

Political connectedness and business performance: Evidence from Turkish industry rankings

Gül Berna Özcan^a and Umut Gündüz^b

^a *School of Management Royal Holloway, University of London, Egham Hill,
Egham, Surrey, TW20 0EX, UK*

^b *Faculty of Management, Department of Management Engineering, Istanbul
Technical University, 34367, Besiktas, TURKEY*

Abstract

This paper examines the degree to which political connections affect business rankings through a statistical analysis of Turkey's industry rankings between 2003-2011. The analysis demonstrates that business performance is associated with connectedness through industry and firm level data. We show that political connectedness varies according to a firm's channel of access to obtain favouritism either through direct personal ties or institutional networks. Ideological motivations emerge to be significant in mobilising, shaping and tying firm behaviour to broader political agendas. In the conclusion we discuss the impact of deepening connectedness on long-term business fortunes and political institutions.

Keywords: politically connected firm, business ranking, firm performance,
Turkish industry

Acknowledgements: The authors are grateful to the *Critical and Historical Perspectives on Management Research Group* at Royal Holloway University of London for giving financial support to this study. We thank the anonymous referees and Jonathan Liebenau for their insightful comments.

Political Connectedness and Business Performance: Evidence from Turkish Industry Rankings

1. Introduction

The spread and effects of political connections between firms and politicians are widely acknowledged in business and economics literature. Most quantitative studies set out to examine how politically connected firms' (PCF) financial performance and preferential access to banking and government favours are positively affected by their links to political candidates and parties. These are measured in a variety of ways: higher stock returns,¹ projected earnings and financial forecasts,² access to finance,³ protection against competition,⁴ or the impact of a single political actor's business links on firm performance and policy formulation.⁵

However, along with its perceived advantages to the firm, business-politics relationships also incur societal and economic costs. Scholars broadly agree that political interference in the management of firms can also be harmful to the long-term performance and bring opportunity costs. Such firms survive despite poor operational skills,⁶ have lower returns on assets,⁷ have a negative impact on employment and income distribution,⁸ and even when privatised PCFs underperform their non-connected counterparts.⁹ PCFs seem to be problematic with regard to political justice and allocative efficiency. Such studies see a strong link between political interference in business, corruption and clientelism.¹⁰ Relations between dominant business groups and the state shape the political regime type and institutions,¹¹ the way in which client business networks and lobby groups benefit from and provide selective and pro-business agendas,¹² and how the detrimental consequences of inefficient redistribution and clientelism lead to high inequality and low productivity.¹³

¹ Fisman 2001; Claessens et al. 2008.

² Goldman et al. 2009; Chen et al. 2010.

³ Khwaja and Mian 2005; Dinc 2005.

⁴ Johnson and Mitton 2003.

⁵ Roberts 1990; Acemoglu et al. 2010.

⁶ Bertrand et al. 2007; Boubakri et al. 2012.

⁷ Claessens et al. 2008; Abdel-Baki, 2012.

⁸ Abdel-Baki, 2012.

⁹ Fan et al. 2007; Boubakri et al. 2008.

¹⁰ Kettering 1988.

¹¹ Nam 1995; Guriev and Rachinsky 2005; Adly, 2009; Choi and Thum 2009.

¹² Buğra 1995; Salas-Porras 2005.

¹³ Robinson and Verdier 2003; Abdel-Baki, 2012.

During major economic downturns and/or political changes governmental ties may become critical for business survival and growth. Under such conditions the firm management grows dependent on the political class.¹⁴ The subject of this paper is a period of major transformations in Turkish economy and politics. Since Turkey shifted to liberal economic growth in the 1980s, the most radical developments took place under the moderate Islamist Justice and Development Party (*Adalet ve Kalkınma Partisi*-AKP) from 2002. Securing almost 50 per cent of total votes cast in the 2011 general elections, the AKP gained the mandate to rule for a third term. In government, the party has followed a pro-business agenda with fundamental market transformations: state owned assets were re-allocated through privatisation, foreign direct investment (FDI) reached a record high, municipal and state procurement schemes were expanded, and infrastructure and housing projects generated lucrative contracts. Increasing private sector development produced impressive economic growth with annual GDP growth rates hovering around 5-6 per cent in the ten years since 2002.¹⁵ However, the country has also become one of the most leveraged economies among emerging markets with a net external debt of 413 billion USD, about 51 per cent of GDP.¹⁶

In politics, the AKP worked to transform the secular state with legal purges, bureaucratic cadre building and institutional re-structuring.¹⁷ Growing political pressures unleashed unprecedented protests against the autocracy of Prime Minister Recep Tayyip Erdoğan (hereafter Erdoğan) in May-June 2013 across the country. Uniting around those groups who opposed the construction of a shopping mall in Istanbul's Gezi Park, thousands marched in major cities to express their discontent with AKP rule. The government's heavy-handed use of the police force led to several deaths and injured more than seven thousand protestors.

Many political scientists have argued that the AKP aimed to restructure state institutions according to its ideology and followed partisan policies to nurture a new breed of capitalists in power.¹⁸ Scholars have substantiated their arguments with findings from local business operations¹⁹ and small and medium-sized enterprises.²⁰ Others showed the degree to which the AKP government created its own pro-government press through financial and regulatory pressures on business

¹⁴ Acemoglu et al. 2010.

¹⁵ See: <http://databank.worldbank.org/> (Accessed on 26 June 2013).

¹⁶ Harvey and Bilgic 2013.

¹⁷ Polat 2013.

¹⁸ Atasoy 2009; Öniş 2011.

¹⁹ Author; Bayırbağ 2011.

²⁰ Hoşgör 2011.

groups.²¹ However, the broader impact of AKP ties to business fortunes have not been addressed systematically. By studying data of the top 1,000 companies of the Istanbul Chamber of Industry (*İstanbul Sanayi Odası*- commonly known as ISO) between 2003-2011, business connections of leading AKP members and pro-government business associations, we are able to examine the following questions: i) to what extent do connected firms show different performance indicators in their ranking mobility vis-à-vis their non-connected peers? ii) does the type of political connectedness through personal ties and institutional networks show performance variations among firms? iii) To what extent did the state of Turkish industry rankings change under AKP rule?

