from what we have so far said in this section that it is

not only an economic necessity to bring the agricultural sector

within the tax system but that the sector also carries a substan-

tial tax potential which cannot be neglected in a country where

the main obstacle to economic development is the low level of

total savings.

There are two methods of taxing the agricultural sector

directly :-

(1) taxation of agricultural land, and

(2) agricultural income tax.

In the Ottoman Empire and in the initial stages of development of

today's advanced countries, much greater reliance has been put on

the former.   But, today, it has lost its significance in Turkey,

and only has some role in the budgets of the local administrations.

Taxing the agricultural sector within the General Budget

was made possible with the Income Tax Law No. 193 which was enacted

on the eve of return to the parliamentary regime, 31.1.1961,

following the May 1960 coupe d'état.   However, the heavy pressure

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1. From the report of Prof. J. L. Enos given to the Turkish Govern-
   ment quoted in Dr. G. Kazgan, "Agriculture and Industrialization"
   in the Agricultural Aspects of Economic Development, op. cit.,
   p. 65.

by the big landlords on the political organs soon resulted
in the enactment of the Law No. 35 on 22.8.1962 which provided
that the application of the legislation of the Income Tax Law
No. 193 pertaining to agricultural incomes should be postponed
till new legislations are prepared[1].

On 19.2.1963, the articles of the Income Tax Law No. 193
referring to agricultural incomes were changed with the Law No. 202
on the recommendations of the Tax Reform Commission.

The Income Tax Law No. 193 exempted the "small" farmers
from taxation.   It accepted two criteria for the small farmer
exemption:

(a) Those cultivating a land smaller than a certain size
     which varies according to the type of produce;

(b) Those whose annual sales are under 15,000 T.L., whatever is
     the size of land they cultivate.

The Law also granted a 5,000 T.L. exception to those earning a net
income up to 10,000 T.L. above the exemption limit of 15,000 T.L.
It was expected that with this Law about 200,000 farm families would
have been brought within the general income tax schedule, and that
a revenue of around 150 million T.L. would have been obtained.

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1. M. Yaşa, "Taxation of Agricultural Land and Income", ibid,
    p. 194.

The Law No. 193 was criticized mainly on grounds that the limits of exceptions and exemptions were too low, resulting in the imposition of a heavy burden on small farmers, and that neither the taxpayers' nor the Administration's technical capacities to comply with such an extensive liability were taken into account; accordingly, the Law No. 202 increased three to four times the size of cultivated area which is the first criterion of the small farmer exemption, and increased the amount of annual sales, which is to be considered as the second criterion, from 15,000 T.L. to 40,000 T.L. The 5,000 T.L. exception limit was kept unchanged. Furthermore, while the Law No. 193 accepted a 100,000 T.L. annual sales proceeds as the dividing line between those farmers whose taxable income would be calculated on the basis of a lump sum method and those whose taxable income would be based on an accounting system, the Law No. 202 raised this limit to 150,000 T.L.

The Government estimated that the Law No. 202 would reduce the number of agricultural taxpayers from 200,000, which would have been subject to the Law No. 193, to 20,000 and provide a revenue of 100 million T.L. to the 1963 budget. But the first year's application brought about a great disappointment for the supporters of a moderate taxation who put more weight on the incentive effects of taxation than on the direct saving effects.

In fact, 18,000 new taxpayers declared a revenue of only

110 million T.L.[1] and the tax levied was 24·4 million T.L.[2].

This result forced the government to revise the Law

No. 202 and the Parliament approved the 1964 budget on the

assumption that these revisions would become legislations at the

end of the 1963 fiscal year (at the end of February 1964).   In

reality, the revision draft could become a law, the Law No. 484,

only on 26.6.1964 and brought with it two principal changes:-

(a) The land size criterion for the small farmer exemption

was reduced as much as coming closer to the provisions

of the Law No. 193.   The annual sales criterion was also

lowered from 40,000 T.L. to 30,000 T.L.   Furthermore,

the exception limit was decreased from 5,000 T.L. to

2,500 T.L. for the net profits below 10,000 T.L.   With

these changes, the tax base was enlarged and the number

of taxpayers was increased.

(b) For the farmers whose incomes are above the exemption

limits minimum taxes were assessed which would change

according to the amount and kind of their produce.

These changes have been expected to increase the revenue to

200 million T.L.[3].

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1. M. Yaşa, op. cit., p. 197.
2. Ministry of Finance, Budget Revenues Bulletin, Ankara 1965,
    pp. 63.
3. O.E.C.D.'s Economic Survey, Turkey, Paris 1964, p. 33.

The attempts so far made to tax agriculture could not be regarded as successful even if they had provided a revenue around the official expectations, since they have not been tailored to the characteristics of the Turkish agriculture and to the requirements of economic development of Turkey. Any method of taxation of agriculture in Turkey, first of all, should aim at serving as an effective tool of economic development; and this would require a careful study of the following points[1]:-

(a) the place of the agricultural sector in the economic development;

(b) relevant characteristics of the agricultural sector;

(c) the types of proprietary relationships among the farm populations; and

(d) the source of motivation for work and investment in agriculture.

Chapter 1 of this dissertation has been intended to cast some light on these points. Once reviewed from these points of view, it is not surprising at all that the above-mentioned attempts have resulted in failure. Such a review, which we are about to start, will also show that taxation of agricultural land would suit best

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1. Papers and Proceedings of the Conference on Agricultural Taxation and Economic Development, H. P. Wald (ed.), Camb. Mass. 1954.

to the requirements of economic development in Turkey.

The dominant place of the agricultural sector in Turkish economy has time and again been pointed out in this essay, and it is a corollary of this fact that a sizeable contribution to the Development Plan would have to be obtained from the agricultural sector despite the low level of average per capita income in that sector. As Mr. Kaldor puts it, "if agriculture were to make a genuine contribution to economic development, which would make it possible to expand investment and industrial production without creating inflation, and if the official estimates on the net product of agriculture are anywhere near correct, its contribution to direct taxation should be nearer to T.L.1,000 million than to T.L.100 million[1]". This would mean a burden of direct taxation on agriculture around 5-6% of its income, whereas the burden of direct taxation on all other activities is about 12·5%

Turkish agriculture is characterized by the dominance of food crops and subsistence farming which makes it difficult both to assess incomes accurately and to collect taxes. Moreover, the great degree of illiteracy prevailing in this sector is an important barrier for an income taxation to rely on self-assessment and

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1. N. Kaldor, Report on the Turkish Tax System, mimeographed by the S.P.O., 1962.

maintenance of records.   These difficulties would no doubt make

for higher exemption limits, even if not as high as in Law No. 202,

in any agricultural income tax.   Furthermore, self-assessment

requires a high degree of tax morale which is obviously lacking

in the Turkish agricultural sector.   The striking evidence of

this is the fact that, in 1963, 18,000 top-earning farm families

declared only a revenue of 110 million T.L., which on average

means about 500 T.L. per month, i.e., less than the monthly salary

of a modest civil servant.   As a matter of fact, it is evident

from Table 4 in chapter 1 that these families altogether own

almost 1/5th of the total cultivated area.   Assuming that their

share in the total agricultural income is around their share in

the total cultivated area - we are neglecting the favourable

effect on productivity of elimination of indivisibilities in

large holdings - they altogether must have an annual income of

3,000 - 4,000 million T.L.   Even if we assume that they share their

income half and half with sharecroppers and tenants, their income

tax returns must have shown a total income around 1,500 - 2,000 mil-

lion T.L., but certainly not around 110 million T.L.   The huge

difference could be attributed to two factors or to a combination

of them: they have either concealed the true amount of their

earnings or handled the resources available to them in a surpri-

singly unproductive manner.   It is therefore necessary to have a

method of taxation of agriculture which would not be easy to evade
and which would penalize the inefficient farmers.   Such a method
of taxation was recommended by Nicholas Kaldor in his Report on
the Turkish Tax System submitted to the Prime Minister on
April 21st, 1962.

According to Mr. Kaldor, a successful taxation of the
agricultural sector in Turkey can be realized by means of an
agricultural land tax.   The tax would be levied on the "potential
output" rather than on the actual output of any piece of land[1].
A "basic value" of land per hectare for each of the 67 provinces
of the country can be obtained by dividing the net product of each
province, which is estimated as defined for the purpose of national
accounting, by the number of "cultivable" hectares[2] in the province.
The next step is to determine the individual value of each hectare
of land in the province by taking into account all the factors
such as average annual rain-fall, irrigation, slope or inclination
of the land, porousness, etc., but not the value of crops or the
type of crop actually produced, except in the case of horticulture

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1. By "potential output", it is meant the output which the land would
    yield if it were managed with average efficiency.
2. "Cultivable hectares" cover those lands which are either actually
    producing crops or could be brought into cultivation without any
    large capital outlays.

and viniculture where the land should be valued on the basis of the crop.   Once the relationship between the individual value of each hectare of land and the "basic value" for the province is established, it will serve as a permanent yardstick of the potential output of each hectare.   Only by revising the "basic values" as a moving average of the net value of the output of the province in the last five years, the system could be kept up to date in relation to variations both in the output and in the average level of prices without reassessing the individual pieces of land.

The system recommended by Mr. Kaldor has numerous advantages over the method of taxing agricultural incomes within the general income tax scheme as in Law No. 193 and its versions.   It is, first of all, possible to raise the revenue needed for the Five-Year Development Plan with a land tax described above without putting an exorbitant burden on the taxpayers.   A 1,000 million T.L. revenue, or about 6% of the net agricultural product, could be obtained from such a land tax by taxing only those families owning more than 10 hectares of land who constitute only about 16% of the total farm families but possess about 60% of the total cultivated area.   Even on them, the burden of the land tax would not be more than 10% of the net product of the land, assuming that the average productivity of the land does not vary with the size of landholdings.

Once the preliminary requirements have been fulfilled, the administration of the land tax would be easier than that of an agricultural personal income tax[1]; it would not also require any particular technical capacity on the part of taxpayers. Moreover, the taxpayers would not be able to evade the land tax since its base cannot be concealed.

It has been pointed out in chapter 1 that the existing proprietary relationships among farming population account for the low productivity in agriculture and that the number of farmers without land or with inadequate land creates an important social problem. Since the prospects for a land reform in Turkey are very remote, some contribution to the betterment of the proprietary relationships needs to be done by the tax system. Neither Law No. 193 nor its revised versions could have any favourable effect in this respect. Farming income and the absentee landlord's income are not subject to differential treatment. These laws do not contain any deterrent to the increasing concentration of

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1. It is true that the application of a land tax of Kaldor type would require the valuation of each hectare of land in the country and this would be an expensive task in terms of both resources and time. But it is of a once-and-all character and would provide useful data for many considerations other than taxation. Prof. B. Hansen, however, thinks that the same economic results could be obtained with the present land tax, which is levied on the rental value, if the tax base is freed of erosion and increased accordingly. (H. Kizílyalli, ibid., p. 40).

ownership. Instead, they have every kind of incentives for the big landlords[1]. On the contrary, a land tax of the type recommended by Kaldor would work in the direction of lessening the inequality in distribution of land. Since its base would be the potential output of land, it would penalise the absentee land-lords and the inefficient farmers[2]. Graduation of tax rates would augment these favourable effects. Graduation of tax rates could be accorded to the system not only on the basis of the size of landholdings of a family but of the total value of holdings as well. Even without imposing a rate of progression of "penal" character, favourable effects could be had on the distribution of land-ownership with a moderate rate of progression. Mr. Kaldor, for example, suggests that, if the holdings between 10 and 50 hectares are taxed at 10% and the holdings above 50 hectares at 15%,

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1. In addition to the minimum subsistence allowance and to the
    5000 T.L. agricultural income allowance, the consumption
    expenditures of the family are also deducted from the agricul-
    tural income. Capital gains are not taxed. Those whose
    taxable income is calculated by presumptive methods do not
    have to add their non-agricultural incomes to their agricul-
    tural income. The total amount of investment required to
    benefit by the investment allowance is 50,000 T.L. in
    agriculture whereas it is 250,000 T.L. in the non-agricultural
    investments. (H. Kizilyalli, ibid., p. 31-39).

2. The "penalty" would fall on landlords if the further
    exploitation of tenant cultivators by landlords is prevented
    by legislation.

a man who ownes 55 hectares might prefer to sell rather than keep

5 hectares since the tax on his last 5 hectares would work out

at $15 + \frac{250}{5} = 65\%$[1], provided that the tax schedule is expressed in

terms of effective rates and not marginal rates.

III

TAXATION OF INCOMES, PROFITS, and WEALTH

In Turkey, today, all kinds of personal incomes are subject

to a unitary income tax, the coverage of which has recently been extended

so as to include agricultural incomes and the incomes of artisans

and small traders. Incorporated businesses' profits are subject

to a corporation Tax. Furthermore, there are some taxes on

wealth such as Inheritance and Transfer Tax, Building Tax and Land

Tax, but they play, as we shall see below, an insignificant role

today owing to the effects of inflation and of their structural

defects.

A. Taxation of Personal Income: As seen from Tables 29

and 29a the income tax is the largest-revenue-raising tax in the

Turkish Tax system, though its share in the total tax revenue has

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1. A similar suggestion of using the land tax for land reform
    purposes is made by I.M.D. Little in "Tax Policy and the Third
    Plan", published in Pricing & Fiscal Policies, P. N. Rosenskin-
    Rodan (ed.), London 1964, p. 39.

somewhat declined since 1960. Its coverage in terms of the
numbers of taxpayers is very much limited when compared with that
in the advanced countries[1]. About 30% of the national income is
assessed to the income tax[2]. This ratio is around 75% in the
U.K., but only 10-20% in the Caribbean and something of the order
of 5% or less in African territories[3].

We have already seen that a remarkable feature of the
taxation system of Turkey in the 1950-62 period has been the almost
constant share of taxes in national income. It is necessary to
seek if the low income elasticity of tax revenue in Turkey is due
to the unresponsiveness of the income tax. In Table 30 below, we
relate the revenue from income tax to the non-agricultural net
national product, since agricultural incomes have not been subject
to the income tax until 1963. Income tax revenue in money terms
has recorded about a ten-fold increase in the period 1951-1962.
However, much of the increase has been due to the rising prices and
to the increase in the number of taxpayers as a result of the

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1. In 1963, 3,848,633 persons paid income tax. (Ministry of Finance,
   Budget Revenues Bull., 1964, p. 55). This corresponds to about
   12% of total population. This ratio is of the order of 30-40%
   in the U.S.A. and U.K., but 2-3% in the Carribean and 1-2% in
   Africa and Asian Countries. (A. R. Prest, Public Finance in
   Underdeveloped Countries, London 1962, p. 28).
2. We are caught by the lack of data about the amount of the assessed
   incomes of wage and salary earners. According to Kaldor they
   altogether amount to 11,500 million. Adding to this 3,000 mil-
   lion T.L. income declarations in 1960 by the remaining income tax-
   payers, we find that the income tax in Turkey covers 30% of
   national income.
3. A. R. Prest, Ibid., p. 28.

TABLE 30

ELASTICITY OF THE INCOME TAX, 1952-1962.

Year	Non-Agricultural N.N.P. at current Prices (00 million T.L)	Income Tax Revenue (00 mil.T.L)	I/II %	Income Tax assessed by declarations (00 mil.T.L)	IV/I %
	I*	II	III***	IV**	V***
1951	51·3	2·1	-		
1952	62·3	3·0	5·8		
1953	74·6	3·9	6·2	1·4	2·2
1954	88·5	5·3	7·1	2·1	2·8
1955	105·8	6·5	7·3	2·6	3·0
1956	121·0	8·4	8.0	3·3	3·1
1957	146·1	9·7	8.0	3·7	3·0
1958	177·2	11·5	8.0	4·9	3·3
1959	220·3	15·6	8·8	5·4	3·0
1960	240·0	18·5	8·4	6·8	3·1
1961	246·0	20·5	8·5	7·0	2·9
1962		19·1	7·7	6·6	2·7

* Agricultural incomes were not subject to income tax till 1963.

** Assessment by declarations covers incomes from businesses, professions and properties. Tax on wage- and salary-earners is withheld at the source.

*** The calculations are made on the basis of one year lag between N.N.P. and tax revenue collections.

Sources: N.N.P. figures are from the S.P.O., Development Plan, p. 13. Income tax figures from the Ministry of Finance, Budget Revenues Bull., 1964, pp. 128-129.

growing population and of the extension of the monetized sector.
Expression of the revenue from income tax as percentage of the non-
agricultural N.N.P. as in the column III of Table 30 cancels all
these effects, and the emerging trend of the income tax ratio
reflects the following factors:-

(a) Changes in the structure of the tax;

(b) Progressiveness of the income tax rates;

(c) Changes in the distribution of income.

The only significant change in the income tax during 1952-
1962 was made in 1958 by increasing both the minimum subsistence
exemption and family allowances, on the one hand, and the progres-
siveness of the tax rates for higher incomes, on the other hand.
The income tax had a rate of progression rising from 17·5% effec-
tive rate on 5,000 T.L. annual income to 35% on 100,000 T.L. and
above, which was raised in 1958 to 50% on the incomes of 500,000
T.L. and above per annum.   During the period considered, non-
agricultural N.N.P. in money terms has increased by about 5 times
and the distribution of this income, according to a study by the
S.P.O., has changed in favour of the groups deriving their incomes
from capital and real estate at the expense of the living standards
of wage- and salary-earners[1].   Consequently, since there has not

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1. The conclusions of that study are quoted in the Development
   Plan 1963-1967, pp. 45-50.

been an increase in the share of the number of wage- and salary-earners in the total number of taxpayers[1], a growing share of the non-agricultural N.N.P. must have come under the higher rates of the income tax schedule.