The paper has three contributions. First, we show that the type of political connection matters in business performance through a historical analysis and their benefits tend to stem from either direct personal channels or institutional and network ties. Second, in most international business and economics literature on PCF, political party ideology is seen as dormant or insignificant. In contrast, we regard ideological motivations to be highly significant in mobilising, shaping and aligning firm behaviour. This allows us to see deepening linkages between business and politics in relation to the regime type and political institutions. Third, we provide an extensive treatment of connectedness with a robust sample of the top 1,000 firms rather than a small set of stock listed companies or global listings. Thus, our industry-level analysis demonstrates the extent to which business performance can be associated with connectedness through industry and firm level data. Overall, we aim to deepen academic debate on firm performance in relation to political ties in the business and politics literature. The article demonstrates why scholars, policy makers and the wider public should be interested in the scope of political associations as it raises questions on a number of important issues: i) long-term business efficiency under political constraints; ii) opportunity and welfare costs of business favouritism and clientelism; iii) influence of deepening ties on political institutions and freedoms.

Following a literature review on business-politics relations and connectedness, we develop a set of hypotheses. The methodology section explains how the data were utilised, connections were identified, and business rankings were calculated. The penultimate section provides a discussion of the key findings. The conclusion expands on the significance of the results, discusses the impact of deepening connectedness on political institutions along with limitations and future directions.

²¹ Kuban and Sozeri 2012.

2. Literature review: politically connected firms and business-politics relations

Firms get preferential access to a number of value enhancing resources and opportunities through political connections. Fisman's (2001) analysis of Indonesia showed that a considerable percentage of well-connected firms' value came from their high level political connections and favours they obtained through them. In her widely cited work, Faccio (2006) found corporate political connections to be relatively widespread: They exist in 35 of the 47 countries that she sampled. However, they appear to be less common in countries with more stringent regulation of political conflicts of interest and more widespread in countries that are perceived as being highly corrupt. Connections are also more widespread among larger firms. Faccio (2006) finds a significant increase in corporate value when those involved in business enter politics. The stock price impact of a new connection is larger whenever a businessperson is elected as prime minister, rather than as a member of parliament, and whenever a large shareholder, rather than an officer, enters politics. However, while these findings rest on a relatively large sample of PCF in the UK (154 firms), Japan (31 firms) and Thailand (23 firms), the study detected a rather small and sporadic number of PCF in several leading emerging economies where PCF are expected to be widespread. For example, there is only one company in her sample connected with a minister or MP in each of Turkey and the Philippines, and none in South Africa or Brazil. This shortcoming indicates broader problems of identifying PCF in cross-country analyses. Indeed, two other such studies, Boubakri et al. (2012) and Chen et al. (2010), formulate their initial sample of politically connected firms based on Faccio's (2006) original data.

Boubakri et al. (2012)²² update Faccio's (2006) data with another 61 PCF from 2002 and 2003 and investigate the impact of political connections on firm performance and risk-taking in publicly traded companies. Using a long-term event study covering a sample of 234 politically connected firms headquartered in 12 developed and 11 developing countries over the period of 1989-2003, they find that firms increase their risk-taking practices and performance after the establishment of a political connection. The authors also document an increase in PCF's financial leverage, their use of long-term debt, and their liquidity ratio

²² In the sample of Boubakri et al. (2012) there are 79 British companies (33.76% of their sample), followed by Japanese firms (27 firms, 11.54%), and Malaysian firms (22 firms, 9.40%). Out of the 541 politically connected firms in her study, Faccio (2006) finds 154 connections in the UK (28.47%): 32 in Japan (5.91%); and 88 in Malaysia (16.27%). Furthermore, 146 connections involve members of parliament whereas the others involve close ties with government officials or heads of state. Politically connected firms are spread across industries, with 19.66% in the financial sector, 15.38% in consumer durables, and 10.68% in services.

during the first three years of the political connection vis-à-vis the three years before the connection.

Through an analysis of stock price responses to the announcement of the board nomination of a politically connected director in S&P 500 companies between 1996 and 2000, Goldman et al. (2009) find that PCF show positive abnormal stock returns. This finding on the US is in line with other research such as Johnson and Mitton (2003) on Malaysia and Claessens et al. (2008) on Brazil. Johnson and Mitton's study shows that PCF benefited from the capital controls imposed in Malaysia during the Asian financial crisis in 1998 and PCF associated with PM Mahathir Mohamad had significantly higher stock returns. By using indicators of political connections constructed from political campaign contribution data, Claessens et al. (2008) similarly show that Brazilian firms that provided contributions to elected federal deputies experienced higher stock returns than firms that did not around the 1998 and 2002 elections. However, the prediction of this benefit in earnings and stock return are also subject to volatility and political uncertainties.²³ Boubakri et al. (2013) show PCF have more volatile earnings and show greater risk taking in countries where they are rescued in case of turbulence.

Benefits of political ties to the firm do not only appear in the form of increased business opportunities, predicted earnings, and rise in fixed and collateralisable assets, another critical factor can be in the form of improved access to finance. Using a loan-level data set of more than 90,000 firms in Pakistan between 1996 and 2002, Khwaja and Mian (2005) show that PCF borrow 45 per cent more and have 50 per cent higher default rates. They claim that such preferential treatment occurs exclusively in government banks and has an economic cost as it goes to often poorly performing firms.²⁴ Similarly, in her study on Italy, Sapienza (2004) shows that state-owned banks serve as a mechanism to supply political patronage. In a cross-country examination, Faccio et al. (2006) illustrate that PCFs are more likely to be bailed out than are their non-connected peers and they exhibit poorer operating performance than others at the time of the bailout and over the following two years.²⁵

However, there is some controversy over assessing the performance of PCF and the value of political connections. A close relationship between a country's political leadership and a segment of the business community can be an asset as it frequently provides privileged access to resources, finance and government

²³ see Chen et al. 2010.

²⁴ Khwaja and Mian 2005.