In fact, the income tax ratio shown in column III of Table 30 has an increasing trend which may imply that the implementation of the progressive income tax in Turkey has been successful in transferring a growing proportion of income to the public use as the national income rises and inequality in income distribution grows. A closer study, however, will show the opposite. Although the share of income tax revenue in non-agricultural N.N.P. in 1961 was about 50% higher than the 1952 ratio, much of the increase, i.e., about 40%, was achieved between 1952-1956. On the other hand, the 1962 ratio was even lower than the 1956 ratio. The incremental income tax ratio (the ratio of the increase in the income tax revenue to the increase in the non-agricultural N.N.P.) was 9·6% for 1952-56 and fell to 7·6% in 1956-1962 in spite of the

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1. We do not have accurate data about the number of wage- and salary-earners who pay income tax. But we understand from the data on civil servants given in the statistical Yearbook 1964 of the State Institute of Statistics that in no public service has the number of employees more than doubled in 1952-1962. As for the number of wage-earners, we have seen that the number of non-agricultural workers increased by about 5% p.a., in the 1950's (Chapter 1). On the other hand, the number of taxpayers whose liabilities are based on their declarations rose from 72,318 in 1953 to 304,601 in 1962, recording a more than four-fold increase.

facts that the non-agricultural N.N.P. increased by 11·3% in the

period 1955-61 and that the above-listed three factors did not

account for such a drop.   The drop could be explained better if

we divide the income tax revenue into its two components, namely,

the revenue from the taxpayers who derive their incomes from wages

and salary, and the revenue from those whose incomes come mainly

from businesses, professions and properties and whose liabilities

are assessed on the basis of self-assessment (of their declarations).

The latter is shown as absolute amounts in column IV of Table 30 and

as percentages of non-agricultural N.N.P. in column V.   It appears

that the share of the revenue from the income tax declarations in

the non-agricultural N.N.P. had slowly risen till 1958 and then

gradually declined, the 1962 ratio being lower than the 1954 ratio.

This decline has not been effected by any deterioration in the

relative incomes of this category of taxpayers.   No deliberate

policy measures have been taken to affect the distribution of

income in favour of wage and salary-earners.   If such an effect

were produced by the overall development of the economy, a similar

effect within the sector of businesses, properties and professions

would have operated in favour of low income groups.   But an obser-

vation of the data about the income tax declarations shows that in

1952-1962 there has been no significant change in the shares of

low and high income classes both in the total number of and revenue

from the declarations[1].   We therefore have to come to the conclu-
sion that tax evasion has been taking place on a large scale, and
creating, particularly since 1957, a setback in the way of effect-
ive functioning of the income tax[2].   Since wide-spread tax evasion
in a country is the result of deficiencies in tax-morale and in
fiscal administration and since these are deep-rooted problems in
Turkey which cannot be remedied in the short-run, it can be
reasonably assumed that the tax evasion will continue to be a set-
back even after the First Five-Year Plan.

We had indicated in Section II above that in the pre-plan
period agricultural incomes escaped the income tax completely.
We also pointed in this section to the low income-elasticity of

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1. The data given in the 1964 Budget Preamble show that the
    share of the taxpayers who declared an income under
    17501 T.L. in the total number of taxpayers was 88% in
    1953, 86% in 1957 and 86% in 1962 and in the total declared
    income was 34%, 31% and 30% in respective years.

2. In connection with the scale of tax evasion, it is significant
    to note the following facts:-
    (a) between 1953 and 1962, the average per capita income tax
        assessed according to declarations increased by only 3%
        per annum, while in the same period the average annual
        increase of G.N.P. (minus agriculture) was 12% in current
        prices (O.E.C.D., "Turkey 1964", Paris Aug. 1964, pp.32-
        33); and
    (b) according to the declarations, the average income of this
        category taxpayers in real terms have fallen from 10,371
        T.L., in 1953 to 6,845 T.L. in 1957 and to 4,422 T.L. in
        1962.   (I deflated the income figures given in the 1963
        Budget Proposal with the wholesale price index given in
        the Development Plan).

the tax and to the large-scale tax evasion in that period.   These are of course not the only problems of the income tax of the pre-plan period but are surely the essential ones which one must bear in mind when making suggestions with respect to the income tax in the plan period.

The basic structure of Turkish Income Tax reform in 1949 was formed on the German model.   There has been no fundamental change in the income tax system in the pre-plan period.   When the tax was developed, economic development was not the dominant aim of public policy.   Nor is the German pattern of income taxation suited to the very different conditions prevailing in Turkey.   One would have expected, therefore, that steps would have been taken at the outset of the development planning to reform the system of income taxation.   Significant changes, indeed, were made with Law No. 193 at the end of 1961.   A Taxation Reform Commission (T.R.C.) was appointed in 1961 and in 1962 Mr. Kaldor was called in as a consultant to suggest reforms in the tax system. Mr. Kaldor suggested fundamental changes in the structure of direct taxation but they were not accepted by the Turkish Government.   On the other hand, the government, acting on the recommendations of the T.R.C. Report, introduced with Law No. 202 such amendments to the Income Tax Law No. 193 that the latter has almost completely lost its essential features.

The main factors effecting the Income Tax Law No. 193 were the need, on the one hand, to increase the tax revenue, and, on the other, to correct the distribution of the tax burden distorted by inflation in the 1950's. With these purposes, the progression of the income tax rates was mitigated for low income groups and increased for the high incomes; the personal allowances were increased; high agricultural incomes were brought within the tax net; the exemption limit for small traders was lowered; the time period during which transactions in real estate /cannot escape tax liability was extended from 2 years to 4 years; an obligation of wealth declaration was imposed on those taxpayers whose income tax liabilities are assessed on the basis of the tax returns.

Mr. Kaldor, in addition to his proposal of a land tax in place of the agricultural income tax, suggested further steps which would bring the capital gains within the tax net and which would make tax evasion more difficult.

The Income Tax Law No. 193 had had a chance of application for only a year and in 1963 was revised substantially with Law No. 202 which introduced the following main changes: the rate of progression of the whole income tax schedule was reduced; the personal allowances were further increased; the limits for the small farmer exemption were raised; the assurance was given that

wealth declarations would not be used with a purpose of investiga-

tion of any matter prior to their first submission; incentives

were given to the investors mainly in the form of investment

allowances and accelerated depreciations.

It is neither possible nor pertinent to our task to discuss

the relative merits of all kinds of the above-mentioned schemes.

For our purpose, it will suffice to examine critically those

aspects of the present income tax which might have considerable

effects on the aggregate savings; and, in this connection, we

shall deal with its progressiveness and its incentive features.

The income tax has a fairly steep rate of graduation.   The

rates of taxation in force since 1950 are given in Tables 31 and

32.   It will be seen from these tables that the minimum rate of

income tax (10%) is applicable to an annual income of 2,500 T.L.

and that the maximum rate (60%) is made applicable above the level

of 1,000,000 T.L.   In the low income ranges the tax rates are

sharply progressive, rising from nil at 1080 T.L. income to 14·1%

at 10,000 T.L. income.   This means a marginal tax rate of 15·8%

for the first 10,000 T.L. income.   For the additional incomes

marginal tax rates are increasing but not at any definite pace.

This is observable from the slope of the dotted line in Diagram 5

and 5a.   However, it is conspicuous that the curve representing

TABLE 31

INCOME TAX RATES APPLIED SINCE 1950

Law No	Period of Implementation.	10%	15%	20%	25%	30%	35%	40%	45%
5421	1/1/1950	-	2,500	5,000	10,000	20,000	20,000	20,000	22,500
6908	1/1/1958	-	2,500	5,000	10,000	20,000	20,000	20,000	22,500
193	1/1/1962	2,500	-	7,500	-	15,000	-	30,000	-
202	1/1/1963	2,500	2,500	5,000	15,000	-	30,000	-	60,000

Law No	Period of Implementation.	50%	55%	60%	65%	68%	70%
5421	1/1/1950	-	-	-	-	-	-
6908	1/1/1958	25,000	50,000	125,000	-	-	-
193	1/1/1962	70,000	-	157,500	-	-	217,500
202	1/1/1963	-	150,000	225,000	225,000	285,000	-

Fixed Rates:-

In the Law No. 5421, 35% on the incomes over 100,000 T.L.

" " " " 6908, 50% " " " " 300,000 T.L.

" " " " 193, 60% " " " " 500,000 T.L.

" " " " 202, 60% " " " " 1,000,000 T.L.

Source: Ministry of Finance, Budget Revenues Bull.
1964, p. 132.

TABLE 32

EFFECTIVE AND MARGINAL RATES IN THE PRESENT INCOME TAX
(LAW NO. 202)

Income Ranges	Effective Rates %	Marginal Rates %
1,080	Nil	-
10,000	14·1	15·8
20,000	19·2	24·4
30,000	23·3	28·9
50,000	28·2	36·8
90,000	34·6	42·5
150,000	41·0	50·0
200,000	44·5	55·0
300,000	48·6	56·7
500,000	53·2	60·2
1,000,000	60·0	66·6
Above 1,000,000	60·0	60·0

Source: Calculated on the basis of information
given in Table 31 above.
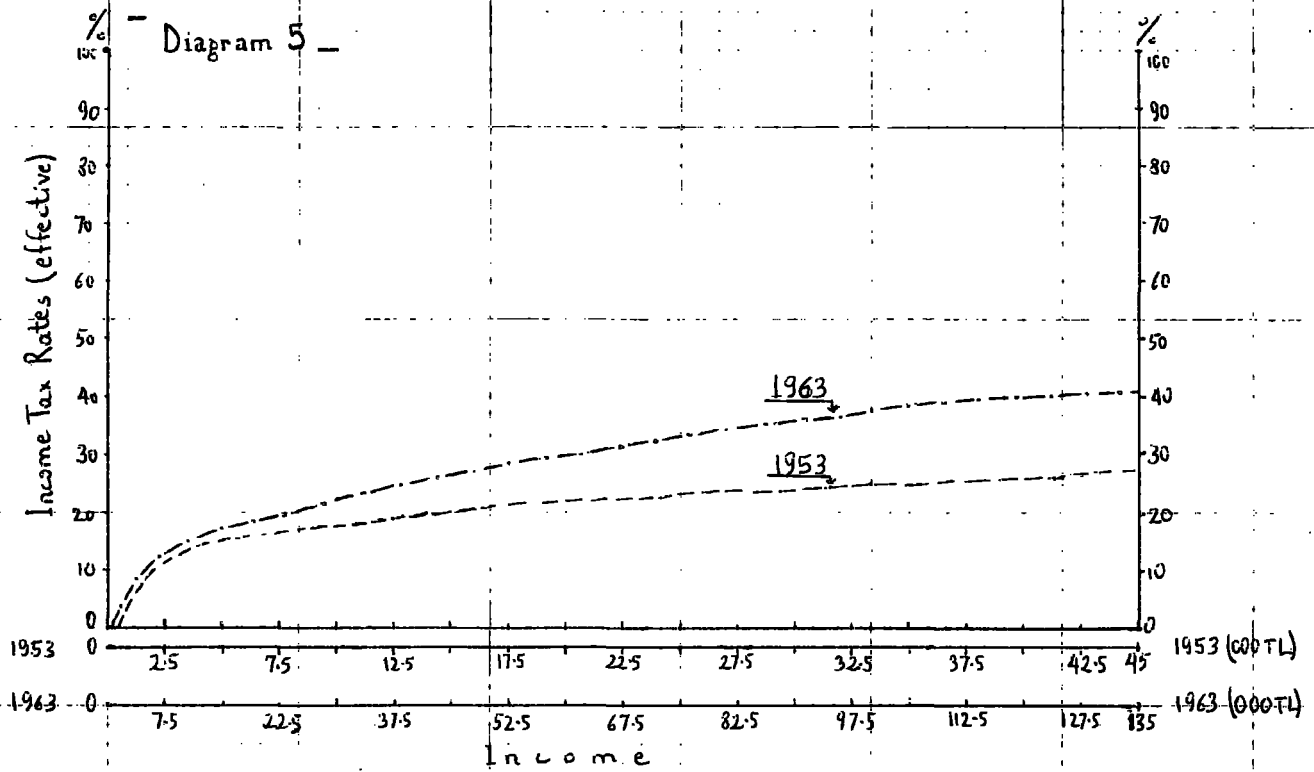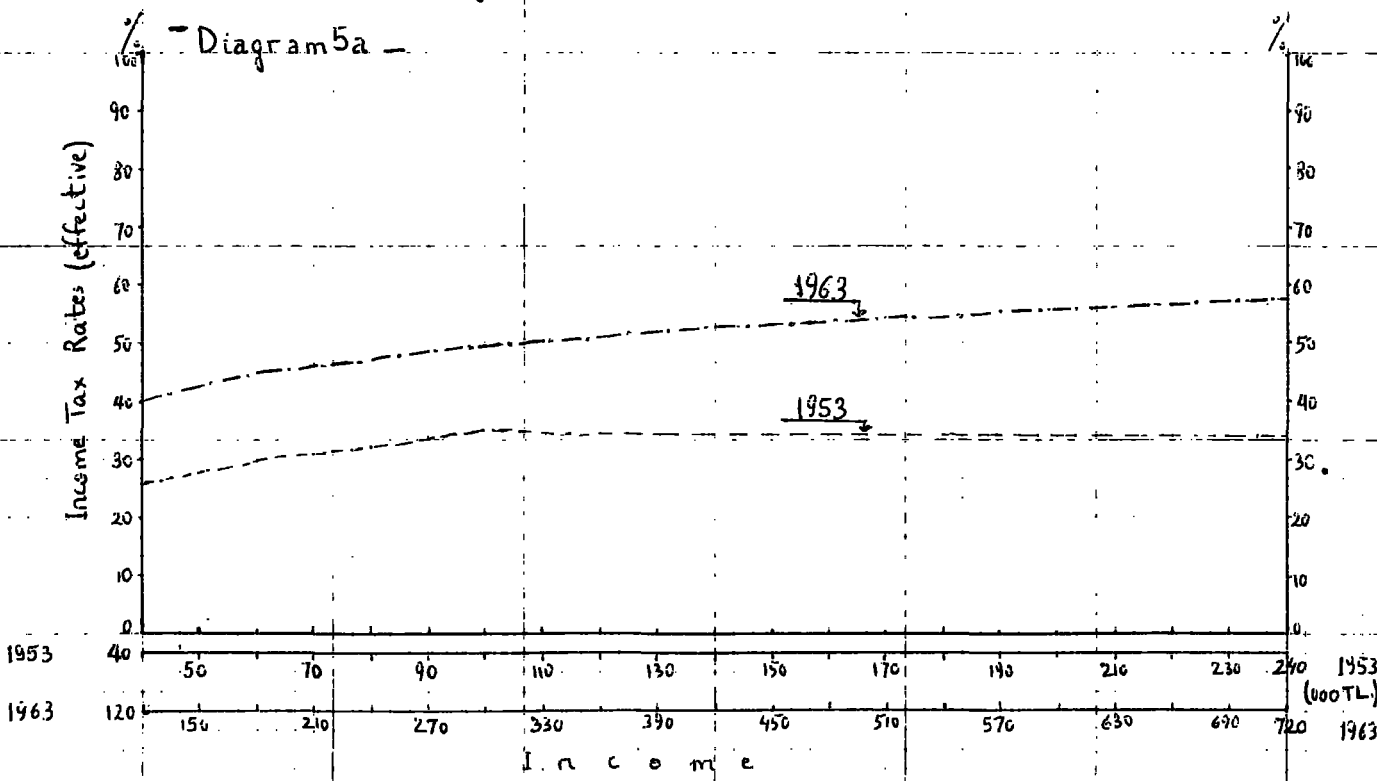
Diagram 5 & 5a – Progressiveness of the Turkish Income Tax in 1953 and 1963.

Note: The personal allowance was 540 TL in 1953 and 1,080 TL in 1963.

Sources: Both figures have been drawn on the basis of the information given in Table 31 above.

the effective tax rates on various income ranges is rising

relatively steeply up to around 100,000 T.L. annual income and

then flattening, particularly after 400,000 T.L. income[1]. This

observation points to an important feature of the income tax,

that is, the increases in tax burden get smaller as one moves up

from lower to higher income ranges. This is no doubt the

opposite of what should have been if the income tax is to contri-

bute to the realization of the Plan's objective that a more

equitable distribution of income will be approached in the Plan

period. Nevertheless, if one entertains the view that high

income groups have a greater marginal propensity to save than low

income groups, the present income tax schedule seems to be

favourable to the high-savers. But there is in Turkey no evi-

dence in support of this view[2]. In fact, the examples of rich

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1. The relatively high rate of progression in the lower end of
   the income scale would have been more apparent if Diagram 5
   and Diagram 5a. had been drawn on the same scale instead of
   the former's scale being 1/4th of the latter's.

2. In Turkey, no data on the saving propensitives of various
   income classes. have so far been available through family
   budget studies. Only in a few underdeveloped countries,
   e.g., Puerto Rico and Delhi, scientifically designed sample
   surveys of this kind have been conducted. They indicate
   negative saving ratios in the lowest income classes and in-
   creasing saving ratios in higher income classes. These data,
   however, measure average rather than marginal propensity to
   save. If saving is a linear function of income and the inter-
   cept of the saving curve is negative, saving will be a larger
   fraction of high incomes than of low incomes, but the M.P.s will
   be the same for all income levels. Under these conditions the
   degree of progressivity will not affect the amount of private
   saving. (R. Goode, Taxation of saving and consumption in Under-
   developed Countries, National Tax Journal, December 1961.)

spendthrifts could be met more frequently than those of rich
high-savers.   Furthermore, in a country like Turkey, where a
considerable portion of the private sector savings is invested
with speculative purposes, it would be wiser to treat favourably
only those savings put into desirable uses rather than the whole
savings.   It therefore seems reasonable to suggest that the
effective tax rates on incomes above, say,100,000 T.L. be raised
so as to attain present highest rate at 500,000 T.L. instead of
1,000,000 T.L. and 70% at 1,000,000 T.L. and over.   If the
increases in the tax rates applied to higher incomes are incor-
porated with a generous treatment of savings directed towards the
uses conducive to the realization of the Plan's objectives, there
would not be much ground for the criticisms that high income tax
rates cut deeply into the return on savings and on risk-taking.
Such an increase seems appropriate also on the grounds of inter-
temporal and international comparisons.

The present income tax has surely gone some way towards
increasing the tax burdens of high - as well as low - income
classes as compared with the income tax of the 1950's.   As will
be seen from Diagram 5&5a, the curve representing the effective
tax rates at various income levels in 1963 lies above the similar
line of 1953 throughout the whole income scale.   As the income
scales of the two curves have so been adjusted that the corres-

ponding points on the two scales represent those incomes standing at

the same relation to the per capita G.N.P. in the respective years[1],

it is obvious from the Chart that in 1963 every person pays a greater

percentage of his income in income tax than his counterpart did in

1953. The rate of progression, however, has been increased more for

those in the lower end of the income scale than others. This is

manifested by the chart as the two curves diverge glaringly up to

around 100000 T.L. (in 1963) annual income; thereafter become almost

parallel to each other up to about 300,000 T.L. (in 1963), and diverge

again but at a less degree than the former divergence.

How does the graduation of the Turkish income tax compare

with that of the American, British and Indian income taxes.? Diagram 6

and 6a provide us with such a comparison between the U.S., U.K. and

Turkey. Once again, the income scales for each country's curve have

so been adjusted to each other that the corresponding points on the

three income scales represent those incomes in each country which stand

at the same relation to the per capita G.N.P. of the respective country[2].

The Chart does not aim at comparing the tax burden of a Turkish tax-

payer with a certain income with that of a British or American taxpayer

with an equal income. Instead, it shows comparatively how the relative

tax burden changes in each country as one moves up along the income

1. See the note to Diagram 5 and 5a.
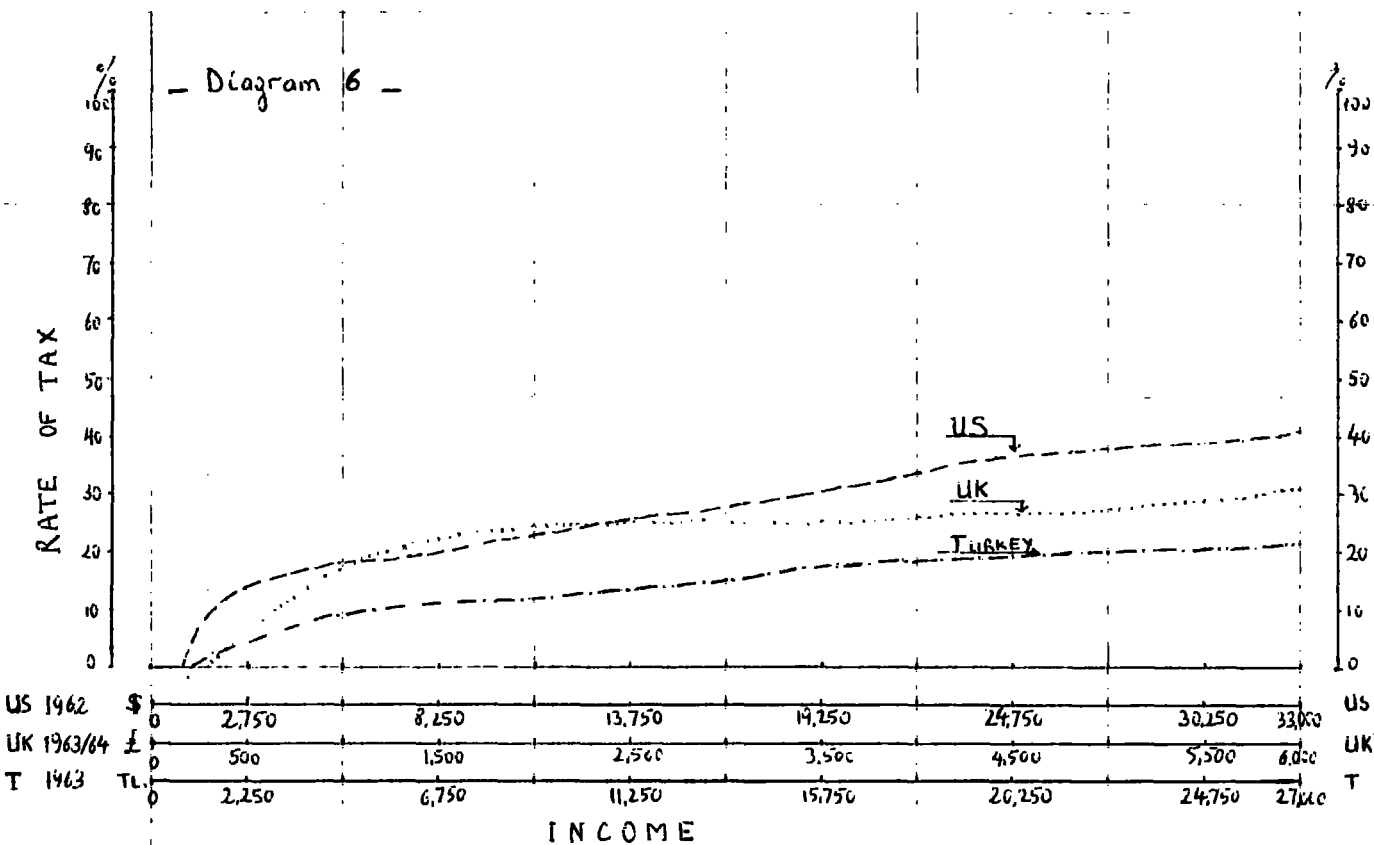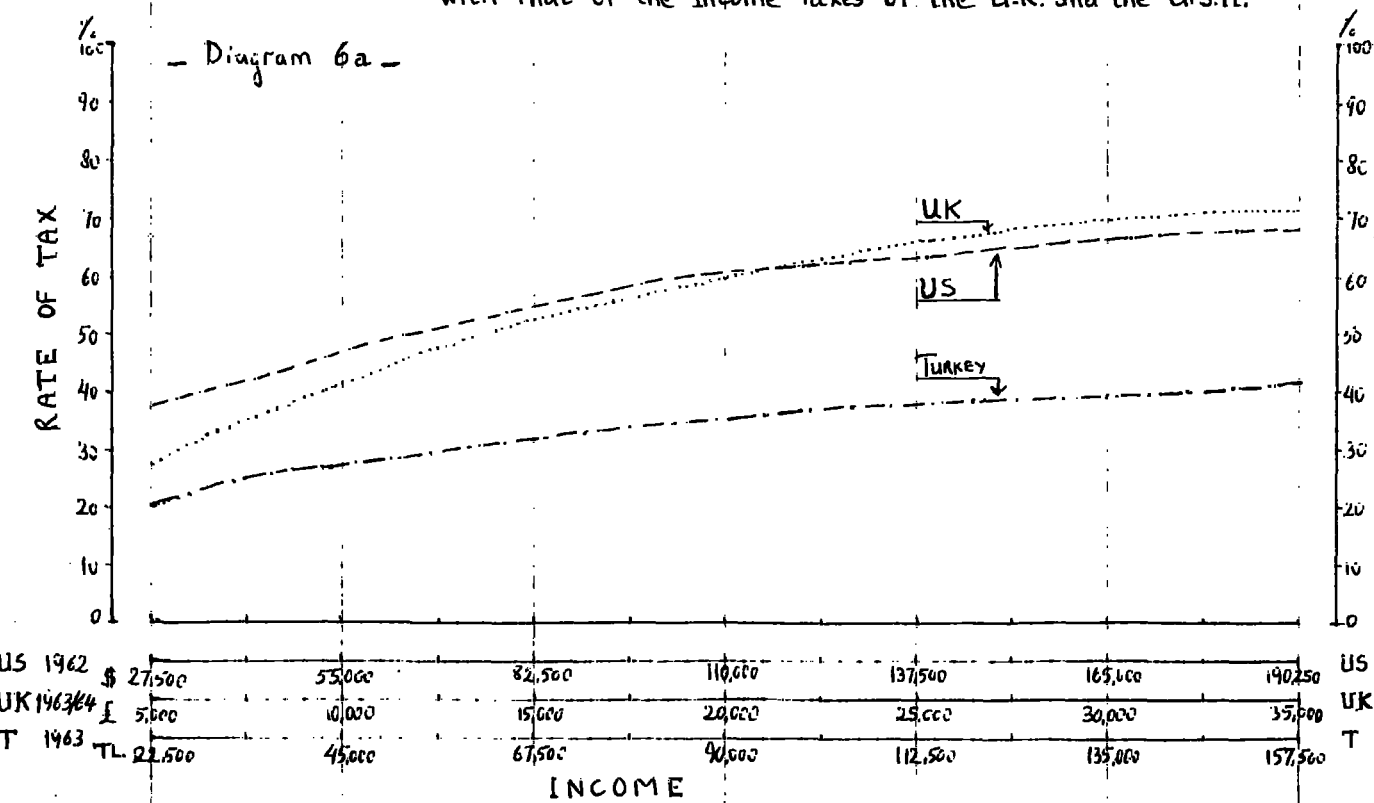
2. See the note to Diagram 6 and 6a.

Diagram 6 & 6a — Progressiveness of the Turkish Income Tax as Compared with That of the Income Taxes of the U.K. and the U.S.A.

Note on the preparation of the diagrams:-

The curve representing the Turkish Income tax has been drawn on the basis of Table 31 above.

The curves representing the American and British Income Taxes have been taken from A. R. Prest, Public Finance in Theory & Practice, pp.

The income scales have been adjusted in relation to each other according to the per capita gross national incomes in national currencies at current prices. Thus, corresponding points on the three scales represent different levels of incomes but these incomes stand at the same position in relation to the per capita income. That is to say, for instance, incomes of 9,000 T.L., £2,000 and $11,000 are 4.5 times the per capita incomes in the relevant countries.

The per capita incomes were calculated on the basis of the national income and population data given in the Turkish Statistical Yearbook 1964. They are 2,050 T.L.; £450; and $2,250.

scale. The Turkish income tax is less progressive for the incomes

below 5,000 T.L. than the British income tax[1]. However, in the

income ranges between 5,000 T.L. and 25,000 T.L. the Turkish tax

is more progressive than the British. Above the 25,000 T.L.

incomes the Turkish income tax becomes increasingly less progressive

than the British income tax up to 157,500 T.L. which is apparent

from the increasing divergence of the two curves in Diagram 6a.

It is significant to notice that in the British income tax an

effective rate of 60% is applicable to an income of £20,000, which

is less than 50 times the percapita G.N.P., the same rate in Turkey

is applied to an income of 1,000,000 T.L., which is about 500 times

the percapita G.N.P. in Turkey. A similar comparison can be carried

out between the U.S. and Turkey. At the very start the American

schedule is much more progressive than the Turkish, but the situa-

tion shortly turns to that the American schedule is only a little

more progressive than the Turkish schedule up to 20,000 T.L.; and,

thereafter the former becomes much more progressive up to an income

around 100,000 T.L. Above 100,000 T.L. incomes the difference in

the rate of graduation disappears until the American income tax stops

being progressive.

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1. The comparison is between the incomes in Turkey under 5,000 T.L.
    and the incomes in the U.K. situated similarly, that is, between
    the incomes being of the same percentage of the per capita
    G.N.P.'s. In order to simplify the explanations the comparison
    will be conducted only in terms of Turkish incomes.

In India[1] personal incomes are subject to three different taxes, namely, the income tax, the super tax and the surcharge, which also are supplemented by an expenditure tax on the personal spendable income above a certain amount and an annual wealth tax. The income tax, super tax, and surcharge together result in a highest effective rate of 74·4% (a marginal rate of 77%) on an earned income of Rs. 1,000,000. On the other hand, the first Rs. 2,000 of taxable income is taxed at a low rate of 3%. Unearned income is discriminated against through higher rates of surcharge. The Indian tax system operates with much lower rates than the Turkish system in the lower end of the income scale. An Indian with an income about 10 times the per capita G.N.P.[2], i.e., Rs. 3,600, is charged at an effective rate of 2·2% while a similarly situated Turk would be liable at a rate of about 21%. On the other hand, the higher rates of taxes become effective at relatively higher levels of incomes in the Indian income tax than in the Turkish; however, the former operates with considerably higher tax rates at the upper end of the income scale.

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1. The source of information about the taxation of incomes in India is R. J. Chelliah, Fiscal Policy in Underdeveloped Countries, London 1960, pp. 111-114.

2. As I calculated on the basis of the information given in the U.N., 1964 Statistical Yearbook the per capita G.N.P. was Rs. 345 in 1963.

The personal allowances in the Turkish income tax are very

low by international standards[1].   In Western countries, the

personal allowance for a single person is so set as to extend the

tax net to the lower ranges of clerical workers and the top ranges

of manual workers[2].   The Turkish Income Tax works with an annual

allowance of 1,080 T.L. (£43) for a single person, which is equal

only 1/6th of the annual income of an average worker[3], (certainly

less than half of the income of the lowest paid unskilled labourer).

This is an important element making for the relatively higher

progressiveness of the income tax in the lower income ranges.   A

married taxpayer benefits by an additional family allowance of

720 T.L. and by another allowance of 360 T.L. for each child.

Under the Law No. 202, from 1/1/1966 the personal allowance was

revised to 1,800 T.L., the family allowance to 1,080 T.L., and the

allowance for each child to 720 T.L.   These increases will no

doubt ease the tax burden on the low-income classes.   But they

will also mitigate the tax burden on those who are not burdened

adequately.   It is difficult to see the point, particularly,

behind the rise in the children allowance.   The tax relief to a

1. N. Kaldor, Report on the Turkish Tax System. He does not,
    however, give any concrete comparison.

2. U.K. Hicks, Development Finance, Oxford 1965, pp. 91-92.

3. According to the figures of the Worker's Insurance Institution
    the average daily income of insured workers was 17·91 T.L. in
    1963. (The S.P.O., 1965 Annual Programme, p. 32).

family by such an allowance bears no relation to the expenses of
bringing up a child. Furthermore, the economic conditions compel
the children of the lower-income families to earn their living at
a young age, and, thus, the allowance for a child becomes another
element accounting for inadequate progressiveness of the tax at
higher income levels. Moreover, it seems unreasonable to offer a
tax allowance for a child in a country where the rapid increase in
population is one of the basic obstacles to economic development
and where the government engages in birth control[1].

Let us now have a brief look at the incentive features of
the Turkish income tax. The present income tax contains incentive
measures in the form of accelerated depreciation, investment
allowance, higher exemption limit and tax holiday, offsetting the
losses from other profits, and exemption of capital gains[2].

The usual method of depreciation accepted by the Turkish
income tax is the writing off of the normal wear and tear on the
basis of the current book value (historical value) of the fixed

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1. U.K. Hicks, op. cit., pp. 91. A similar remark is also made
   by A. R. Prest in his "A Fiscal Survey of the British Caribbean,
   London 1957, p. 29.

2. The provisions of the Income Tax concerning these allowances
   are also applicable to the corporations subject to the
   Corporation Tax.

capital. With Law No. 205, the Law on the Taxation Procedure, dated 19/2/1963, it was left to the discretion of the taxpayer whose income is assessed on the basis of his balance sheet[1] to choose between the normal wear and tear allowance and the declining balance method of depreciation at a rate[2] twice as high as the rate which would have been applied under the normal method of depreciation.

Investment allowance is a recently introduced measure in Turkey. Since 1963, 30% of investment expenditure made in commerce and industry (including tourism) may be deducted from taxable income, provided that the investment projects have gained the approval of the S.P.O. This percentage is increased to 40% in case of agricultural investment and to 50% in underdeveloped regions. The advantages of the allowance are, however, enjoyed only for investments of at least 250,000 T.L. values (125,000 T.L. in agricultural investments) by the taxpayer whose income is assessed on the balance sheet basis, irrespective of the source of investment funds, i.e., allowance is given for the investments financed by bank credit as well as by retained profits.

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1. The assessment of tax liability on the balance sheet basis is applied to those taxpayers whose annual purchases are more than 400,000 T.L. or whose annual sales are above 440,000 T.L.

2. This rate, however, cannot be higher than 25% p.a.

Income Tax offers favourable treatment to the revenue from real estate. While only 1,080 T.L. out of the annual income of an unmarried wage or salary earner is exempt from the income tax, if a real estate provides an annual revenue less than 5,000 T.L. it is completely exempted from the income tax. Moreover, the tax liability on a building arising from the Building Tax, can be deducted from the income tax levied on the income of the building. Furthermore, if a building is enjoying a "tax holiday" in the context of the Building Tax, the tax liability on the building which would have been due under the Building Tax can be deducted from the income tax liability on the revenue from the building as if it had been taxed by that amount. This is another way of inserting a "tax holiday" concession into the income tax for the revenue from buildings as in the Building Tax where the new buildings were until recently exempt from the tax for ten years without any regard to the kind of building but at present the ten-year tax holiday applies only to the houses built for social purposes and a five-year exemption to the residential buildings of unluxury type and to the construction for tourism.

The present income tax makes it possible for a taxpayer to offset his losses from some activities completely against other profits. If, on the balance, he is still in loss he can take the advantage of deducting his losses from the following years' profits,

provided that the carry-over is completed in five years.

The gains from the transactions in real estates are subject to income tax only if they are more than 10,000 T.L. and if the realization takes place within the 4 year time span from the purchase of the real estate.

To what extent might these incentive measures lead to an increase in the aggregate savings and mitigate the discrimination against risky enterprises inherent in any income tax ?   It is argued that in the period of rising prices the method of writing off the capital assets on the basis of book values results in the appearance of a part of the capital as profits, and, hence, in the transfer of a part of capital to the owner of the business, the customers, the other productive factors and the government[1]. As a corollary of this argument it is suggested that there will not be sufficient funds to replace the capital assets.   It is not, however, reasonable to suppose that the businessmen would determine their policies on the basis of a false picture of profits[2].   Also, "there is no holy writ that replacement of

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1. H. Kīzilyalli, op. cit., pp. 85-87.

2. It is true that the method of depreciation on the original cost basis has distorted the investment and pricing policies of the S.E.E. and caused the transfer of a part of their capital to the private sector through underpricing of commodities, this is due to the failure of the management rather than to the depreciation method.

capital equipment can only be met from accumulated depreciation funds[1]. Although the taxable income will be enlarged as much as the difference between the original and replacement cost, this could be considered the taxation of capital gains accruing to the firm as its existing assets gradually increase in value in the period of rising prices.