²⁵ The study identified only one firm in Turkey. The most common cases occur in Malaysia.

procurement, and regulatory policies. However, there are also inefficiencies and risks born out of this close association with political interference and nepotism that affects firm management, trade relations and employment choices. Thus, political ties bring about a long-term liability and market constraints. Numerous findings suggest that individual ties to key political figures and connections matter more and have greater influence on firm value when power is concentrated in the hands of a few people or a small number of business groups, but much less when it is dispersed through various democratic structures that contain checks and balances. These studies suggest that changing circumstances of the key political figures (illnesses, death or removal from power) have great effect on firm performance and economic growth in non-democracies, but much less or no effect in democracies. Jones and Olken's (2005) pioneering study shows how the random death of a leader has a significant effect on economic growth in autocracies.²⁶ In China, as in other emerging economies, political ties help firms to secure access to key resources more easily. Firms seek to appoint business executives with such ties to enhance business performance.²⁷

In mature democracies, political connections are structured differently and arguably institutionally more complex but perhaps not less influential.²⁸ In their study, Acemoglu et al. (2010) argue that the effects of political connections between mature markets and middle income emerging economies may not be as wide as is commonly assumed. Examining the appointment effect of US Treasury Secretary Timothy Geithner, they find a cumulative abnormal return to Geithner connected firms of around 15 per cent, from day 0 (when the announcement was first leaked) to day 10. Abnormal returns enjoyed by Geithner-connected firms following his nomination must reflect some reason for the markets to believe that having Geithner at the Treasury would benefit those firms. Their result is close to previous findings in emerging markets and much higher than other studies have found for the United States or other relatively rich democracies. However, the authors admit that they have no evidence that Geithner actually implemented the kind of favouritism implied by the initial stock market reaction. They suggest that the increase in the perceived value may lower the cost of capital and allow some firms to stay in business when others close.

²⁶ See also Fisman 2001 on Indonesia, Johnson and Mitton 2003 on Malaysia.

²⁷ Li and Tang 2013.

²⁸ For example, see Johnson and Kwak's (2010) arguments that "the Wall Street banks are the new American oligarchy," operating "by the soft power of access and ideology" rather than bribery or blackmail. Some argue about the global implications of this, such as Bhagwati (1998) who points out that Wall Street firms pushed Washington to lobby for capital market liberalisation around the world.

Only a small number of studies illuminate the economic costs of PCF. Boubakri et al. (2012) suggest that political interference in the management of the firms and the weak managerial skills of politicians could be harmful to the firm's performance. Bertrand et al. (2007) find that the profits of French firms managed by politically connected CEOs tend to decline as the fraction of their employment located in politically contested areas increases. Fan et al. (2007) on China and Boubakri et al. (2008) through an international sample find that newly privatised politically connected firms under-perform their non-connected counterparts. In an interesting study on Brazil, Claessens et al. (2008) show that PCF that make more campaign contributions have significantly lower returns on assets despite having higher investment rates.²⁹

Political economy approaches look at the problem through economic justice, regime type and allocative efficiency. Such studies tend to link political interference to business or businessmen's career in politics in relation to corruption and clientelist ties. They examine how relations between dominant business groups and the state shape the political regime type and institutional trajectories;³⁰ the way in which client business networks and lobby groups benefit from selective and pro-business agendas and in return shape the policy agenda;³¹ and how detrimental consequences of inefficient redistribution and clientelism lead to high inequality and low productivity.³²

Clientelist ties are the most noteworthy element of PCF and they include a broad range of relationships.³³ A narrow definition by Robinson and Verdier (2003) states that clientelism is a political exchange between a politician who gives patronage and a client who provides a vote or support. Clientelism is utilised as a tool to create a loyal network of supporters in democracies as well as non-democracies. Kettering (1988) defines political clientelism as a system constituted by patron-broker-client ties and networks. Robinson and Verdier (2003) argue that clientelism emerges in countries where productivity is low. However, it is prematurely assumed that modernisation and development eliminates clientelism.

²⁹ They estimate the economic costs of capital misallocation associated with PCF to be at least 0.2 per cent of GDP per annum. This is measured in relation to: a welfare loss, which would arise if the rate of return on investment financed by this credit is lower than that on resources invested elsewhere.

³⁰ Nam 1995; Guriev and Rachinsky 2005; Choi and Thum 2009.

³¹ Buğra 1995; Salas-Porras 2005; David et al. 2009.

³² Robinson and Verdier 2003; Adly 2009; Abdel-Baki 2012.

³³ There is an important difference between the concepts of clientelism and patronage. Patronage simply means the "exchange of public sector jobs for political support whereas clientelism includes not only jobs but also other state resources (goods, services, decisions, etc.)" (Hicken 2011: 295).

The first necessary condition is that the relation must be beneficial for both parties and there is a scale problem. A well-known example of clientelism is the relationship between large companies and the state in the era of General Park's military regime between 1963 and 1979 in South Korea. Nam (1995) shows how most of the financial incentives were given to the largest companies in return for financial support to the military regime. The government controlled the allocation of credit and foreign currency, and the *chaebol* enjoyed preferential access to these and other resources.

Thus, the nature of connectedness has important implications for political institutions. In many late industrialising economies governments historically developed clientelist ties with industrialists and supported the formation of business groups by protecting them through tariffs and trade restrictions.³⁴ They also granted discretionary concessions (for example, in media, mining, and other licenced and regulated sectors), direct and indirect subsidies to certain favoured industries. In return for their loyalty, these business groups benefitted from state-induced consolidation and foreign competition. There is some evidence to suggest that economic liberalisation benefitted old business groups while creating new ones through privatisation.³⁵ However, further cross-country analysis is needed to see how the shift from state-centred development to market liberalisation has altered business-politics relations and the nature of connectedness.

State insiders, as managers of economic units and civil servants, shaped ownership structures of key industries in most post-communist economies through de-regulation and privatisation. Inter-elite conflicts have led to opaque allocation mechanisms. Authoritarian political regimes are progressively entrenched wherein ruling elites increase their ownership and/or political control of strategic assets.³⁶ In an analytical paper on Russia's largest oligarchs, Guriev and Rachinsky (2005) illustrate how the concentration of ownership leads to a highly corrupt political regime in which neither oligarchs nor the bureaucracy are interested in implementing policies that will open the economy to broader participation. In China, Wank (2002) argues that clientelist networks evolved in line with market opening as the business fortunes of those connected to the Communist Party increased. Local officials implemented the economic reform policies first and foremost as a way to ensure their self-interests and provide further benefits to the political elite.³⁷

³⁴ Buğra 1995.

³⁵ Khanna and Palepu 1999; Khanna and Yafeh 2007.