The provision introduced by Law No. 205 allows enterprises to write off a greater proportion of a capital asset in the early years of its life span. This will, in the first instance, reduce the scope for concealed taxation of capital gains, and, secondly, postpone some tax liabilities. The former would lead to an increase in the aggregate savings only if the reduction in the tax revenue is more than offset by the consequent increase in the private savings. The latter would influence investment in two ways: first, it increases the ability of firms to expand by increasing the liquid assets at their disposal, and second, it reduces the risk to the capital investment arising from progressive income taxation. Neither of these influences would lead to an immediate increase in aggregate savings, though they may lead to an

1. A. R. Prest, Public Finance in Practice and Theory, London 1960, pp. 310-11. Dr. Prest also there demonstrates how a firm with a growing stock of capital may always spare adequate funds for replacement unless the outflow due to the price rise is more than sufficient to offset the inflow due to net investment.

increase in savings through increasing output.   But there is no
reason to believe that the resultant increase in output, and hence
in savings, would be greater than what it would have been if the
government savings had not been reduced by the accelerated
depreciation allowance.   Moreover, the liquidity influence may
at times clash with money and credit policies to be followed against
inflationary pressures.   Furthermore, while the small firms are
more in need of liquidity and of encouragement for risk-taking, the
accelerated depreciation allowance has in fact been granted to the
big firms.

Similar effects of increasing liquidity and the encourage-
ment for risk-taking would result also from the investment allow-
ances.   But the stimulation for risky investments would be greater
in the case of investment allowances than accelerated depreciation,
since total wear and tear allowances do not exceed 100% of cost in
the latter case whereas they do in the former case.   Again, the
advantages of the investment allowance have been confined to the
large enterprises while the small firms need them more.   From the
aggregate savings point of view, the investment allowance may
hardly be expected to exert any positive effect, since the funds
above 250,000 T.L. would be invested anyway and the concession is
not confined to the investments financed by accumulated profits.

The provision to offset losses has the same effects, but is not restricted to the use of big enterprises only.

These three incentive measures have important features in common. They do not appear to stimulate the aggregate savings directly but do appear to influence the allocation of investible funds, in the first place, in favour of the private sector against the public sector, and, in the second place, in favour of relatively more capital-intensive investment. We shall return to this point later.

The treatment of the revenue from real estate as described above is, first of all, incompatible with justice, secondly, with the priorities of the Plan. It is the favourable provisions of the income tax and Building tax that have stimulated the flow of more than 60% of the private investment into the construction sector during the 1950's.[1] In view of the diminishing share of total investments directed to the construction sector as proposed by the Plan, tax concessions applied to revenues from buildings and from transactions in real estate

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1. A. T. Peacock and H. Hauser, Fiscal Policy in South East Europe, in the Government Finance and Economic Development (ed.) A. T. Peacock, Paris 1965. (A Collection of the papers read in a Conference arranged by OECD.)

must be abolished, except for tenement houses for occupation by lower income classes. This may have a considerable revenue effect in addition to its favourable effects on social justice and allocation of resources. In order to mitigate the pains of such a transition to a wider concept of income, Mr. Kalder proposes that for some time the gains made on the sale of real estate should be taxed fully if the realization is within 4 years but that afterwards the taxable gain should be reduced by 10 per cent for each further year for which an asset was held.[1]

B. Taxation of Company Income :- The profits of all corporations, limited liability companies, co-operatives and state economic enterprices, are subject to the withholding income tax and the corporation tax.

The withholding tax is levied at a flat rate of 20 per cent on the taxable income of the company which is arrived at by deducting all kind of taxes paid, reserves and counterpart funds, and the losses of previous years from the profits. Thus the withholding income tax is levied on the distributable profits and is supposed to be paid by the company on behalf of the shareholders who are given credit for the tax paid on the distributed profits. It seems that the assessment of the whole of the profit, distributed as well as undistributed, to the

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1. N. Kaldor, Report . . . . ., op.cit.

withholding tax needlessly penalises the ploughing back of profits of the company.[1] It would, therefore, be more feasible to confine the withholding tax to actual divident payments. Against this it is maintained that in Turkey most of the corporations are closely held family concerns and there are various ways of distributing profits to "inside" shareholders other than through a formal divident payment. The dangers of tax evasion would, however, be met adequately if a minimum part, say, one-third, of the profits is made subject to the withholding tax, since most corporations have to plough back a considerable share of their profits for expansion purposes.[2] With this change, it will be necessary to raise the rate of withholding income tax, since its present rate of 20 per cent is reached as an effective rate in the personal income tax at an annual income of 20,000 TL. which is surely below the average income of a shareholder in Turkey.[3]

Companies' profits are also subject to the corporation tax. The rate of corporation tax was raised in 1962 from 10 per cent to 20 per cent in private companies and to 35 per cent in public enterprises. In 1963, 4704 Companies paid 427 million

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1. N. Kaldor, ibid.
2. For the ratio of undistributed porfits to total profits, see page 116.
3. N. Kaldor, op.cit.

TL corporation tax which was equal to only 4.9 per cent of total
tax revenue. The low level of revenue from corporation tax is
due to two reasons: first, the sectors in which companies
usually predominate (e.g. heavy industry) have a relatively small
share of GNP and second, the number of incorporated businesses
is relatively smaller inside any given sector. Therefore, to
achieve an increase in the revenue from this source is, in the
first place, a matter of structural change which depends on the
overall development of the economy. For an immediate revenue
increase, however, a higher tax rate as suggested by Mr. Kaldor
may be considered. In fact, the present rate of 20 per cent on
the privately owned companies seems extremely low in comparison
with other countries. The rate of this tax is 52% in the U.S.,
58% in Israel, 50% in France and 45% in Ceylon, and in all these
countries there is also income tax liability on the personal
income of shareholders.[1] An increase in the rate of corporation
tax becomes more necessary particularly in view of the recent
important tax concessions, in order to offset at least partly
the revenue loss of the government and to make the incentive
measures more effective. However, one could doubt if the
feasible scope for an increase in the tax rate is as great as
envisaged by Mr. Kaldor who suggested a uniform rate of 40% be

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1. N. Kaldor, ibid.

applied to all corporations. The imposition of a non-refundable tax on the company profits in addition to a refundable income tax is explained by the fact that an incorporated enterprise stands as an entity independent of its shareholders. But Turkish corporations are mostly family concerns and the burden of corporation tax is felt more strongly by the shareholders than in other countries. As a matter of fact, under the existing circumstances in Turkey the need for the spread of corporate form of business is immense and this requires light taxation of company profits in comparison with personal incomes.

C. Taxation of Wealth :- We have already pointed to the defect in the Turkish tax system regarding taxation of capital gains arising from the transfer of real estate,[1] which is by far the most important form of wealth in Turkey. Since portfolio investment in shares is relatively rare in Turkey's present stage of development, it does not seem necessary to extend the tax net to the gains from the sale of stocks and shares.

There are three main taxes on the value of capital: land tax, building tax and inheritance and gift tax. The revenue from the first two goes to the local administrations and the central government has a share of revenue from the building tax. Both of these taxes are levied on the cadostral value of estates

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1. See: pp. 190 and 191 of the present chapter.

and have therefore been largely eroded.[1]   In their present terms
they can neither contribute significantly to the public sector's
revenue nor perform their function of supplementing the taxes on
incomes and profits so as to reduce inequalities.

The inheritance and gift tax provides very little revenue
and has so far been applied on account of social justice
considerations.[2]   The contribution of this tax was only 0.13 per
cent of the total expenditure from the General and Annexed Budjets
in 1960.[3]   In 1964 its revenue was 1/25th of the revenue from the
sugar consumption tax.[4]   This very low level of revenue is the
result of various factors. First, the base of the tax is assessed
according to the acquisition value which results in the assessment
of real estates according to the 1936 cadostral valuation.
Consequently, the revenue from this tax has been largely eroded
owing to the rising prices in the last two decades or so.
Strangely enough, the valuation of all business estates, whether
tangible or net, for purposes of inheritance and profit tax is
carried out at their current market value. This creates a harmful
discrimination against the productive employment of capital and in
favour of keeping wealth in idle forms. Secondly, it is estimated
that tax evasion is practiced on a tremendous scale.[5]   Thirdly,

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1.   See: p.148 in this chapter
2.   H. Kizilyalli, op.cit., p.119
3.   SPO. "Sector Programmes, Taxation", mimeographed & in Turkish,
     Ank 1962, p.12.
4.   See Table 29.
5.   H. Kizilyalli, op.cit., and SPO, Vergi, Mimeographed 1962.

the tax rates are low and exemption limits are very high.[1]   Thus,

a considerable amount of wealth passes on without paying any   tax.

IV

TAXATION OF COMMODITIES AND SERVICES

The revenue from indirect taxes[2] constitutes the major

part of the total tax revenue, i.e., two-third in recent years.

As will be seen from Table 29a, the share of indirect taxes in

the total tax revenue in 1963 and 1964 was 67.4% whereas it was

61.7% in 1960 and 62.8% in 1956.   This is accounted for by the

enlarged coverage and increased rates of indirect taxes as well

as by the unsusceptibility of direct taxes to rising national

income.

When we look at the structure of indirect taxes, no single

tax is seen as relatively predominant.[3]   The largest revenue

yielding tax is the production tax, which is an excise tax.

Tobacco and alcoholic drinks also provide a significant revenue.

The only mass consumption commodity of basic need nature which is

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1. SPO, ibid.
2. There is no universally agreed criterion to distingwish indirect
   taxes from direct. We adopt here the classification used by the
   Ministry of Finance as shown in Table 29.
3. This runs counter to the case observed in underdeveloped countries
   For instance, in 1959 Chana raised 25% of its revenue from import
   duties and 38% from export taxes; Ceylon 30% from the former and
   27% from the latter; Malaya derived 25% of its revenue from export
   taxes. (A. R. Prest, Public Finance in underdeveloped Countries
   pp63 & 66).

taxed is sugar. Such services as banking and insurance, P.T.T. and transport are also subject to taxation. There is neither a general sales tax nor a purchase tax and no multi-stage tax. The tax on imports brings in a revenue equal to the one-tenth of total tax revenue. Export tax is unknown in Turkey since the end of World War II.

In order to envisage the role of indirect taxation in financing the Plan, let us acquaint ourselves with the important taxes on commodities and services.

Prior to 1956 the taxation of commodities and services had a very complex structure with separate tax laws for some individual commodities and services. An integration in this field was achieved in 1956 with Law No. 6802, which brought together various taxes on commodities and services within the code of "Taxes on Outgoings".[1] The Law comprises two broad category taxes: The Production Tax and the Taxes on Services.

The production tax is levied on the specified commodities as they are disposed of. The tax is deducted at source by the disposer of the commodity who includes the tax into his price.

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1. In the publications of the Ministry of Finance the title of the Law No. 6802 is translated into English as "Expenditure Taxes". As this may cause an outsider to confuse it with Kaldor's expenditure tax, we prefer here to adopt the U.K. Hicks' terminology used in her Development Finance, op.cit.

If a commodity subject to the tax is used by its owner the tax is to be levied in the same way as if it has been trasfered to another hand. The taxable commodities are arranged in four tables. The first table enumerates the raw materials and primary products such as cement and bricks, all kind of processed minerals (including oil), rubber, paper, glass, textiles, plastics, furs and jewellery, and electricity and gas. The second table contains manufactured commodities such as explosives and weapens, vehicles, watches, radios, record-players and tape-recorders, cameras and cine-cameras, matches, and ceramics. The third table includes, coffee, cocoa, glucose and some alcoholic drinks which are outside the state Monopoly Administration. Table 4 lists the imported commodities which correspond to those included in other tables.

As it is easily seen particularly from the content of the first table the ultimate usage of the commodities taxed are not readily ascertainable. Although, at present, the Turkish industries are in the main consumption goods industries, the capital goods industries have been gaining importance and hence the indirect taxation of capital goods. A tax on investment goods may be an anti-inflationary measure and may also have the effect of encouraging the use of labour-intensive methods of production, both of which are desirable from the viewpoint of the plan targets. But, in view of the incentive measures mentioned

in the last section, there is quite clearly some conflict: a tax
policy which boosts private capital formation with one hand and
knocks it down with the other is obviously lacking in consistency.
Indeed, the Production Tax may have some advantages in favour of
saving and investment only if capital goods are not subject to
the tax.

The Production Tax applies differentiated rates to different
products on an ad valorem basis with a few exceptions such as
petrol and petroluem products, electricity, gas, matches and the
commodities in the third table which are taxed at specific rates.
On the raw material and primary products, the rates vary from 12.5
per cent on construction material to 30 per cent and over on some
textiles and to 75 per cent on furs and jewellery. On the
manufactured commodities it varies between 10% and 40% and in the
case of imported goods between 10% and 60%. Concerning those
commodities of which end-usages are ascertainable, the differ-
entiation of rates would certainly accord progressiveness to the
production tax.   For instance, in the case of imported commodities,
the taxation of textiles at a rate of 12.5 - 18 per cent, as
against the tax rate on plastics of 35% and on furs and jewellery
of 60%, could claim to have progressive effects in relation to
income differences.   The same could be said with respect to the
taxation of manufactured goods.   On the other hand it is difficult

to explain the lenient taxation of wine and beer in comparison
to whisky - 0.2, 0.4 and 30 TL per litre, respectively. Although
whisky may be considered rich peoples' drink, it is hardly
possible to treat beer and wine as basic necessities.

As regards the commodities listed in the first table,
although attempt is made to accord a progressive nature to the
production tax through differentiated rates, the fact that end-
usages of most commodities included in this table cannot be
ascertained makes incidence of the tax ambiguous.

With respect to the differentiation between capital goods
and consumption goods, the former is taxed at lower rates than
the latter in the case of imported commodities. This provides a
stimulus for the future against the present consumption. But
if the capital goods are used in the production of consumption
goods, the effect of this differentiation on the capital formation
would be limited. In the table of raw materials and primary
products, some investment goods such as cement, bricks, some iron
products, and electricity used in production are taxed relatively
lightly. But the uncertainty regarding end-usage of them makes
impossible any prediction of their possible effects on capital
formation and saving in relation to consumption.

The taxes on services comprise these three taxes: Banking
and Insurance Transactions Tax, Transportation Tax, and P.T.T.

Service Tax.   In 1964 they together accounted for less than 8%

of the indirect tax revenue.   The banking and insurance tax is

levied at a rate of 20 per cent on the incomes of banks and

insurance companies from all of their transactions.   This tax

would make for a higher effective rate of interest which might be

deemed desirable in view of the necessity of using the scarce

factor "capital" in the most economic ways.

Let us now examine briefly the excise levied on the mass

consumption commodities.   Of these commodities, tobacco, aloholic

drinks, tea, salt and sugar are the most important ones.   With

the exception of sugar and some alcoholic drinks, their production

and distribution are under the monopoly of the State Monopoly

Administration.   The tax on the monopoly products consists of two

elements: a specific tax called "Defence Tax", and profits of the

Administration.   In 1963 the former brought in a revenue of

477 million TL., and the latter 761 million TL. which comprised

336 million Tl profit from tobacco, 235 million TL. from drinks,

171 million TL from tea, 19 million TL. from coffee, 1 million TL

from matches and 1 million TL. loss from salt.

Under the present system, the profits of the Monopoly

Administration serve not only as a tax but also as a buffer to

maintain stable prices for the monopoly products against changing

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1.   Ministry of Finance, "Budget Revenues Bulletin, 1969", pp. 143 -
     144.

costs. This is criticised on the ground that it leads to the
inefficient use of the resources at the disposal of the Administra-
tion, and it is suggested that the monopoly products should be
charged a predetermined tax and that the Monopoly Administration
should be free to apply a monopolistic price policy[1].

Having a low price-elasticity and a high-income-elasticity
of demand, the monopoly products, except salt, are best suitable
for excise taxation. Besides, in view of their "non-essential"
character and of the diseconomies connected with their consumption,
the taxation of the monopoly products could hardly provoke any
argument of regressiveness. These points, however, do not seem
to have influenced the tax policy with respect to the "mass
luxuries" in question. Indeed, the total revenue, i.e., taxes and
profits, of the State Monopoly Administration rose from 473 million
T.L. in 1956 to 1248 million T.L. in 1963, recording a rise of only
164% whereas in the same period the gross national product at
current prices has increased by 182%. If account is taken of the
fact that changes in the social conditions and the increasing
monetization of the economy which have taken place in Turkey during
1956-1963 must have had the effect of increasing the high income-

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1. A. Alaybek and others, "Reform in the Indirect Taxes", as quoted
   in H. Kizilyalli, op. cit., pp. 78-80.

elasticity of demand for the monopoly products, the failure of the taxation of these commodities in responding to the increases in money incomes will become more conspicuous. The failure is certainly due to the "profit" element in the taxation of the monopoly products. There is therefore a good case to adopt a method of taxing these commodities that would lay the emphasis merely on the revenue aspect. Nevertheless, a reservation must be made here with respect to the taxation of tea. The domestic production of tea is protected from foreign competition with a customs duty of over 100% and a plus-value charged by the Monopoly administration on the imported tea twice as high as charged on home-produced tea. Although, the protection is granted in the national interest, it could hardly be maintained that the consumers of tea benefit directly from the policy of protection. On the contrary, they are forced to pay a higher price because of protection. It is then far from reasonable to ask these same consumers to bear the extra burden of the excise tax on tea. A similar argument may be put forth for the taxation of tobacco, which is one of the main sources of foreign currency so scarce in Turkey. To the extent that domestic consumption of tobacco competes with its export, an additional tax burden on the consumers of tobacco may be necessary in order to divert the supply of tobacco from home to foreign markets and to make the consumers of tobacco pay in taxes the gap between the social and private cost of

consumption of tobacco which arises because of the competition of domestic consumption with export.

Apart from such commodities as clothes and matches which are subject to the production tax there are two widely consumed basic-necessities, namely, salt and sugar, which are subject to the excise taxation. Salt is a state monopoly product. Although the Monopoly Administration has in the recent years incurred small losses from the sale of salt, these have been more than compensated for by the defence tax charged on salt at a rate of 67%[1] which is higher than the tax rates applied to many luxuries within the production tax.