³⁶ Author, Zhang and Liu, 2010, Junisbai 2012.

³⁷ Zhang and Liu, 2010.

Based on this discussion we identify three methodological and theoretical insights:

- i) *Institutional context:* While firm based studies show the advantages of the firm's connectedness to business fortunes, political economy analyses aggregate business-politics relations in broader frameworks of regime type and economic efficiency.³⁸ We believe a more nuanced approach that takes into account the institutional context of connections can enhance our understanding of business-politics relations and bridge the gap between these two bodies of literature. The channels of access and ties between firms and political parties deserve further articulation. Recognising the fact that relationships between business and politicians are non-homogenous across political parties and over time, we differentiate between direct personal ties and institutionally structured networks of business interests to the ruling party. While these two channels may frequently overlap, they have distinct scales and functions.
- ii) *Measurement issues:* The evidence suggests that political connections are more covert and deeply embedded in informal institutions and business networks in emerging markets, which also tend to have deep information asymmetries.³⁹ Studies mostly deal with large listed companies that are subject to corporate governance disclosures. For companies that are subject to lesser disclosure regulation the spread and depth of ties and influence in policy formulation remain under-researched in the business and economics literature. In addition to these methodological problems, existing international comparisons are flawed as they fail to apply their criteria of connectedness evenly across countries. Therefore, the studies of Faccio (2006), Boubakri et al. (2013) and others do not capture the depth and breadth of political connections, especially in emerging economies. We address this shortcoming through an industry and firm level analysis of the largest 1,000 establishments. Our analysis provides a replicable model for further studies. Our methodology extends the techniques used to refine the identification of connections and to overcome various measurement issues.
- iii) *Implications for political institutions:* How politics changes through deepening linkages between ruling parties and their business constituencies is another neglected area in business and management literature that deserves further investigation. Evidence from post-communist states show that deepening ties between businesses and politics has weakened democratic formations. There is a need to examine how

³⁸ Such as Faccio 2006; Hankla 2006; Choi and Thum 2009; Abdel-Baki 2012.

³⁹ Khwaja and Mian 2005; Chen et al. 2010.

political institutions have been shaped by the evolving character of political patronage over business under economic liberalisation in young democracies such as Turkey. This requires a bridge between PCF studies and political party lines: To what extent do connected firms remain loyal to their political party links? What determines this binding relationship in the long run? The character of the relationship carries important implications for political power, party trajectories and democratic institutions.

In the light of this discussion, we show our hypotheses and methodology below.

3. Hypothesis development and methodology

Numerous studies argue that capital formations and the identity of capitalists changed fundamentally as the intensity of Islamist political discourse grew since the 1990s.⁴⁰ Turkey's Islamist political movements have long been in ideological confrontation with modern secularism and westernisation that rested on a Eurocentric worldview.⁴¹ Recognising the economic backwardness as a major problem, political Islam promised a new economic rejuvenation and salvation against decadent capitalism and imperialism through a moral course of state-led developmentalism. Several Islamic parties before the Justice and Development Party (AKP) faced closures or judicial bans due to their anti-establishment religious bias by the secular state institutions, the military and the judiciary. Nevertheless, Turkish politics accommodated and frequently promoted Islam against the spread of communism during the cold war. The rise of political Islam to power, however, is closely linked to the recent history of market liberalisation, its debilitating effects on the traditional centre right politics, and a general societal discontent with development prospect offered by the main stream political parties.

The September 1980 military coup created initial conditions for market deregulation and subsequent suppression of opposition interests and left wing politics. A former World Bank employee and an ideologue of the New Right, Turgut Özal, played a crucial role in introducing the Washington Consensus principals, initially as an economic policy advisor to the post 1980 coup and later as Prime Minister and the leader of the Motherland Party (Turkish acronym ANAP). A member of the Nakshibendi order, one of the most influential Islamic brotherhoods, Özal was also a parliamentary candidate from the first Islamist party in 1970. When the generals banned former political leaders and closed down incumbent parties in 1980, Özal formed ANAP, which contained centre right, ultra-nationalists, Islamists and democrats at once. ANAP came to power in the

⁴⁰ Author; Atasoy 2009; Tuğal 2009; Gumuscu 2010.

⁴¹ Gülaip, 1999; Tuğal 2009.

1983 elections with a full-fledged programme of de-regulation and liberalisation of the economy backed by a military made authoritarian constitution. Having shaped a decade long switch to liberalisation and re-Islamisation, Özal died unexpectedly while serving as President in 1993.

The rise of Islamic politics to centre stage began when Erdoğan was elected as mayor of Istanbul in 1994 for a four-year term. Erdoğan, Abdullah Gül⁴², and others from the Refah Party formed the AKP in 2001 and came to power in 2002. The new party pledged to adhere to multi-party democracy and economic liberalisation. Its cadres, however, originated from earlier right-wing Islamic political movements, most notably Milli Görüş.⁴³ With a pro-business liberal outlook, the AKP challenged the status quo in domestic politics, gained international sympathy, and maintained the economic growth necessary to secure electoral support.

The AKP benefitted greatly from the growing number of Islamic charities and their affiliated business groups in its election campaigns. Yavuz (2004) argued that the spread of Islamic brotherhoods was associated with the rise of civil society against the authoritarian state and a new force for democratisation. Contrary to this claim, the most influential such groups were linked to official policies to promote Islam in the state and society, especially in the aftermath of the 1980 military coup.⁴⁴ Tuğal (2009) referred to this transformation as the de-radicalisation of the Islamist political movement and its embrace of neo-liberalism as a “passive revolution”.

Neo-liberalism and democratisation rhetoric offered two critical tools for the AKP in its aspiration towards hegemonic regime change.⁴⁵ This took place through the expansion of party control over the judiciary, the police force, the military and in education. It strengthened its control over privatisations, urban development projects and capital flows in local and regional markets. The AKP also weakened societal resistance and interest group pressures through social welfare reforms in public health, mass housing provisions and education policies. Subsequently, while the AKP grasped control of central institutions and monopolised state power, it developed a decentralised populist reach to the electorate through two channels: state and municipal provisions and Islamic charities and foundations.⁴⁶

⁴² Abdullah Gül became President in 2007.

⁴³ Atacan 2005.

⁴⁴ Tuğal 2012.