Sugar is very heavily taxed at a specific rate of 0·85 T.L. per kgr. for crystal sugar and 1 T.L. per kgr. for cube sugar. At present this amounts to the taxation of sugar at a tax rate of more than 50% of its cost per kgr. By its nature, taxation of sugar is heavily regressive and, as a result of high sugar prices, results in a significant burden on the low income groups. However, since the poor rural population substitute sugar with pekmez (boiled grape-juice), it is especially the low-income classes of urban population that bear the heavy burden of the taxation of sugar.

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1. H. Kizilyalli, op. cit., p. 120.
   In 1963 the Monopoly Administration incurred a loss of 1 million T.L. from the sales of salt which was 16 million T.L. This shows the existence of about 7 million T.L. defence tax on salt.
   (Figures are from the Budget Revenues Bulletin pp. 123-124).

Finally, a glance at the customs duty. In Turkey the customs duty is to a great extent used for the protection of infant industry as well as for economizing on the meagre foreign currency reserves, though to obtain revenue to the Treasury is the main purpose. The average rate of duty is low, being 13.35% in the 1959-61 period[1]. A differentiation of rate is applied, raw materials being taxed at a lower rate than manufactured goods, capital goods than consumption goods, and necessities than luxuries[2]. Low duties on capital goods, however, induce capital-intensive production methods and also prevents the development of capital-goods industries at home. So long as the domestic production of luxuries is not effectively discouraged, higher duties on imported luxuries, on the one hand, and the low duties on imported raw materials, which can be used in the production of luxuries as well as the necessities, on the other hand, would no doubt provide a stimulus for the productive factors to flow into the production of luxuries.

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1. S.P.O., "Sector Programmes, Taxation", Ankara 1962 (mimeographed and in Turkish), p. 22. The average rate of customs duty is calculated on the basis of the value of total imports and of the total revenue from the customs duty.

2. Ibid.

IV

THE TAXATION POLICY IN THE PLAN PERIOD

The 1962 Interim Programme envisaged a total tax revenue of 8,000 million T.L. but the actual collection turned out to be 7,100 million T.L.   The actual rate of growth of G.N.P. in 1962, 6%, also lagged behind the Programme target of 7%.   Since the Development Plan had been drawn up on the assumption that the G.N.P. would grow in 1962 by 7% over its 1961 level, it was imperative to revise the Plan's targets according to the actual outcome of the 1962 Interim Programme.   But this necessity had not been realized, and the expenditure and revenue targets of the Plan for 1963 in absolute amounts were kept intact in the 1963 Annual Programme, though the G.N.P. target was stated as 7% higher than the actual G.N.P. in 1962[1].   Consequently, the target for tax revenue in the 1963 Annual Programme, that is, 9,000 million T.L., stood at 16·2% of the G.N.P. ~~target~~ instead of 15·95% as envisaged in the Development Plan.   At the time of the preparation of the 1963 Annual Programme the total tax revenue in 1962 was expected to be around 7,300 million T.L., which necessitated an additional tax revenue of 1,700 million T.L. in 1963 in order to reach the target.

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1. S.P.O., 1963 Annual Programme, p. 51.

Of this, 550-600 million T.L. was expected to come about under the existing tax system as a result of the increases in incomes and expenditures, assuming an income elasticity of one in the tax system. The rest would be made up by increasing the rates and enlarging the coverage of the existing taxes. In this connection, significant increases were expected in the revenues from the income tax, the production tax on petroleum products and on domestic production, the stamp duty, and the monopoly products. We have already pointed to the great failure in the attempt to extend the personal income tax to the agricultural incomes. Furthermore, the inclusion of artisans among the income tax payers, which had been expected to provide a revenue of 50 million T.L. in 1963, was postponed. The increases in the tax rates of indirect taxes produced important additional revenue but no indirect tax reached the Programme target except the sugar consumption tax and customs duty which both exceeded their targets. The actual tax revenue in 1963, therefore, could reach 8,400 million T.L. against the target of 9,000 million T.L. The rate of realization, 93%, however, was higher than the one attained in 1962, that is, 89%.

In the 1964 Annual Programme the expenditure and revenue targets in absolute amounts were taken from the Development Plan, adjusting them for the rise in the general price level. Thus, the tax revenue for 1964 was estimated to reach 10,400 million T.L.,

increasing by 24% over the out-turn of 1963.   Of the additional

tax revenue of 2,000 million T.L., 1,200 million T.L. was expected

to arise from the normal increase in tax yields following the growth

of national income[1].   This corresponds to an increase in yields of

13%, as against a forecast rise in G.N.P. by 7% in real terms.

Even assuming a certain rise in prices, the implied elasticity of

tax yields appears rather high in comparison to the past experience.

An additional 800 million T.L. was expected to come from new tax

measures.   Direct taxation of agricultural incomes was to be

enlarged, as already explained above in the section on the taxation

of agriculture, so as to yield 200 million T.L. in 1964.   Increases

in various types of indirect taxes were expected to provide about

400 million T.L.   The government was also planning to obtain an

additional 100 million T.L. by improving the tax administration,

as control and collection of direct taxes are poor and evasion is

extensive, especially when the taxes are not withheld at source.

But the government proposals could get Parliamentary approval only

after having been circumscribed considerably so that the expected

yield from the new measures in 1964 was reduced to about 440 mil-

lion T.L.[2].   In order to avoid a budget deficit, public expenditures

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1.   1964 Annual Programme, p. 268.

2.   O.E.C.D., "Economic Survey, Turkey", August 1964, p. 30.

were cut down which reinforced the tendencies of slowing down of
economic activity already observed by the end of 1963. The slowing
down of expansion affected at least the yield of indirect taxes.
In fact, in spite of the new tax measures, the actual total tax
revenue in 1964 was only 9,200 million T.L. which was less than
expected to occur automatically, let alone the additional yield
from the new measures. The rate of realization was as low as 88%.

In the 1965 Annual Programme we observe a change in the
method of determining the tax targets. The tax/income ratio,
instead of tax revenue in absolute amount, as envisaged by the
Development Plan to occur in 1964 was applied to the G.N.P. target
of the 1965 Annual Programme, that is, 69,840 million T.L. at 1963
prices[1]. This showed a target of 11,800 million T.L. at 1963
prices for total tax revenue to be obtained in 1965. This would
require an increase in tax revenue by 28% over the 1964 out-turn.
The 1965 Annual Programme, however, did not deem feasible such an
increase in tax revenue in view of the fact that considerable
increases in tax rates and coverage had already been made in 1963
and 1964[2]. It was expected that the existing taxes would yield
10,800 million T.L., 300 million T.L. of which would result from

1. S.P.O. , 1965 Annual Programme, pp. 11 and 303.

2. S.P.O., 1965 Annual Programme, p. 304.

the rationalization and improvement of the tax laws and administra-
tion, and that the remaining would be made up by the non-tax revenue
sources such as the S.E.E. and local administrations and by internal
borrowing[1]. But the actual tax revenue was only 10,200 million T.L.
in spite of a rise by 8% in the wholesale price index. And the
94% rate of realization seen in the column IV of Table 33 would have
been reduced to 86% had the additional financing required to bring
the consolidated budget (General and Annexed Budgets) into balance
been planned to be met by taxation as had been the case in the 1963
and 1964 annual programmes.

It is thus apparent that the taxation policy in 1962-1965
has not been successful in fulfilling its task of providing the
required resources for use by the public sector. Before dealing
with the shortcomings of the taxation policy itself, it seems
necessary to question the feasibility of the tax revenue targets
of the annual programmes. The annual programmes adopted as their
tax revenue targets those set for the relevant years in the Develop-
ment Plan. This has paradoxically involved an arbitrariness
because of the following two reasons. First, the Plan's targets
for various kinds of public revenue to be obtained in a certain year

1. Ibid., p. 304.

are meaningful only when considered together with the G.N.P. target
set for that year in the Plan.   It would not be reasonable to assume
that the Planners, when setting the tax target, say, for 1965, meant
it to be attained regardless of the levels of G.N.P. in that year.
Secondly, the practice of determining the tax revenue targets in
the Annual Programmes implies an ignorance on the planners part of
the close relationship between the composition as well as the level
of expenditures, both private and public, and that of the tax
revenue.   As it is known, the S.P.O. had proposed a scheme for the
taxation of the agricultural sector which would have made it
possible to collect the revenue needed for the Development Plan.
But the government, which approved the Development Plan, has
refused to sanction the scheme for financing it[1], and the task of
obtaining the required finance has been left to the annual program-
mes.   As we have seen, the annual programmes squeezed every source
for additional tax revenue but not the agricultural incomes[2].
Thus, the tax revenue targets in the annual programmes have been
set at unduly high levels, and have been intended to be realized
by concentrating the burden of taxation on the non-agricultural
sectors.

1. N. Kaldor, Will Underdeveloped Countries Learn to Tax, Foreign
    Affairs, Vol. 41, No. 2, January 1963, pp. 410-420.
2. It is hardly possible to consider as a serious attempt the
    inclusion of agricultural incomes into the personal income tax
    which yielded a revenue of 30 million T.L. in 1963.

In a development plan of the Turkish type, which puts great emphasis on the induced participation of private initiative, tax revenue targets in each year of the plan period should not be considered as imperative targets. However, prior estimation of required resources, and, hence, tax revenue, is necessary in order to have an idea of the magnitude of the task of achieving a successful implementation of the Plan. The refusal by the government of the scheme of burdening the agricultural sector according to its share in national income made it obvious at the outset that the required domestic resources would not be forth coming during the plan implementation. It would therefore have been more feasible to reduce the Plan in size. This has not been done. Nor have the revenue targets of the Development Plan been adjusted downward when they are adopted by the Annual Programmes in spite of the fact that a host of other targets, including G.N.P. and investment targets, have not been fulfilled since the beginning of the 1962 Interim Programme. Furthermore, the refusal of the original financing scheme should have caused not only a reduction in size of the Plan but also a complete alteration in the objectives as well as the strategy of the Plan, since there are undeniable "cause-and-effect" relations between the composition of investment and that of financing. It is simply illogical to assume that a considerable part[1]

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1. In 1963 an additional financing of 1,200 million T.L. was necessary, 1,000 million of which was originally assumed to come from the direct taxation of agriculture.

of the required financing originally envisaged to come from the agricultural sector could be obtained from the other sectors and, at the same time, the Development Plan, with its targets concerning the allocation of resources between different sectors and that of expenditures between saving and consumption, could be implemented successfully as originally forecast. In view of these facts, it would perhaps not be an exaggeration if one says that the Turkish Development Plan was still-born.

So much for the faulty choice of tax revenue targets in the Annual Programmes. It is now time to search for the shortcomings of the taxation policy in 1962-1965 which might have held back the growth of the tax revenue. As seen in Table 33, despite the fact that the rate of realization has been low, the share of tax revenue in the G.N.P. has continuously increased from 12·8% in 1962 to 14·3% in 1965, recording an increase by 1·5% of G.N.P. This implies that the tax system has recently achieved the income-elastic character which it had lacked in the 1950's. This is better observed in the last column of the table, where the income elasticity of the tax system, that is, the ratio of the rate of increase in tax revenue to that in G.N.P., is seen as 1·33 in 1963, 1·45 in 1964 and 1·58 in 1965. Indeed, the tax revenue has increased in the period 1962-1965 at a rate of 9·7% per annum while the increase

TABLE 33

SOME INDICATORS OF THE TAXATION POLICY, 1962-1966

(000 Million T.L. at current prices)

Year	G.N.P.[1]	Tax Revenue		Rate of Realiza-tion (%)	T/G.N.P. (%)	$\Delta T/\Delta GNP$	$\frac{(\Delta T/T)}{\frac{(\Delta GNP)}{GNP}}$
		Programme	Actual				
	I	II	III	IV	V	VI	VII
1962	55·2	8·0	7·1	89	12·8	6·6	0·48
1963	62·7	9·0	8·4	93	13·4	17·3	1·33
1964	66·8	10·4	9·2	88	13·8	19·5	1·45
1965	71·4	10·8	10·2	94	14·3	21·8	1·58
1966	76·4	12·2	-	-	16·0	40·0	2·80

1. The G.N.P. figures are the realized ones, except
   the 1966 figure, which is the Program Target.

Note on the sources: The G.N.P. figures for 1962 and 1963
were taken from O.E.C.D., "Economic Surveys, Turkey",
Paris Aug. 1964, p. 43, Table 1;   those for the years
1964 and 1965 from S.P.O., A Summary of 1966 Annual
Programme, First Draft, mimeographed, p. 64, Table 9.
The latter source gives the 1963 G.N.P. figure which
exactly corresponds to that given in the former source,
and this shows that the 1962 figure in the above Table
has a common method of estimation with the other years'
figures.   The 1965 figure is the first estimate made
in October 1965.   The 1966 Annual Programme aims at
7% growth in G.N.P. over the 1965 out-turn and expresses
this target as 75,100 million T.L. at 1964 prices.   Our
figure in the table, 76,400 million T.L., was arrived at
by increasing the 1965 figure by 7%.   The estimates of
G.N.P. by the State Statistical Institute differ from
the S.P.O. estimates.   They are 60,300 million T.L.,
68,490 million T.L., 72,940 million T.L. and 78,983
million T.L. in 1962, 1963, 1964 and 1965, respectively,
as given in the Ministry of Finance, Budget Proposal
for the 1966 Fiscal Year, Ankara 1965, in Turkish,
p. 54, Table 1.

Note on the sources of Table 33 contd.

      The sources for the Programme figures for tax
revenue are as follows: for 1962 and 1963, S.P.O.,
A Summary of the Progress Report on the Implementation
of the 1963 Annual Programme, Ankara July 1964, p. 31,
Table 26; for 1964, S.P.O., 1964 Annual Programme,
Ankara November 1963, in Turkish, p. 267, Table 156;
for 1965 and 1966, S.P.O., A Summary of 1966 Annual
Programme, first draft and mimeographed, p. 78,
Table 14.

      The figures for the actual out-turn of tax
collections have been taken from the following sources:
the 1962 and 1963 figures from S.P.O., A Summary of the
Progress Report....., ibid. p. 31, Table 26; the 1964
figure from S.P.O., A Summary of 1966 Annual programme,
ibid., p. 64, Table 9; the 1965 figure is the expected
out-turn calculated by myself by extrapolating the fact
that the total tax collections of the first eight
months of 1965 is greater by 11% than that of the
corresponding period of the previous year.

      The last three columns have been arranged on the
basis of the first three columns.

      Finally, while the years for G.N.P. figures are
calendar years, those for tax revenue figures are
fiscal years, i.e., 1 March - 28th February.

in G.N.P. in the same period was only 6·8% per annum[1], giving an

income elasticity of 1·3 for the period. This has been possible

as a result of achieving an incremental tax-income ratio higher

than the average tax-income ratio. Columns V and VI of the table

1. Both rates are compound rates, calculated on the basis of data
    given in Table 33.

show comparatively the incremental and average tax-income ratios.
The portion of the incremental income-taken in taxes had sharply
increased in 1963 compared with 1962 and has steadily grown larger,
reaching 21·8% in 1965 as compared with the average tax ratio of
14·3% in that year.   For the period as a whole the incremental
tax ratio is 19·1% while the average tax ratio is 13·6%.

Despite the favourable impression created by the preceding
paragraph, one could not expect the same tax trend to continue in
the near future.   The higher average and incremental tax ratios
have not been produced by a built-in flexibility in the tax system;
instead, this result has been achieved through the increases in the
rates and coverage of the tax system.   Table 34 below reveals the
fact that indirect taxes have played an almost equal part with the
direct taxes in increasing the total tax revenue during 1963-1965
whereas the direct taxes are supposed to be more sensitive to the
increases in national income.   If the 1962 ratios as well are
taken into account, which shows that the increase in the total tax
revenue was completely due to the increase in the revenue from
indirect taxes, it appears that the indirect taxes have provided a
greater part of the increase in total tax revenue.

Recalling the survey of indirect taxation in Turkey made in
the last section, it is hardly possible to envisage further increase

TABLE 34

INCREASES IN TOTAL, DIRECT AND INDIRECT TAXES IN PERCENTAGES

(Current prices)

	1962	1963	1964	1965
Tax Revenues	6·2	18·4	9·9	11·1
a. Direct taxes	- 11·0	17·8	9·9	11·8
b. Indirect taxes	17·3	18·7	9·9	10·7

Sources: 1962, 1963 and 1964 ratios were taken from S.P.O.,
A Summary of 1966 Annual Programme, p. 62, Table 8.
1965 ratios were calculated on the basis of collections
at the end of October, 1965, as given in the Ministry
of Finance, The Budget Proposal for the 1966 Fiscal year,
p. 156, Table 8.

in the indirect tax revenue apart from what could be done as a
result of the increase in spendings. There are significant limita-
tions on the possibility of increasing the revenue of the Production
Tax through raising the tax rates and/or enlarging its coverage.
First, the approaching of the data of Turkey's joining the E.E.C.
(European Economic Community) precludes the possibility of increasing
taxation of imported commodities, and hence, of home-produced import-
substituting commodities. Secondly, since the end-usage of most of
the raw materials and primary products subject to the Production tax
cannot be ascertainable, any tax measure regarding these commodities
is limited with an uncertainty about its incidence. On the other

hand, the present state of fiscal administration does not seem capable of coping with the complications of a sales tax at even the wholesale stage. Finally, the Production Tax is not suitable for an extensive discrimination against those commodities for which demand rises more than proportionately with income. As regards the sugar consumption Tax, one might incline not to wake up the sleeping dog but certainly no further increase in the tax rates can be suggested. The only promising field of indirect taxation, therefore, is non-essential mass-consumption goods such as tobacco and alcoholic drinks (mass-luxuries). But the political limit of the taxation of such commodities will certainly be reached much earlier than the economic limit.

Once it is agreed that there is not much scope for further increases in the indirect tax revenue, one has either to be content with the present tax/income ratio or to seek the means of increasing the direct tax revenue. The examination of the direct taxation in Turkey in the earlier sections above has made it clear that there is an immense tax potential which could be exploited by means of direct taxation. The first and foremost reform in the field of direct taxation is required in the taxation of agriculture. The discussion in Section II above has brought it into light that the equal treatment of the equals (horizontal equity) cannot be achieved in Turkey so long as the agricultural sector is attempted to be

taxed within the personal income tax.   And unless this deficiency
is remedied, the measures taken to increase the tax burden of the
non-agricultural sectors would only serve to aggravate the
inequal distribution of tax burden and the misallocation of
productive resources.   Therefore, the suggestions made in this
dissertation with respect to the changes in the present form of
the income taxation are only meaningful if accompanied by an
effective taxation of the agricultural sector.

In Turkey, the revenue from the direct taxation is held
back by the influence of the two wrong arguments, which amazingly
contradict each other[1].   On the one hand, it is argued that the
surplus of income over the minimum subsistence needs of the popu-
lation is so meagre that the proportion of the national income
which can be taken in taxes is bound to be much smaller than in
the rich countries.   On the other hand, the taxation of incomes
and profits is furnished with every measure of incentive to the
high income-classes as if Turkey had large untapped resources at
her disposal but their activation was prevented by the lack of
adequate incentives.

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1. For instance, both arguments constitute the skeleton of the
    conference given at the University of Saarland, Germany, by
    Prof. Orhan Dikmen, the most influential member of the Taxation
    Reform Commission.   It has been published in the Public Fin-
    ance Vol.XIX, No.4 , pp.1-25, and as a booklet by the Institute
    of Public Finance of the Istanbul University: Financing of the
    Investments in the Development Plan, Ist.1964, in Turkish.

The tax potential of the Turkish economy cannot be assessed on the basis of the low percapita national income. The study of the distribution of income and wealth made in the first chapter reveals that those with a surplus over the essential consumption have command over a considerable proportion of the national income. Although there is no accurate data, it would not be far from the truth if one says that the degree of concentration of wealth in Turkey is as great as in the advanced countries[1]. Moreover, the higher share of indirect taxes as compared with the direct taxes, that is, a 67/33 ratio of indirect to direct taxes, means that the incidence of taxation in Turkey is far more regressive than in the advanced countries. The limited degree of progressiveness which could be accorded to the indirect taxation at the present stage of development of the Turkish economy cannot alter this general conclusion. Furthermore, far more of the income tax falls on the wage and salary earners. The share of the wage and salary earners and liberal professions in the G.N.P. was about 12% in 1963, while their share in the total tax revenue was around 52%[2].

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1. According to Mr. N. Kaldor, the share of the national income which accrues to property owners of all kinds is probably appreciably larger in countries like Turkey, Mexico, Chile, India or Persia than in the U.S. or in Britain. (Will Underdeveloped Countries Learn to tax, op. cit.). In fact, the studies of income distribution made with respect to India by Mr. S. J. Patel and MrS. Kuznet confirm this. (Raja J. Chelliah, op.cit., pp.63-64).

2. The ratios were calculated on the basis of the data given in the Ministry of Finance, Budget Revenues Bull, Ankara 1964, pp.58-59 and 138.

Whatever allowance is made for the difference in the method of classification of the wage and salary earners and liberal professions in the national income and income tax statistics, the huge disparity between the above-mentioned two shares will not be much narrowed.   These indicators give sufficient support to the general argument of this chapter that the tax/income ratio in Turkey could be raised far above the present ratio, particularly through increases in the direct taxation, without creating a social tension.

Nevertheless, the limitations on the extension of income taxation to the middle-income-classes apart from wage and salary earners, which arises from the underdeveloped character of the economy, necessitates the use of wealth taxes at a greater extent as a supplement to the taxation of incomes.   Indeed, the taxation of the small trader within the personal income tax is as great a problem as the taxation of agricultural incomes.   The present practise of deducting a fixed sum of expenses from the business turnover (gross receipts) is not an effective method.   To get hold of business turnover is as difficult as to assess business profits of the small trader.   Also, the state of illiteracy and of commercial practices compel the acceptance of a high level of business turnover as the limit for presumptive method of taxation.

On the other hand, an annual tax based on the net value of property of the small trader would be both easier to administer and difficult to evade.

It is an element of the strategy for domestic financing of the Plan, which has been discussed in Chapter 3, that the savings of the private sector are expected to increase at a greater rate than the public savings. It follows from this that the tax policy should not deter the saving incentives of the private sector and, in any case, avoid increasing the public revenue at the expense of the private savings. Putting it differently, the tax instruments should be so manipulated as to lead to an increase in the aggregate savings and not only in the public savings. In accordance with the recommendations of the Tax Reform Commission, the income tax has been made less progressive at the high income levels with Law No.202 and embodied with various incentive measures in order to encourage the accumulation of savings and the capital formation. In view of the analysis of the taxation of incomes and profits conducted earlier in this chapter, it is hardly possible to regard the present incentive measures as contributing to the increased savings. First of all, it seems more encouraging for the accumulation of savings to maintain a sharp progressiveness with exceptions for savings put into desired uses rather than to treat favourably all kind of non-consumption through a low rate of progressiveness.

Secondly, the present incentive measures, e.g., investment allowances, accelerated depreciation, etc., affect the allocation of investible funds among different uses rather than that of income between consumption and saving. Confinement of the incentives to small savings put into such assets as saving bonds and shares and bonds of the public and private corporations operating in the fields most conducive to the economic development could do much more good for increasing the aggregate savings, as the high business incomes would in any case be invested. Nevertheless, it is no doubt necessary to use incentive measures to direct the investible funds in the hands of high income classes to the desired fields. But this policy should be in harmony with the general objectives and strategy of the Plan. The present measures are inefficient also from this point of view. The right kinds of inducement seem to be those encouraging the production methods using more of the abundant factor, that is, labour. Finally, the clash between the indirect taxation of capital goods and incentive measures of the direct taxation requires to be remedied. The refund of the Production tax levied on the capital goods of labour-using character, which are used in the approved industries, might have favourable effects on capital formation.

The above suggestions may be criticized on the ground that they would cause revenue losses for the government. The explanations referring to the composition of expenditures and investments in Chapter I and to the saving behaviour of the private sector in Chapter IV have shown that the amount of saving put into the uses which may be desirable from the standpoint of the Plan's objectives is so small that their exemption from taxation would not lead to any significant loss of public revenue. However, the problem boils down to that of administrative efficiency as the choice of the right kind of exemptions and exceptions and avoidance of the creation of loopholes for tax evasion are the crux of the matter.

CHAPTER 6

DEFICIT FINANCING OF THE PLAN

It has been pointed out in Chapter 3 that the Development
Plan adopts the principle of not resorting to deficit financing.
We have shown there that the Plan aims at obtaining the additional
savings required from the public sector through increases in the
public revenue proper (taxes, the S.E.E.'s surpluses, and borrow-
ing from the public), the limitation of increases in the public
current expenditures, and foreign aid.   As seen in chapter 5, the
tax targets of the Plan have not been fulfilled, though a consider-
able increase in the tax/income ratio has been achieved.   Due to
the limited scope of this dissertation as well as to the seriously
incomplete data, it is hardly possible to examine in detail the
non-tax revenues and current expenditures of the public sector.
However, an attempt will be made in Section I below to have a
bird's-eye view of the developments in the public revenues and
expenditures during the early years of the plan period, that is,
1962-1965.   This will provide the answer to the question whether
deficit financing has been resorted to in the course of the plan
implementation.   In Section II, the ways and means of financing
the deficit, if any, will be reviewed, and their repercussions on
the general equilibrium of the economy will be analysed.

I

Deficit financing may take place in the private as well as in the public sector. But it has become a common practice to use the term "deficit financing" for the public sector. Nevertheless, the definition of deficit financing of public capital formation varies considerably in practice. In the U.S. the term "deficit financing" is generally used to mean any expenditure by the government that is in excess of its current revenues. Borrowing from the public is therefore included in the measurement of deficit in the budget[1]. In India, however, only expenditure in excess of current revenues and non-bank borrowings is regarded as "deficit spending" or "deficit financing"[2]. In Turkey, neither the Budget Preambles nor the Development Plan and the Annual Programmes adopt a certain concept of deficit financing. In this essay the term "deficit financing" will be taken as meaning "the excess of public capital formation over any surplus of genuine government revenue left after covering other non-capital government expenditure, due adjustment being made for transfer items[3].

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1. R. J. Chelliah, op. cit., p. 150.

2. Ibid.

3. H. W. Singer, "Deficit Financing of Public Capital Formation", Social and Economic Studies, Vol. 7, No. 3, p. 85.

The public sector in Turkey may be conceived of at four
levels: Central Government, the S.E.E.'s,Administration with
Revolving Funds, and Local Administrations. The major part of the
public capital formation takes place in the first two levels, while
the Administrations with Revolving Funds and Local Administrations
have only limited funds for investment purposes.

Table 35 summarizes the available information concerning
the Central Government's "free" surplus during 1962-1965. Of the
total current revenue the parts coming from the direct and indirect
taxes have already been subjected to a critical analysis in chapter 5.
It has been shown there that in spite of the considerable increases
in the total tax revenue/G.N.P. ratio resulting from the tax reform
attempts since 1962 the revenues from both the direct and indirect
taxes have fallen short of the tax targets set in the Plan and the
Annual Programmes. The revenue from the Saving Bonds, which is
included in the item (3) in Table 35 has been dealt with in chapter
4[1]. The other public revenues, which are also included in the
item (3) in Table 35, comprises the Treasury shares taken from some
imports, the revenue on the State property, etc. They amounted to
345 million T.L. in 1962, 800 million T.L. in 1963 and 725 million
T.L. in 1964. When they are compared with the targets set in the

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1. See chapter 4, pp. 132 & 134-135.

TABLE 35

CENTRAL GOVERNMENT BUDGETS, 1962-1965[1].

T.L. Million

	Actual			Expected[4]	Pro-gramme
	1962	1963	1964	1965	1966
1. TOTAL CURRENT REVENUE	8,226	10,089	10,921	12,850	14,360
2. Direct taxes	2,336	2,752	3,024		3,735
3. Indirect taxes[2]	5,527	6,945	7,495		10,060
4. Annexed budgets	363	392	402		565
5. CURRENT EXPENDITURE	5,787	6,546	6,785	8,050	9,080
6. CURRENT SURPLUS (1-5)	2,439	3,543	4,136	4,800	5,280
7. TRANSFERS	1,680	2,536	3,251	3,142	4,202
8. Debt repayments	801	799	1,224		
9. Interest payments	255	308	391		
10. Other current transfers[3]	170	304	428		
11. State Economic Enterprises	240	380	645	760	
12. Other capital transfers[3]	214	745	563		
13. Central Government's FREE SURPLUS (6-7)	759	1,007	885	1,658	1,078

1. Consolidated General and Annexed Budgets.
2. Includes Saving Bonds and other revenues of the General Budget, but excludes Counterpart Funds.
3. Includes transfers to municipal and local governments.
4. Estimated on the basis of the data available in October 1965.

Sources: O.E.C.D., "Economic Surveys, Turkey 1965/1966", Paris Feb. 1966, p. 32;
S.P.O., A Summary of 1966 Annual Programme, (mimeographed), pp. 64; 69; 70 and 78.

Annual Programmes, which are 210 million T.L. and 600 million T.L.

for 1963 and 1964 respectively[1], the outcome must be regarded as

satisfactory.

The revenue on the Annexed Budgets is expected in the Plan

to grow at a rate of 5% per annum[2]. The actual revenue was

363 million T.L. in 1962 and is expected to be 443 million T.L. in

1965, giving a rate of increase of 6·8% per annum. Remembering

that the price index has in that period risen, on average, by

3·7% annually[3], the growth of the revenue on the Annexed Budgets

at constant prices has so far lagged behind the Plan targets. The

revenue on the Annexed Budgets has also fallen short of the targets

of the Annual Programmes, which have envisaged a revenue of

450 million T.L. on the Annexed Budgets in 1963, 550 million T.L.

in 1964 and 553 million T.L. in 1965[4].

Given the current revenue of the Central Government, the

size of the current surplus (saving) of the Central Government is

1. The 1963 Annual Programme, p. 260; The 1964 Annual Programme,
   p. 267.
2. See chapter 3, p.97 , of this essay.
3. See chapter 4, p.110n, of this essay.
4. The 1963 Annual Programme, p. 260; 1964 Annual Programme, 267;
   1965 Annual Programme, p. 305.

determined by the size of the current expenditures.   The Plan's

projections concerning the public current expenditure were already

explained in chapter 3, pages 97-98. Table 36 gives the realized

current expenditure figures as compared with the Programme figures.

The realization has fallen short of the Annual Programme figures

throughout the period under consideration.   The short_falls have

been caused by the failure of the public revenues to reach the

target figures as well as by impediments in the legislation relating

to expenditures[1].   However, the growth in the realized current

expenditures has been in line with the Plan's projections.   The

realized current expenditure was 5,787 million T.L. in 1962 and is

expected to reach 8,050 million T.L. in 1965, reflecting an average

rate of growth of 11·6% per annum.   If the rise in the general

price level in the period 1962-65 is taken into account, the average

rate of annual increase in the realized current expenditure at con-

stant prices appears to be only slightly below the rate envisaged

by the Plan, which is 8·7% per annum.

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1. S.P.O., A Summary of 1966 Annual Programme, p. 68.   It is
    stated there that since such laws as those governing the
    General Accounting, tender and contracts "prefer security
    rather than speed in the State activities, they impede to
    a certain extent the realization of the public expenditures
    in time even though the equivalent sums are available."

TABLE 36

CURRENT PUBLIC EXPENDITURE AS PROGRAMMED & REALIZED, 1962-1965.

(At current prices,
Million T.L.).

	1962	1963	1964	1965
Programme	6,195	7,160	7,331	7,800
Realization	5,787	6,576	6,785	8,050
Shortfall	408	614	546	- 272
Realization in %	93·4	91·4	92·5	103

Sources: The realized figures are from Table 35 above.
The Programme figures for 1963-1965 are from
S.P.O., A Summary of 1966 Annual Programme,
Table 11, p. 69.
The Programme figure for 1962 is from O.E.C.D.,
"Economic Surveys:
Turkey 1963", Paris May 1963, Table 13, p. 44.

The biggest increases took place in 1963 and 1965 - 13% and 18%, respectively - the increase in 1964 being relatively small. The growth of the current expenditure in 1965 has, however, been influenced by the rise in the general price level to a greater extent than that in 1963 and 1964. In fact, the general price index has risen by 8% in 1965 over the previous year, while it has recorded an increase of 4% in 1963 and a fall of about 0·5% in 1964.

The shortfall in the actual current expenditure in 1962 in comparison with the Programme figure was due mainly to the saving of 200 million T.L. salaries for unfilled posts and to the special cuts imposed by the authorities[1]. The actual increase of 759 million T.L. in the current expenditure in 1963 can partly be explained by the special cuts in 1962 and by the effective cost (about 400 million T.L.) of the long-delayed 15% rise in the public sector salaries and wages[2]. The 1964 forecasts of current expenditure were 12% above the 1963 outcome. But the actual increase turned out to be about 3.7% because of the government's decision in June 1964 to check the increase of current expenditure, which had been taken in view of the lower than planned revenue prospects[3]. The 1965 Budget had originally foreseen a 15% rise in current expenditure over actual 1964 current expenditure, but was subsequently amended so as to set the current expenditure 25% above the 1964 actual current expenditure, principally to allow higher military expenditures[4]. The latter ratio is, however, unlikely to materialize. During the first ten months of fiscal year 1965 (March through December), current expenditure was 11% higher than

1. O.E.C.D., "Economic Surveys, Turkey 1963", Paris May 1963, p. 43.
2. Ibid, p. 43; and, O.E.C.D., "Economic Surveys, Turkey 1963-64", Paris Aug. 1964, p. 28.
3. O.E.C.D., "Economic Surveys, Turkey 1965-1966", Paris February 1966, p. 31.
4. Ibid. p. 16.

in the same period of 1964[1].   Nevertheless, the S.P.O. estimates

on the basis of the data available in October 1965 that the 1965

current expenditure may be realized around 8,050 million T.L.,

18% above the actual 1964 current expenditure (see Table 35).

As to the pattern of actual current expenditure, it is not yet

known if the necessary priorities envisaged in the Plan to be

granted to expenditures on health, education and agriculture have

been observed or not[2].

   With the total current revenue increasing at a greater

pace on average than the current expenditure, a growing surplus

has been achieved on the Central Government Budgets during 1962-

1965.   Actually, the current revenue during 1962-1965 has

increased at an average rate of 16% per annum against an average

increase of 11·6% per annum in the current expenditure[3].   Conse-

quently, the current surplus of the Central Government went up

from 2,439 million T.L. in 1962 to 4,800 million T.L. in 1965,

increasing at an average rate of 25·3% per annum.   The share of

the current surplus in the current revenue of the consolidated

General and Annexed Budgets has varied between 30 and 38 percen-

tages during the period 1962-65.   However, as seen from Table 35,

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1. O.E.C.D., "Economic Surveys, Turkey 1965/1966", Paris Feb. 1966,
   p. 16.
2. Ibid., p. 52.
3. Both rates have been calculated as compound rates on the basis
   of data given in Table 35 above.

only a part of the excess of the current revenue over the current expenditure is available for investment directly from the General and Annexed Budgets if due allowance is made for transfer payments.

Table 35 shows that the transfer payments of various kinds have been a great drain on the savings of the General and Annexed Budgets during the plan implementation so far. They swallowed up 69% of the current surplus in 1962, 71% in 1963 and 78% in 1964. This rising trend was checked in 1965, when the ratio of the transfer payments to the Central Government's surplus was cut down to 65%. The major element in the total transfer payments is the payments of debt and interest on them,which together amounted to 43%, 31% and 39% of the current surplus in 1962, 1963 and 1964, respectively. The foreign debts, which accumulated in the 1950's far exceeded the debt-payment capacity of the economy[1]. The consolidation of the foreign debts in 1959 deferred debt payments so as to start falling due during the plan period. The Plan's projections of the foreign debt payments have turned out to be considerably smaller than the actual figures. Excess of the public debt over the Plan estimates was 255 million T.L. in 1963, 469 mil-

1. S.P.O., 1965 Annual Programme, p. 303. The foreign debt payments of Turkey used up 28·8% in 1960, and 38% in 1963, of her export proceeds. (The Ministry of Finance, Budget Preamble for the Fiscal Year 1966, p. 135).

lion T.L. in 1964 and is expected to be 946 million T.L. in 1965[1].
The transfer payments to the S.E.E., local governments and private
establishments also have accounted for an important portion
(25 to 40%) of the current surplus of the Central Government.
Contrary to the Plan's projections, the S.E.E. and the local govern-
ments have not yet been able to cater from their own resources for
their total expenditures.