⁴⁵ Polat, 2012

⁴⁶ Bartu and Kolluoglu 2008; Karaman, 2013.

Islamic fraternity organisations and charities expanded their activities into business ventures taking advantage of liberalisation.⁴⁷ Alternative capital formations led to Islamic finance discourses in provincial economies⁴⁸ and religious fraternity groups promoted their own business ethics to counter-balance social inequalities.⁴⁹ This implies that during its rule the party and its strong leader developed their influence in businesses to build market power parallel to their political might. Thus, we study political connections to the ruling party and their performance effects through H1 and H2.

H1: Connected firms enjoyed abnormal growth rates compared to other listed firms.

H2: Connected firms are less likely to drop rank in the list.

The establishment of the Islamist business association, MÜSİAD,⁵⁰ in 1990 was the first step in the growth of pro-Islamic business solidarity groups that supported Islamist political parties. The antagonism between MÜSİAD and its rival, TÜSİAD⁵¹ (established in 1971), gave way to a growing political split in the form of old secular vs. new religious bourgeoisie.⁵² Intra-business struggles also took place among different factions of the local business groups, which led to organisational splits between pro-AKP associations and their rivals.⁵³ While MÜSİAD emerged as a powerful pro-AKP business group with representative offices in 48 countries, several business federations united to form TUSKON⁵⁴ in 2005. TUSKON's base is dispersed among SMEs and Anatolian cities with strong links to the Gülen Movement (commonly known as *Hizmet*, or “service”), an influential Islamic fraternity organisation.⁵⁵ Thus, the two new Islamic employers' organisations, MÜSİAD and TUSKON, enjoyed extensive political and business

⁴⁷ Hoşgör 2011; Öniş 1997.

⁴⁸ Author.

⁴⁹ Uygur 2009.

⁵⁰ MÜSİAD: Müstakil Sanayici ve İş Adamları Derneği (Independent Industrialists and Businessmen's Association).

⁵¹ TÜSİAD: Türkiye Sanayici ve İş Adamları Derneği (Turkish Industrialists' and Businessmen's Association).

⁵² Çokgezen 2000.

⁵³ Bayırbağ 2011.

⁵⁴ TUSKON: Türkiye İşadamları ve Sanayiciler Konfederasyonu (Turkish Confederation of Businessmen and Industrialists).

⁵⁵ Atasoy 2009; Hoşgör 2011. The movement operates schools in over one hundred countries and is associated with many businesses united under TUSKON, television channels and Zaman, one of Turkey's largest-circulation newspapers.

ties with the AKP government,⁵⁶ and the former is reportedly closer to Erdoğan and his circle. These two associations competed for influence from the mid 2000s. In December 2013, corruption allegations, involving leading cabinet ministers, Erdoğan and his family prompted the AKP to denounce the Gülen Movement as a parallel state and initiated a smear campaign against Gülen-affiliated schools and business activities.⁵⁷ Our analysis considers the period before the growing confrontation between these former allies.⁵⁸ We assess the performance variation according to their distinct political capital and access to AKP through H3. Furthermore, we investigate whether power building by the AKP affected the status of old business groups in Turkish industry. Karadağ (2010) pointed out that the AKP diminished or destroyed some of the older business holdings while protecting its affiliated firms. [The authors' paper] on energy utility privatisations between 2003 and 2013 showed that highly personalised and opaque allocation of assets increased the power of new business groups that enjoyed close ties with Erdoğan and key party officials. Thus, we test if the ranking of the business groups that originated from the early Republican Era were challenged by AKP linked firms through H4.

H3: Type of connection through either Islamic employer's organisation (MÜSİAD and TUSKON) is differentially effective on firm performance.

H4: Connected firms weakened the position of old business groups in the industry rankings.

3.1. Data

The Istanbul Chamber of Industry (ISO) data, collected annually since 1993, is the most comprehensive and reliable business record in the country. There are three other leading national lists, Forbes 500, Capital 500 and Fortune 500. However,

⁵⁶ An example: the former head of MÜSİAD, Mr. Ömer Bolat, later became a member of the governing board of the AKP.

⁵⁷ The Gülen Movement has long been in a partnership with Erdoğan's government in their power struggle against the military and secular establishment, in particular the judiciary. However, the Movement is accused of infiltrating into police, judiciary and other state organs and pursuing an agenda of their own under orders from their spiritual leader, Fetullah Gülen, who leads a reclusive life in Pennsylvania. A vicious power struggle has led to an open battle between Erdoğan and Gülen. A string of high level corruption allegations that have emerged against AKP's top officials and their relatives since 17 December 2013 is claimed to be orchestrated by the Movement's members (see reporting at Financial Times, by Daniel Dombey, March 18, 2014).

⁵⁸ See the insightful coverage at "Human Rights Practice in Turkey"
<http://humanrightspracticeinturkey.com/2014/02/13/23/>(accessed on 1 May 2014).

these have numerous methodological constraints and biases since their Turkish editions are compiled by magazines owned by leading business groups (Çalık Holding, Doğan Holding and the Mutlu Journal Group, respectively). In addition to its perceived neutrality, the chamber's annual business survey has a very high penetration across Turkish regions through its sister organisations. As the biggest and most developed organisation of its kind, it benefits from close links to chambers of industry in each town. This facilitates data collection through a nation-wide survey administered by local chambers.

New firms as well as old ones are surveyed annually. Although inclusion in the ISO database is voluntary, its survey has high participation due to its well-established professional credibility and national prominence. For featured firms it is highly prestigious to be included in the Istanbul Chamber of Industry business ranking. For local chambers it brings visibility and recognition to their towns and sends positive signals to potential investors and helps to build lobbying activities for local economic development. Every year the announcement of ISO's annual ranking creates excitement in business circles and the press nationwide. Towns far from Istanbul, such as Kahraman Maraş and Gaziantep, take pride in the number of firms they have in the ISO's top ranking. While it is expected that Turkey's largest business groups get top positions, the list frequently stimulates wider commentary on the ranked firms from less known towns. Thus, both local chambers and industrialists have incentives to get involved in the annual business surveys. The ISO data initially ranked the top 500 firms in the country but later expanded its coverage to include the top 1,000 in 1997.⁵⁹

There are a number of restrictions in identifying PCF in the Turkish context. Firstly, political ties in business are poorly recorded in the mainstream media.⁶⁰ Only major scandals get attention. Secondly, there is no reliable database of political campaign contributions, business stakes of politicians, or any disclosure

⁵⁹ The stock-market data, based on 370 listed firms (including foreign-owned ones), appear to be inferior to Istanbul Chamber of Industry's coverage.

⁶⁰ The AK Party in government has systematically purged the independent press and journalists who reported about poor management and corruption. See the EFJ website for the details: <http://europe.ifj.org/en/articles/turkish-authorities-attack-tgs-the-largest-ifj-and-efj-affiliate-in-the-country> (accessed on 14 June 2012). Journalists such as Nedim Şener, Ahmet Şık and Soner Yalçın, were arrested on conspiracy charges. Mr Şener wrote books to illustrate that the Gülen Movement has infiltrated the police force and the judiciary (*The Economist*, March 17th 2012). <http://www.economist.com/node/21550334>. (Accessed on 17 October 2012). Soner Yalçın supported this claim in his recent book written from his prison cell. See Soner Yalçın (2012) *Samizdat* (Doğan Yayıncılık, Istanbul). See also the influential "Human Rights Practice in Turkey" blog: <http://humanrightspacticeinturkey.wordpress.com/2013/11/08/how-moral-is-the-conservative-rule-in-turkey-media-assassinations/> (accessed on 15 November 2013).

requirements by firms that have politicians as shareholders or on their boards. As the majority of the ISO 1,000 are not traded on the stock-market, they are also not subject to disclosure rules. Thus, our identification of political connections rests on extensive media and secondary data analysis. While national media outlets have been restrained in reporting politically sensitive news, the local press continues to provide a broad range of information on business activities and political ties. This widespread and vibrant press, tied to dynamic local realities, is a good source for understanding political ties.

MÜSİAD and TUSKON have membership data bases but do not allow us to see the data about year of joining. However, there is a clear identification: both have been part of the Islamic political movement from their start and closely in tune with the AKP.⁶¹ Thus, our analysis regards both associations as part of politically connected networks. We tested our claim by examining if firms were switching from TÜSİAD to MÜSİAD, and this movement has been found to be insignificant. Double memberships also appear to be insignificant. Moreover, TÜSİAD has not been losing membership.⁶²

3.2 Definitions, identification of connections and analysis

We group politically connected firms in two categories, separating those with direct personal connections (PCF-1) from those connected through networks (PCF-2).

1) Firms with direct personal connections (PCF-1): By using Faccio's (2006, p. 370) definition of "politically connected firm" we classified PCF-1 if one of the company's shareholders or top managers is: i) a member of parliament from the ruling AKP; ii) a minister or the head of state; iii) closely related to the top AKP officials. We first identified the firm's key owners, shareholders and board members. Then, we investigated their associations in the Turkey search engine of

⁶¹ PM Erdoğan and AKP ministers have long established political and personal ties with MÜSİAD and TUSKON.

<http://www.dunya.com/28-subatin-en-onemli-izi-ortadan-kalkti-150037h.htm>;

<http://www.dunya.com/tuskon,-hukumetin-yaninda-82273h.htm>

<http://www.dunya.com/tuskon,-afrikali-isadamlariyla-bulustu-104711h.htm>

<http://www.dunya.com/son-10-yildir-dindarlar-degil,-devler-buyudu-151791h.htm>

Both organisations have considerable influence on policy formation: <http://www.dunya.com/musiad-ve-kosgeb-girisimci-yetistirecek-106936h.htm> (all accessed on 2 October 2012).

⁶² TÜSİAD gained 79 new members in 2012, one of the highest annual increases in new memberships. <http://gundem.bugun.com.tr/tusiad-da-yeniden-boynere-donemi-181843-haberi.aspx>
The tension between MÜSİAD and TÜSİAD continues. <http://www.dunya.com/musiad-alatona-kapimiz-acik-121921h.htm> (all accessed on 1 October 2012).

“Google” and the USA site of “Yahoo” (in the absence of a Turkish equivalent site). However, all investigations were carried out using Turkish key words. Our examinations took place before the AKP government first shut down Twitter and YouTube and later introduced draconian rules to monitor social media and internet to block the spread of protests and corruption allegations. After identifying the key individuals (usually 2 or 3 people), their names were searched along with the Prime Minister, cabinet ministers, MPs and the mayor of the town where the firm is located or originates from. Since it would have been laborious to use the names of all MPs and cabinet ministers we instead inserted the title used before the name, “Bakan” (the Turkish term used for a cabinet minister) and “Milletvekili” (the term for a member of parliament). For example, for a firm with two leading owners the investigation proceeds typically like this: firm’s name, the name of owner 1, and the name of owner 2 are matched with the words of “Prime Minister Erdoğan”, “Cabinet Minister”, “Member of Parliament”, and “the name of the local mayor”. Thus, the first three names are investigated one by one with the four possible political connections in 12 combinations. For example: “Firm’s name” + “Prime Minister Erdoğan”; “Name of Owner1” + “Prime Minister Erdoğan”; “Name of Owner2” + “Prime Minister Erdoğan”.

We provide three illustrative cases: i) Kiler Holding is linked to Vahit Kiler, a member of parliament from the ruling AKP⁶³; ii) AB Food is linked to Kemal Unakıtan, the former Finance Minister and leading AKP politician⁶⁴; iii) Çalık Holding is closely related to Erdoğan as the CEO of the company is his son-in-law.⁶⁵ Other examples illustrate less known cases. One diary products company in a large southern town of Turkey is linked to several AKP members of parliament. One of the major owners is the former chairman of the town’s football association, a member of the municipal council from AKP, and an AKP mayoral candidate. A hazelnut production and trade firm in a town on the Black Sea coast is linked to several members of parliament from the AKP. They and the town’s

⁶³ Sources: http://tr.wikipedia.org/wiki/Vahit_Kiler;
http://www.tbmm.gov.tr/develop/owa/milletvekillerimiz_sd.bilgi?p_donem=24&p_sicil=6266;
http://www.kiler.com.tr/files/kiler_a.%C5%9F_faaliyet_%20raporu_2011_3.%C3%87eyrek.pdf
(accessed on 1 May 2014)

⁶⁴ Sources:
http://www.cumhuriyet.com.tr/haber/diger/112332/Unakitanklar_tesvik_sistemini_sevdi.html;
<http://haber.gazetevatan.com/rabbim-sat-dedi/557485/2/ekonomi>;
http://www.radikal.com.tr/yazarlar/sefer_levent/ogul_unakitana_nazar_mi_degdi-1069417
(accessed on 1 May 2014)

⁶⁵ Sources: <http://www.reuters.com/article/2012/02/21/calikholding-sale-idUSL5E8DH3KG20120221>; <http://www.bloomberg.com/news/2010-09-13/erdogan-s-new-elite.html>; <http://www.hurriyet.com.tr/english/turkey/8939732.asp?gid=231&sz=88743>
(accessed on 1 May 2014)

AKP mayor attended the owner's daughter's wedding. He is a member of TUSKON, active in its trade activities and gave a speech at the European Summit of TUSKON. The latter indicates the overlap of two channels of access.