Subtracting the total transfer payments (item '7' in
Table 35) from the excess of the current revenue over the current
expenditure (that is the item '6' the current surplus) gives the
Central Government's Free surplus which can be used for capital
formation purposes by the General and Annexed Budget Administra-
tions.   As seen from Table 35, changes in the magnitude of the
free surplus during the Plan period have not had any definite trend,
varying in accordance with the changes in the current revenue and
expenditure and transfer payments.

Having reviewed the magnitude of the capital funds created
within the General and Annexed Budgets, we shall now turn to the
funds generated in the State Economic Enterprises (S.E.E.) during
the plan implementation.   For a number of years (particularly,

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1. S.P.O., 1965, Annual Programme, p. 303.

since the early 1950's), these enterprises as a group have not been able to finance themselves even their current operations[1].   All their investment expenditure as well as their operational deficit, have therefore had to be financed through short-term borrowing from the banks, use of counterpart funds and receipt of surpluses of the pensions and social security institutions or, as was the case in 1958 and 1959, through non-payment of premium on imports and through accumulating tax arrears[2].

Despite the increases in 1958 and 1959 in the prices charged by these enterprises their financial situation did not improve.   Their overall deficit in 1960 was 1,200 million T.L., including investment expenditure[3].   The prices of many of the products of these enterprises were again raised in 1960.   The following year, most of their outstanding short-term debts to the Central Bank (3,900 million T.L.) were consolidated and turned over to the Treasury as very long-term claims.   Their tax arrears (800 million T.L.) were also remitted[4].   In spite of these important

1.   O.E.C.D., Turkey 1960/61, p. 17.

2.   O.E.C.D., "Turkey 1960/61", Paris 1961, p. 17.

3.   Ibid.

4.   O.E.C.D., "Turkey 1962/63", Paris 1963, p. 34.

measures the financial position of the S.E.E.s did not improve

sufficiently[1]. Although the investible funds created by the S.E.E.

during the period 1962-1965 have been around the magnitude envisaged

by the Plan, the ratios of the realized funds to the Annual Pro-

gramme figures have been very low except in 1963. In fact, the

Development Plan envisaged that the S.E.E.s would create a total

surplus fund of 3,190 million T.L. in 1962-1965 at 1961 prices

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1. The need for a radical reform of the S.E.E. had been felt for
   some years, and in 1961 a group of foreign experts was invited
   to study the situation and to make proposals for their reform.
   The general study and the twenty detailed sector studies they
   produced was published by the O.E.C.D. as the "Consolidated
   Report on the S.E.E.s in Turkey", Paris, December 1961.
   According to this Report the unhealthy situation of the S.E.E.
   is the outcome of the following factors:-

   (a) The pricing policies followed by the Government have in
       too many cases imposed on the Enterprises the burden of
       subsidising consumption items;

   (b) There has been a misuse of resources through misdirected
       or unfinished, or, in some cases, excessive investments;

   (c) there has been no proper cost accounting because fixed
       assets were not adequately valued;

   (d) an important part of investment has been financed out of
       short-term bank credits;

   (e) the lines of command inside the Enterprises and between
       them and the Government are not sufficiently clearly drawn,
       so that the benefits of neither centralization nor
       decentralization are obtained;

   (f) there is a serious staffing problem, partly linked to the
       comparative levels of remunerations. (Ibid., p. 21).

TABLE 37

STATE ECONOMIC ENTERPRISES' OWN RESOURCES, 1962-1966.

Million T.L.

	Actual			Revised Pro-gramme	Pro-gramme
	1962	1963	1964	1965	1966
A. PRODUCTIVE S.E.E.:					
1. Current gross profits	11	- 5	161	421	-
State Railraods	- 292	- 366	- 390	- 245	-
Others	303	361	551	666	-
2. Depreciation	568	607	674	746	-
3. Short-term operations[1]	- 25	233	- 64	342	-
4. Total cash resources (1+2+3)	554	835	771	1,509	-
5. Direct taxes	- 232	- 217	- 196	- 279	-
6. Debt payments	- 568	- 724	- 577	- 855	-
7. Cash outflow (5+6)	- 800	- 941	- 773	- 1,134	-
8. Net cash position (4-7)	- 246	- 106	- 2	375	310
B. NON-PRODUCTIVE S.E.E.:					
9. Own resources of non-prod. S.E.E.	574	982	1,036	1,409	1,484
Reinvestment	233	399	289	332	201
Credits to productive S.E.E.[2]	341	583	747	1,077	1,283
C. Total own RESOURCES of S.E.E. (8+9)	328	876	1,034	1,452	1,794

1. Difference in stocks, and payable and receivable accounts.
2. Credits from State Investment Bank, Pension Fund and Workers Insurance Fund.

Sources: Re-arranged from Table 13 in O.E.C.D., "Economic Surveys, Turkey 1965/66", p. 37; and Table 1 in the Ministry of Finance, Budget Preamble for the 1966 Fiscal Year, p. 147.

(see Table 21 of this essay).   The actual outcome, which is
3,088 million T.L. at current prices for the period 1962-1965 (see
Table 38 below), lags behind the Plan's target only to the extent
of 100 million T.L. if the rise in the price level is neglected.
But the Annual Programmes have set much higher targets for the
funds to be created by the S.E.E. than those set by the Develop-
ment Plan.   As seen in Table 38, the rate of realization in
relation to the Annual Programme figures was as low as 71 and 58
percentages in 1964 and 1965 respectively.

TABLE   38

THE S.E.E.s OWN RESOURCES AS PROGRAMMED & REALIZED, 1962-1965.

(million T.L.)

	1962	1963	1964	1965
Programme	546	856	1,454	1,452[1]
Realization	328	876	1,034	850[2]
Shortfall	218	- 20	420	602
Realization in %	60	102	71	58

1. It was originally 1,825 million T.L. but reduced to
    1,452 million T.L. in the revised Programme.
2. the estimate based on the data available in October 1965.

Sources: The Programme figure for 1962 is from S.P.O. Program
          for the Year 1962, Table 14.
          The Programme figure for 1965 is from Table 37 above.
          The Programme figure for 1963 and 1964 are from S.P.O.,
          A Summary of 1966 Annual Programme Table 12, p. 70.
          The Realization figures for 1962-1964 are from Table 37
          above;   that for 1965 is from S.P.O., 1966 Annual
          Programme, p. 70.

The productive S.E.E.s as a whole showed only a very small profit (11 million T.L.) in 1962 and a small loss (5 million T.L.) in 1963. In 1964 an overall profit of 161 million T.L. was reported. However, due to inadequate depreciation allowances, the real situation may be one of annual losses[1]. The overall situation, however, is misleading. Most of the losing Enterprises are in the public transportation sector; in particular the deficit of the State Railways has increased steadily during 1962-1964[2]. The remaining S.E.E.s have improved their profits steadily by raising their prices (e.g., coal, iron and textiles)[3].

The stagnation of demand during 1961 and 1962 resulted in low rates of activity and/or large accumulation of stocks in many

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1. "The depreciation allowances in question are based on nominal acquisition values of fixed assets; taking into account the change in the exchange rate and in the internal price level, they represent probably between a third and a half of "normal" depreciation". (O.E.C.D., Turkey 1962/63, Paris, May 1963, p. 20).

2. In Turkey both rail and road transporters are subsidised. The licence fees, transportation and fuel taxes paid by vehicle owners cover only about half the annual costs of maintaining the highways; and the net cost to the state seems to be roughly equivalent to the Railway's deficit. Therefore, a general rise in road transport taxes may be suggested to permit the Railways to adjust their prices accordingly. (O.E.C.D. Turkey 1965/66, Paris, February 1966, p. 38).

3. Ibid., p. 36.

state enterprises.   Accordingly, the item "short-term operations"
(changes in stocks, and payable and receivable accounts) in Table 37
showed a negative change of 25 million T.L. in 1962.   As the econo-
mic activity became brisk in 1963, the selling off of the stocks
provided an increase of 233 million T.L. in the current resources.
The relative stagnation of demand in 1964 again caused an increase
of 64 million T.L. in stocks.   The total cash resources, including
depreciation allowances, have thus amounted to 554 million T.L. in
1962, 835 million T.L. in 1963 and 771 million T.L. in 1964.   But
the cash outflow of the productive S.E.E. in the form of direct
taxes and debt payments has exceeded their total cash resources,
though this operational deficit has shrunk from 246 million T.L. in
1962 to 2 million T.L. in 1964.

In contrast to the productive S.E.E., the non-productive
S.E.E. (Pension Fund, Workers Insurance Fund, State Investment Bank
which formerly was Amortization and Credit Fund, and the Provinces'
Bank) have created surplus funds which have far exceeded the
operational deficits of the productive S.E.E.   The consolidated
resources of the S.E.E. have consequently been of some positive mag-
nitudes, thus contributing to their capital formation expenditures.
The total own resources of the S.E.E. have increased from 328 mil-
lion T.L. in 1962 to 876 million T.L. in 1963 and to 1,034 million
T.L. in 1964.   Despite a more than three-fold increase during

1962-1964, the resources of the S.E.E., as will be seen, have fallen considerably short of their investment expenditures.

The programme for 1965 provides for 1,509 million T.L. of gross internal cash resources. Losses of the railways are planned to decrease by 145 million T.L. to 245 million T.L., and profits of other non-financial (productive) enterprises are expected to reach 666 million T.L. Depreciation allowances will rise to 746 million T.L. and short term operations are planned to show a surplus of 342 million T.L.

Contrary to the expectations of the Programme for 1965 a negative development started in 1965. Although the State Railways have been able to reduce their losses approximately by the amount planned[1], the tariff adjustments made by the Railways affected adversely the Turkish Coal, and Turkish Iron and Steel Companies, whose price increases were cancelled by the Government because their products were basic goods[2]. Moreover, the collective agreements signed with the Trade Unions in 1964 and 1965 have also affected adversely the capacity of the S.E.E. to generate resources. Furthermore, while the production costs of the Turkish Sugar Factories went up because of the rising of beet prices, the sugar prices were not

1. O.E.C.D., Turkey 1965/66, Paris February 1966, p. 37.
2. S.P.O., A Summary of 1966 Annual Programme, p. 30.

raised.   In addition, the sugar production was in excess of consump-
tion, resulting in increased stocks.   Apart from these new adverse
developments, the Turkish Airlines and the State Maritime Bank
continued operating below capacity /because of being unable to compete with
foreign transportation firms[1].   In view of these facts it is not
surprising that the total own resources of the S.E.E. is expected
to materialise at 58% of the Programme target.

Apart from the General and Annexed Budgets and the S.E.E.s,
there are Local Administrations and the Administrations with
Revolving Funds which also create some investment funds.   In the
Development Plan they are expected to be self-sufficient.   The
available data on their revenues and expenditures are scanty and
unreliable[2].   It is therefore not possible here to analyse their
developments.   However, in order to have a complete picture of the
financing of public capital formation, the O.E.C.D.'s figures for
the investment and surplus funds of these Administrations are used
in Table 39.

As seen from this table, the public savings in 1962-1965
have fallen well short of the investment undertaken in the same
period.   It is nevertheless remarkable that the shortfall of public

1. Ibid., p. 31.

2. I.B.R.D., op. cit., paragraph 381.

TABLE 39

FINANCING PUBLIC INVESTMENT, 1962-1965.

(million T.L.)

	1962	1963	1964	1965
A. PUBLIC INVESTMENT:	4,236 (7·6)	5,142 (8·2)	5,660 (8·5)	6,555 (9·5)
1. General & Annexed Budgets	2,247	2,835	3,187	3,800
2. S.E.E.s	1,529	1,617	1,760	1,950
3. Revolving Funds	118	254	250	286
4. Local Administration	342	436	463	519
B. PUBLIC SAVING:	1,787 (3·2)	2,879 (4·6)	3,180 (4·8)	4,073 (5·7)
5. Central Government's Free Surplus	759	1,007	885	1,658
6. S.E.E.'s Own Resources	328	876	1,034	850
7. Transfer to S.E.E.'s from the Budget	240	380	645	760
8. Revolving Funds	118	242	216	286
9. Local Administrations	342	374	400	519
C. DEFICIT FINANCING:	2,449 (4·4)	2,263 (3·6)	2,480 (3·7)	2,482 (3·5)

Note: The figures inside brackets represent percentages of
G.N.P.

Sources: The Public Investment figures ((1) to (4)) for
1962-1964 are from O.E.C.D., Turkey 1965/66,
Table 10, p. 34;

That for 1965 from S.P.O., 1966 Annual Programme,
Table 11, p. 65.

The figures for items (5), (6) and (7) are from
Tables 35, 37 and 38 of this essay. The figures
for items (8) and (9) were taken from Table 11 in
O.E.C.D., ibid., p. 34.

savings has been steady around 2,400 million T.L. whereas the public

investment in 1965 was about 55% higher than in 1962.   This means

that the proportion of public investments financed with public

savings has increased during the period 1962-1965.   Actually, the

ratio of the public saving to the public investment was about 42%

in 1962 but went up to 56% in 1963 and 1964, and to 62% in 1965.

This favourable development[1] has been the outcome of the fact that

public savings have increased annually by 31·6%, on average, during

1962-1965 inclusive, while public investments have in the same

period increased, on average, at an annual rate of 15·6%.

II

The major part of the deficit in public savings during the

Plan implementation in 1962-1965 has been covered by the counter-

part funds of foreign aid (see Table 40 below).   In 1962, about

83% of a total deficit of 2,449 million T.L. was financed with

counterpart funds and project credits which amounted to 2,023

million T.L.   The foreign financing in 1963 was large enough to

meet the whole of a 2,263 million T.L. deficit on the saving-

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1. This favourable development may be observed in terms of the
   percentages of G.N.P. (see Table 32), while the ratio of public
   investments to G.N.P. was, during 1962-65, increasing, the
   deficit financing as percentage of G.N.P. was declining.

TABLE 40

DEFICIT FINANCING, 1962-1965

(million T.L.)

	1962	1963	1964	1965
A. TOTAL DEFICIT:	2,449	2,263	2,480	2,482
B. FOREIGN FINANCING:	2,023	2,292	1,507	1,500
Counterpart Funds to Central Government.	1,062	1,796	1,303	-
Counterpart Funds to S.E.E.	769	229	36	-
Project Credits to S.E.E.	192	267	168	-
C. Implied DOMESTIC BORROWING (A-B):	426	- 29	973	982
Long-term Domestic Borrowing	-	-	200	400
Short-term Domestic Borrowing	426	-	773	582

Sources: For (A), Table 39 above.

For (B) and (C), O.E.C.D., Turkey 1965/66, p. 34, Table 11.

investment account of the Public Sector. But, in 1964, only about 65% of the 2,480 million T.L. deficit could be covered by foreign financing. The total saving deficit in 1965 is expected to be around that in 1964; and the foreign financing, although scheduled in the 1965 Programme to reach 2,070 million T.L.[1], may also be

1. O.E.C.D., Turkey 1965/66, p. 34, Table 11.

expected to materialize at its 1964 level as its March-December 1965

magnitude was almost equal to that of the period March-December 1964[1].

What is left after a part of the total saving gap is covered

by the foreign financing must have been made up through domestic

borrowing. In fact, of the total public investment during the period

1962-1965, an amount of 426 million T.L. in 1962 and of something

around 1,000 million T.L. in 1964 and 1965 have been realized as

being financed by domestic borrowing. Domestic borrowing in 1962

was completely short-term borrowing while in 1964 and 1965 it was

partly long-term and partly short-term borrowing from the Central

Bank and Commercial banks[2].

In the discussion of the effects of the above-reviewed

deficit financing it must be mentioned at the outset that the deficits

on the saving-investment account of public sector shown in Table 40

are ex-post magnitudes. The ex-post "finance" of the government

deficit is itself an outcome of the interaction of government deficit

spending in a given period with other aggregates and propensities in

the economy.

The scope for non-inflationary deficit financing is indicated

by the nature of the balance between the sum total of investment

1. Ministry of Finance, Budget Preamble for the 1966 Fiscal Year,
   p. 107, Table 61.
2. The role of these borrowings will be dealt with in due course in
   the following discussion.

projects, including those financed by public deficit, and the sum
total of what persons and companies would be willing to save at the
current level of prices[1].   If the former sum does not exceed the
latter at the current level of prices, even the financing by the
Central Bank of the whole of the deficit required for public works
will not be inflationary[2].

Intended saving and investment at the current price level
of the private sector cannot be measured.   The figures for the
private sector's savings and investment which have been referred to
in this essay are ex-post magnitudes, which themselves have been
influenced by public deficit spending.   Saving and investment ratios
of the private sector in the pre-plan period cannot also be relied
on for an estimate of the ex-ante saving and investment of the private
sector during the Plan period, since the pre-plan period has been
characterized by extensive deficit financing, strong stabilization
measures, political instability and, finally, a military revolution.

In practice, governments may be able to learn about the
balance between investment and saving by trial and error[3].   Whether

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1. R. F. Harrod, "Economic Planning and Capital Investment", in
    Capital Formation and Investment in Industry, Istanbul 1963, p.313.
2. Ibid., p. 313.
3. R. F. Harrod, op. cit., p. 314.   In learning about that balance,
    authorities may rely on various indicators such as price indexes,
    stock changes, interest rates in unorganized money markets.

the Turkish Government has been able to control its deficit spending during the Plan implementation by means of such a trial and error method may be observed from the price indices shown in Table 41.