Identifying the first two types of links with a member of parliament from the ruling AKP, a minister or Prime Minister Erdoğan has been possible through our search methods and additional sieving through media sources. In the third category, identifying firms closely related to top AKP officials has been relatively easy for well-known firms through extensive internet and media analysis. However, the above two anonymised cases show intricacies of relations. For less known firms we studied a range of connection indicators to see if these were strong enough to secure political favouritism beyond casual ties. For example, we investigated if this connection leads to being a witness “şahit” at a family event of owners and/or their children, such as weddings and circumcision ceremonies. These roles signify non-casual friendship ties in the Turkish social context, especially because they emerge out of and bring further social obligations and reciprocity. We recognise that these are culture specific signifiers and may vary from one country to another. Nevertheless, they can be good indicators when for example club memberships are not significant and many relations are not reported or disclosed⁶⁶.

2) Firms connected through networks (PCF-2): Faccio et al. (2006) provide useful insights to identify indirect connections. High-level political experience in domestic and international operations requires sophistication and access. This is costly to achieve for firms with limited resources as shown by Keillor and Hunt (2004). Since they have developed considerable political acumen and links to the ruling party, MÜSİAD and TUSKON offer scale advantages and cost effective strategies. We examine if the connectedness served by the two pro-AKP business groups facilitate performance.⁶⁷ Thus, we use membership of these organisations as a proxy for PCF-2. This measure helps us to assess the effect of Islamic employers' lobby power and access to political capital.

To identify MÜSİAD and TUSKON links we searched through the commercial portals of “TUSKONtrade” and “e-MÜSİAD”. These web engines helped to verify membership of the identified firms. For firms that did not appear on these sites we carried out additional search through “Google” and “Yahoo” by entering the key owner's name plus MÜSİAD and TUSKON. For example, for a firm with

⁶⁶ For example, Acemoglu et al. (2010) used personal diaries for office meetings to identify relations. It is impossible to secure access to the diaries of Prime Minister Erdoğan, cabinet ministers and AKP members of parliament.

⁶⁷ See, <http://www.musiad.org.tr/> and <http://www.tuskon.org/>.

two leading owners we investigated: “firm name” + “owner1” + “owner 2” + “MÜSIAD” + “TUSKON”. We checked their accuracy through other internet sources such as websites of associations’ local offices and the company sites, as well as national and local newspapers. For firms that did not appear in these web engines, we carried out additional investigations. We searched the links between “the name of the firm”, “owner1” and “owner 2” and “ the name of local director” and “the name of national representative” of MÜSIAD and TUSKON in 18 combinations to test if there is any credible relationship such as benefitting from commercial networks, trade fairs, incentive schemes and export promotion organisations. For example, a typical search was: “firm’s name” + “MÜSIAD”; “firm’s name” + “TUSKON”; “firm’s name” + “the name of MÜSIAD local director”; “firm’s name” + “MÜSIAD national representative”; “firm’s name” + “TUSKON local director”; “firm’s name” + “TUSKON national representative”.

We systematically reviewed a range of news sources to identify connections. As many connected firms and AKP’s business relations spread to various Anatolian towns, these localities have access to business news through usually detailed but straightforward event reporting.⁶⁸

The ISO data set provides information on: net sales on production, total sales, gross value added, owner’s equity, assets, profit/loss, export, number of employees, and the sector. However, the two series are not fully compatible because they are reported separately and transitions between them are not recorded. We created a code for each firm to follow transitions among the lists. The codes given are unique and consist of the characteristic letters of the firm names. We then constituted a top 1,000 industrial enterprise list with an annual time series and rank changes of the fastest growing firms between 2003 and 2011. A ranking based analysis explains better the overall performance of politically connected firms and the change they bring to the industrial structure. For example, a percentage gain or loss in assets, with the firm’s 2003 assets as the

⁶⁸ Scholars have used unconventional methods in identifying political connections. For example, Faccio et al. (2006) identified indirect connections of “friendship” through an analysis of reporting in *The Economist*, *Forbes* and *Fortune* magazines. Acemoglu et al. (2010) identified network relations through personal diaries, club memberships and news reporting among others.

We reviewed and double checked a broad range of national and local media as well as specialist publications. The national newspapers such as *Milliyet*, *Hürriyet* and *Radikal* provide some relevant background. The financial newspaper *Dünya* has also been useful. The list below include the local newspaper publications we most frequently visited: <http://www.konyahaber.com.tr>, <http://www.kayserigundem.com/>, <http://www.duzcepostasi.com>, <http://www.gaziantep27.net>, <http://www.haberantalya.com>, <http://www.antakyagazetesi.com/>, <http://www.denizlihaber.com/>, <http://www.orduolay.com/>, <http://www.gazete55.net/>, <http://www.yeniadana.net>.

baseline, would have been useful to show the trajectory of a particular firm but we are primarily investigating PCF as a pack rather than the efficiency of a single firm. However, in order to check the robustness of our method we also carried out analyses based on the performance of firms (with absolute values of assets) and found considerable overlap with our list of PCF (almost 50 per cent). Absolute values have shown a pattern of steady increase during the 2003 to 2011 period for the majority of firms and this also makes relative performance indicators less suitable.