Wholesale prices in Turkey present a strong seasonal pattern, usually declining from late spring to late summer and rising throughout the rest of the year[1].   Following the dismantling of many price controls during 1961 and 1962, the average price level rose by 5·7% in 1962 and by 4·2% in 1963.   In 1964, wholesale prices were stable.   But the seasonal upturn in the autumn of 1964 was unusually pronounced, and the general index failed to make the seasonal down turn during the spring and summer of 1965.   The average price level in the third quarter of 1965 was 12% above the same quarter of 1964.   The increase in cost-of-living (Istanbul) has been relatively less, about 6% in the third quarter of 1965 over that of a year earlier.

The upward trend of wholesale prices and cost-of-living during 1961-1965 may be taken as the indicator of the presence of excess demand.   The price rises, however, have been moderate till 1965, particularly in comparison with the average rate of 13·5% rise per year during 1953-1960.   The Government has been successful in

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1.   O.E.C.D., Turkey 1965/66, p. 11.

TABLE 41

PRICES AND WAGES, 1961-1965

	1961	1962	1963	1964	1964				1965		
					I	II	III	IV	I	II	III
WHOLESALE PRICES: (1953=100)											
General Index	246	260	271	269	274	270	261	271	286	291	292
Good	239	260	· 271	266	274	269	255	265	284	289	289
COST OF LIVING (Istanbul): (1953=100)											
General Index	236	245	261	263	264	263	261	266	271	273	278
Food	242	255	273	272	274	271	269	275	282	284	291
MONEY WAGES (T.L.)	15·64	16·52	17·91	18·39						19·46	18·65
INDEX OF REAL WAGES[1]	100	101	103	105						108	101

1. Calculated by deflating money wages by the general index of cost-of-living.

Sources: The price indexes are from O.E.C.D., Turkey 1965/66, p. 61.

Money wages from S.P.O., 1966 Annual Programme, p. 35.

maintaining an aggregate investment expenditure during 1962 and
1963 which was not significantly out of line with what the public
was prepared to save plus the current account deficits.   The
current account deficits, which amounted to 4·4% of G.N.P. in 1962
and 4·8% in 1963, played, of course, an important part in raising
the supply of total savings towards the level of total investment
expenditures.

Following the significant rises in the level of real
national income during 1962 and 1963, a slowing down of economic
activity first showed itself by the end of 1963 and permeated the
whole economy in the first half of 1964.   This could have been
considered as a sign of the development of a deflationary gap,
probably due to a lag in the adjustment of the consumption level
to the exceptionally high level of national income attained in
1963.   In addition, while measures were introduced to curtail
investment in housebuilding and to curb imports which also led to
the curtailment of investment in some sectors, no offsetting in-
crease in public investment was undertaken.   On the contrary, with
the purpose of limiting public spending to public revenue, the
Government cut continually appropriations of current and invest-
ment expenditures during the first half of 1964.

The stagnation of economic activity has eventually forced the Government to take recourse to deficit financing from July 1964 on. But the scale of the deficit incurred and the accompanying policy of monetary expansion have, as will be seen soon, resulted in an excess demand during 1965, causing a rapid and continual rise in the general price level.

The rising prices during 1961-1965 have not resulted in falling real wages. As shown by Table 41, real wages have continually risen till the second half of 1965. Although the money wage rates given in the table represent average daily earnings of only insured workers, they could, at least, be considered as indicating that the real wages have not fallen, if not risen. In view of the growing strength of trade unions and the sensitiveness of the public against disparities in income distribution, it is pretty safe to assume that the rise in money wages would keep up with the price rises. This would prevent the price rises from effecting substantial shifts in income distribution in favour of profit earners. Under these conditions, no increase in the level of real savings and investment could be expected to result from inflationary deficit financing. If inflationary deficit financing is halted, a stability may be attained at a higher level of prices without substantial change in savings.

A wage-price spiral which looms large for the rest of the plan period can occur only if some means are found to finance the prevailing scale of production at the higher level of prices and costs[1]. The ways of financing public sector's deficit and the monetary policy followed so far have provided the public with the necessary liquidity. The biggest part of the excess of public investment over public saving was financed by the use of counterpart funds. There is a general belief that increasing public investment by the extent of the available counterpart funds is not inflationary.[2]. As a matter of fact, investment can be stepped up without causing inflation only to the extent that the volume (not value) of consumption of domestic output is curtailed consequent upon the arrival of foreign aid, which creates counterpart funds[3]. A deficit on the balance of current account is due to the existence of an excess of ex-ante investment over ex-ante savings.

1. There is of course some flexibility in the capacity of the public to use a given supply of money (changing velocity of money "V"). But this flexibility is limited, and the limit is quickly approached if prices and wages rise while the money supply is unchanged.

2. This belief is shared by the S.P.O. and Ministry of Finance as understood from the Development Plan and Annual Programmes and the Budget Preambles.

3. This is the reasoning applied by R. F. Harred to the assessment of the inflationary effects of the use of counterpart funds arising from P.S. 480 Aid. See his Sales Proceed Funds and Inflation, in Capital Formation......., op. cit., pp. 227-231.

However, the excess demand arising from the excessive desired investment would have worked itself out through price rises had the means to accommodate the current account deficit been unavailable. The availability of foreign aid may help divert some demand from domestic products to imported goods and maintain price stability. But there is no reason why the decrease in consumption of domestic output must be equal in volume (or in value at existing prices) to the foreign aid creating counterpart funds. If this is so, it is unlikely that the whole of the currently accruing counterpart funds could be used to finance additional investment without causing inflation.

What seems to be an even greater fallacy as regards the counterpart funds is that the counterpart funds standing over from a previous period could be used to finance additional investment without causing inflation. In 1964 and 1965, the counterpart funds used by the Central Government and S.E.E. exceeded the total current account deficits in those years. Since not all the foreign aid generates counterpart funds[1], the public sector must have used the outstanding counterpart funds during 1964 and 1965. This is exactly similar in its effects to the financing of public deficit through

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1. The counterpart funds account in the Central Bank of Turkey is credited with an amount equal to the 90% of the Turkish Lira equivalent of the foreign aid received from the U.S.A.. The remaining 10% is put into a sight deposit account to be used by the Government of the U.S.A. for its expenses in Turkey. (Central Bank of Turkey, Reports of the Board of Directors,1963, Ankara 1964, pp. 46-47 and Table 25.).

borrowing from the Central Bank, because the opportunity to step

up the public investment consequent upon the arrival of aid-supplied

goods must have been either used in the relevant year, or have not

been used in which case there must have been an increase in under-

and/or un-employment and a loss of domestic output.

To sum up, whether the use of counterpart funds in financing

the public deficit will be inflationary or not may be estimated

according:-

(a) to what extent the consumption of domestic goods will be

curtailed in consequence of the receipt of aid-supplied

goods and

(b) to the excess of what all private sources are prepared

to save at the existing level of prices over private

capital formation[1].

The long-term domestic borrowing by the public sector was in

the form of government bonds sold initially to commercial banks due

to the absence of a private capital-market.   The loans to the

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1. "In Greece and later in Turkey we imported a made-in-America
    Inflation by acquiescing in a volume of welfare projects (Greece),
    industrial development (Turkey), and military spending (both)
    which was quite out of line with what those underdeveloped econo-
    mies support.   In Britain and Norway, which were pursuing a
    socialist policy of over full employment with a high level of
    investment, the question of using the counterpart for additional
    expenditures never seriously arose.   Those sophisticated govern-
    ments would simply inquire solicitously which of the items in
    their already approved budgets we would most like to tell Con-
    gress had been financed with the counterpart of American aid."
    (Harland Cleveland, "The Convalescence of Foreign Aid", American
    Economic Review, May 1959, p. 225).

government will increase deposits which will be partly withdrawn in
the form of currency. And, the larger volume of deposits will com-
pel the banks to hold larger reserves. If banks are loaned up
(having no excess reserves) they can lend to the government only by
holding down their loans to business, since they cannot get additional
resources by rediscounting the long-term government bonds at the
Central Bank. They will be able to reduce their loan portfolios in
the absence of call loans only gradually as outstanding loans mature.
Therefore, it is safe to assume that the long-term borrowings by the
Public Sector during 1964 and 1965 have had inflationary effects to
the extent that banks had some excess reserves and that it took some
time to contract loans to the private sector.

In providing the economy with liquidity, which is necessary
for a wage-price spiral to continue, the third means of covering
public deficit, that is, short-term borrowing from the Central Bank,
has undoubtedly been the most effective factor. Central Bank
credit to the public sector doubled between 1962 and 1963[1]. During
the first half of 1964, the increase in Central Bank credit to
public sector was only about 7% above its level at the end of 1963.

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1. The sources of information in relation to the monetary policy
   which have been referred to in this essay are these: Ministry
   of Finance, Budget Preamble for the 1966 Fiscal Year, pp. 111-
   127; O.E.C.D., Turkey 1965/66 pp. 11-15; I.B.R.D., op. cit.,
   Annex I.

But, following the raising in the mid-1964 of the credit ceilings
on Central Bank loans to the Treasury, Soil Products Office and the
Monopoly Administration, the Central Bank credit to the public
sector reached by the end of 1964 a level 32% above that at the end
of 1963.   Public sector borrowing from the Central Bank has
continued to increase during 1965 and reached by the end of the
third quarter a level about 25% higher than year earlier.   The
short-term public borrowing from the commercial banks has also been
increasing.   It rose from 1,332 million T.L. at the end of 1961 to
1,961 million T.L. at the end of 1964, registering a 50% increase,
and to 2,206 million T.L. by the end of the third quarter of 1965
which is about 14% higher than a year earlier.

The primary monetary expansion described above has of course
led to the secondary expansion by the banking system.   The ratio
of currency to money has been around 40% during 1961-1962.   The
legal reserve ratio maintained by banks against deposits was 20%
until mid-1964 when it was reduced to 10% for time deposits[1].   Apart
from this, banks maintain a cash/deposit ratio around 8%.   Accord-
ingly, the credit multiplier was about 1·75 before mid-1964 and now

1. Time deposits amount to something around 1/5th of the total
    deposits.   Consequently, the weighted reserve ratio for after
    mid-1964 is (4 x 20 + 1 x 10)/5 = 18%.

is about 1·8[1].

Monetary authorities are unlikely to have any influence on changes in currency/money ratio, except for the possibility of reducing it indirectly in the long run by encouraging an expansion of the financial and banking system and changes in payment habits and asset preferences. They may, however, influence the multiplier by changing legal cash reserve requirements against deposits as they did in mid-1964. Moreover, in order to increase the demand for credit, they reduced the maximum rate of interest from 10·5% to 9% on loans to designated industrial enterprises and increased individual rediscounting limits on individual enterprises.

Accompanying these developments have been a rapid expansion of credit and money supply. The consolidated net credit increased from 11,247 million T.L. in 1962 to 15,995 million T.L. in 1964, rising by 42%, and to 18,487 million T.L. at the end of the third quarter of 1965 which is 25% higher than a year earlier. Money supply in 1964 was 40% above the 1961 level. By the end of the third quarter of 1965, it was 18% higher than in the corresponding

1. The credit multiplier is defined as being equal to the reciprocal of c + r (1 - c), where c stands for the ratio of currency in circulation to money and r for the legal or customary reserve ratio maintained by banks against deposits. This multiplier is usually considered as a fairly stable ex-ante coefficient. (J. Ahrensdorf, "Central Bank Policies and Inflation, A case study of Four Less Developed Economies", I.M.F. Staff Papers, October 1959, pp. 274-302.)

period of the previous year.   Part of the increment in the money supply during 1961-1965 was used to finance a 25% increase in production.   Part of the increment has met the growing need for liquidity, which is caused by the growing of the economy more complex and by the expansion of the monetized sector.   Neverthe-less, the monetary demand has exceeded, particularly as from the end of 1964, domestic supply as indicated by the rising prices, though contracting foreign trade deficits have also possibly contributed to the rise in prices.

The money supply has increased at a rate of about 10% p.a. during 1961-1963 when a rather high rate of growth in G.N.P. was achieved at relatively stable prices.   Therefore, a 10% increase per year may be considered as a rough estimate of the safe limit for monetary expansion in Turkey.   The increase in the money supply during 1965 far exceeded this limit.   In December 1965 the authori-ties proposed three monetary measures to limit the further expansion of bank credit and money supply:-

(i)   increasing the required reserve ratio from 10 to 20% on the time deposit increases;

(ii) raising the minimum liquidity ratio against their obligations from 5 to 10% on new increases, and

(iii) reducing the Central Bank's ceilings on advances it was willing to make to individual commercial banks by 10%.

These measures may have some effects on the secondary monetary expansion. But in view of the likely development in the financing of the public sector in 1966, it seems that the monetary authorities would need much more effective measures if they aim at curbing the monetary expansion to any significant extent through influencing the secondary expansion by the banking system. The 1966 Annual Programme envisaged a deficit of 1,738 million T.L. on the Public Sector account. Of this deficit, about 400 million T.L. is estimated to be covered through long-term domestic borrowing and the rest through increasing the tax revenue and S.E.E.'s surpluses. In the light of the past experience, it is hardly possible to be optimistic in respect to the revenue targets. It is therefore likely that a substantial increase will take place in the monetary liabilities of the Banking system, especially the Central Bank, if the Government clings to the 1966 investment programme as scheduled in the 1966 Annual Programme.

CONCLUSION.

This dissertation is intended as a study of the efforts of the
Turkish economy to provide that important prerequisite for its First
Five-Year Plan - its domestic financing.   Its primary aim has been to
provide an appraisal of the efficiency of various financial policies
in increasing the real investable funds, that is, real savings, and
suggestions for a successful financing of the Plan.   Since this is
an empirical study, a large portion of it was devoted to a description
of the structure of the economy and relevant events.

We saw that the realization of the level of investment
required for the attainment of the Plan's main target, that is, a
7% rate of growth per annum, calls for a substantial increase in
the level of domestic savings.   We also saw that this increase
would have to be produced by the joint efforts of the private and
public sectors.   In spite of the fact that the Plan did not
specify precise targets in relation to the savings of the private
and public sectors, the actual saving performance of the private
sector during the early years of the Plan implementation may be
regarded as satisfactory with respect to the increase in its level
both in absolute amount and in relation to G.N.P.   On the other
hand, the actual financial performance of the public sector lagged
behind the Plan's targets.   What is significant, however, is not

the comparison of the two sets (planned and realized) of figures, but the analysis of the factors which have caused the divergency of actual developments from intentions, and the lessons as to the adequacy of policies.

It is a well-known empirical observation that the short-term marginal rate of saving is considerably higher than the long-term (marginal and average) rate of saving[1]. If this fact applies to Turkey, the high rates of private savings during 1962-1964 may be regarded as a result of the lag in the adjustment of consumption expenditures to the rising private disposable incomes. The same rates of growth of the private disposable income as in the period of 1962-1964 may not have the same effects on the saving behaviour of the private sector in the coming years as they did in the 1962-1964 period following the stagnation years since 1957[2]. We therefore believe that the task of raising the private savings/income ratio in Turkey to the level observed in advanced countries

1. G. Ackley, Macroeconomic Theory, The Macmillon Co., New York 1961, pp. 252-266.

2. As a matter of fact, we may assume that if the Plan succeeds in maintaining a high rate of growth relative to that attained in the immediate pre-Plan years, the Turkish public may come to regard this rate of growth as "normal and permanent" and, accordingly, an upward shift may take place in the consumption function of the private sector.

requires some structural changes that may effect a shift to the
right in the saving function of the private sector.   To this
effect, we suggested (a) that measures must be taken against
"demonstration effect", (b) that the present static pattern of
wealth ownership should be so changed that the importance of the
part of wealth which is in the hands of profit-earners would
increase at the expense of the part which serves as a source of
rental income, capital gains or merely prestige, and (c) that
special saving institutions must be formed to work together with
commercial banks in inducing and mobilizing small savings.

With respect to the savings through Government the
financing by the genuine public savings during 1962-1965 of an
increasing proportion of the public investment, which itself has
been increasing at an average rate of 15·6% p.a., was undoubtedly
the most significant development achieved in the Plan implementation
so far.   In this development the highest credit of course is to go
to the unprecedented increase in the total tax revenue.   It is
also equally significant that the coverage of the tax system has
been extended, and that some attempts have been made to manipulate
the tax policy with the purpose of inducing capital formation.

Our appraisal of the taxation policy, nevertheless, was
very critical in parts, especially with regard to the taxation of

the agricultural sector and the incentive measures embodied in
the tax system.   This should not be interpreted to mean that we
regard the taxation policy of the Plan period so far as a failure.
In spite of what we considered the errors in the method of
agricultural taxation adopted by the fiscal authorities and the
abuses of the technique of incentive taxation, the mere fact of
the recognition of the need to tackle these problems gives good
ground for hope that the right methods may eventually be recog-
nized as well.   At the same time, in view of the inconsistencies
between the Plan's priorities regarding the allocation of resources
and the primary features of the taxation policy followed, we could
hardly pass by the warning raised by J. H. Adler: "A large pro-
portion of the death rate of ambitious development programs has
been due to the lack of liaison between the planners and the
authorities in charge of the formulation of fiscal and monetary
policies"[1].

The Plan's dogmatism in rejecting categorically deficit
spending as a method of financing aroused our opposition.   Accord-
ingly, the use of the method of deficit financing in the actual

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1.   J. H. Adler, "The Fiscal and Monetary Implementation of
     Development Programs", American.Economic Review (Papers and
     Proceedings), May 1952.

Plan implementation was not criticized in this essay merely by reason of its nature. We endeavoured to show that a programme of deficit financing of public capital formation could be undertaken without disruptive consequences. At the same time, we showed how the faulty hypotheses concerning the counterparts of foreign aid and long-term domestic borrowing have probably caused the deficit financing policy to create some inflationary pressures. We also showed that, while it was essential to follow an alert monetary policy to prevent a wage-price spiral, the monetary authorities seemed to be losing their grip on the liquidity of the economy, particularly since the beginning of 1965, because of the Government's abuse of the method of deficit financing.

The recommendations embodied in this dissertation are largely in the nature of guide lines. They point towards a general direction rather than lay down a detailed programme for the domestic financing of the Plan. To formulate a proper programme would have required much more study and analysis of the institutions and facts. However, to the extent that the analyses and proposals made here contain some degree of reasonableness, it is hoped that this dissertation may serve as a guide for further study.

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