In ranking the fastest growing firms the study used “net sales on production” and “assets” as performance measures. Utilising net sales on production is a difficult measure to use because of its sensitivity to changes in the market and inadequacy in reflecting scale effects of the firms. However, when combined with a measure of assets, they help to minimise sectoral differences, annual fluctuations and exogenous shocks. Moreover, profit rate or exports do not necessarily reflect the economic performance of firms in a comparative manner. In relation to the key arguments of our study, a proxy of economic performance had primarily to be convenient to analyse the effects of business networks. Thus, the net sales on production and assets are two best fitted proxies for the purpose of the study.

Utilising firm rank allowed us to measure the relative performance of the firms. About half of the firms in the latest top 1,000 have been in the list since 2003. Therefore, new entrants and others were analysed separately. The analysis identified the top 50 fastest growing (all years between 2003 and 2011), 50 fastest descending and 25 fastest growing new entrants (since 2003) to provide a sound analysis of the dynamic structure of the business rankings. Each set was examined in terms of the firms’ net sales on production and assets for 125 firms yielding 250 observations.

4. Findings on political connections and firm performance

The Istanbul Chamber of Industry’s top 1,000 firms constitute 4 per cent of total employment, 11 per cent of GDP and 40 per cent of exports in the Turkish economy⁶⁹. Our analysis shows that these ratios did not change significantly since 2003, aside from an observed dip in 2009 due to the global financial crisis (see

⁶⁹ The ISIC Rev. 2 classification of firms are in the following categories: 210-311-312-313-314-321-322-323-324-331-332-341-342-351-352-353-354-355-356-361-362-369-371-372-381-382-383-384-385-390-400

Table 1). The overall analysis of 2011 data provides the following averages per firm: net sales on production (\$232 million); value added (\$90 million); export earnings (\$88 thousand); employees (834 persons). Seventy two per cent of the firms employed more than 250 persons (92% more than 100). This indicates that 28 per cent of ISO firms are SMEs. In the ranking, there are 18 state-owned companies (with the median ranking of 212; 8 of them in the top 100) and 144 firms with more than 50 per cent foreign ownership (with a ranking median of 349; 18 of these are in the top 100). About one third of the firms are located in Istanbul. Five out of the top 10 companies in this ranking are part of the Koç Holding, one of Turkey's oldest business groups. The other high ranked firms also belong to old business groups, each over 50 years old, thus already well-established when the AKP came to power. These include Sabancı, Eczacıbaşı, Akkök, OYAK and Yaşar Holding groups. However, 408 new industrial enterprises entered and stayed in the ISO top company ranking since 2003. This shows significant upward mobility in Turkish industry during the past decade.

Table 1

According to the measure of net sales on production, 26 of the 50 fastest growing firms are politically connected either through direct links or institutional networks (PCF-1 and PCF-2). When measured according to assets, the number of connected firms increases to 28 firms. These connected firms demonstrate that they achieve higher operating profit despite having larger employment and lower asset turnover. The overlap between the two measures is 33 firms; 21 of them are PCF. These findings support our first hypothesis: *Connected firms enjoyed abnormal growth rates compared to other listed firms*. The opposite pattern is observed in the analysis of the fastest dropping 50 firms in the ranking: there are only 7 politically connected firms according to net sales on production and 12 according to assets. The overlap between the two measures is 31 firms and only 4 of them are PCF. This evidence supports our second hypothesis: *Connected firms are less likely to drop rank in the list* (see Table 2).

The composition of the fastest growing PCF-1 and PCF-2 are shown in Figures 1 and 2. This distribution of connected firms shows the predominance of personal ties (15 firms) according to measures of both sales and assets. There is some overlap between PCF-1 and PCF-2: 4 firms (according to sales) and 5 firms (according to assets). Institutional network channels show differentiation as TUSKON emerges as more effective in retaining and cultivating business performance. We observed 10 (in sales) and 13 (in assets) connected firms with it.

TUSKON has also the lowest number of rank drops. These results show that channels of access have varied consequences in business performance. TUSKON has been a more effective business lobby group. Thus, findings support our third hypothesis: *Type of connection through either Islamic employer's organisations (MÜSİAD and TUSKON) is differentially effective on firm performance.* This finding has important ramifications since Erdoğan initiated an extensive purge of all Gülen linked groups since 17 December 2013. Reports suggest that TUSKON affiliated firms increasingly face tax evasion investigations and are de-listed from government procurement schemes.⁷⁰ For example, the majority state owned company, Turkish Airlines, removed Zaman, a Gülen affiliated newspaper, from its in-flight service. This previously favoured daily was also dropped from government linked advertisements and promotions. Bank Asya faced liquidity problems when several large companies, among them Turkish Airlines, withdrew their deposits (Bilgic, 2014). In response to growing purges, TUSKON shut down its business web portal (tuskontrade.com.tr), presumably to block information on its members and to remove sensitive data.

Table 2

Figure 1

Figure 2

Firms with political connections have shown abnormal performance on average over non-connected firms in increase in sales, value added and profit rate. Despite having lower labour production rates, both PCF-1 and PCF-2 operate with higher profit rates on average. According to net sales, the fastest 50 firms' place vary between the 97th and 652nd positions while the fastest 50 according to assets have a spread between the 114th and 882nd positions. Almost half of these observed cases are in a higher ranking position than their non-connected peers on average.

In order to test the robustness of the evidence that supports H1 and H3, we also examined the firms that joined the list and stayed after the AKP came into power. Another striking feature to emerge from the analysis is the rapid rise of AKP-

⁷⁰ See further reporting on business purges:
http://www.cumhuriyet.com.tr/haber/turkiye/14637/Cemaat_sirketlerine_inceleme.html
<http://www.internethaber.com/cemaatin-sirketlerine-sok-baskin-653802h.htm>

linked firms that entered the list since 2003. We studied 25 firms in this category and they moved at least 414 ranks in net sales and 319 in assets since their entry. We identified 16 such firms as politically connected according to net sales and 14 according to assets (see Figure 3). The dominance of politically supported firms among the fastest new entrants is a significant indicator of the increasing influence of AKP in business. Most of the fastest new entrants are members of TUSKON. This distribution might also be another signifier of an intra-factional differentiation among AKP's client business groups (see Figure 3).

Figure 3

Despite the rapid rise of AKP linked business groups and favouritism in the market, only one of these fastest growing 50 firms managed to get in the top 100. Thus, our findings do not fully support the fourth hypothesis: *Connected firms did not weaken the position of old business groups in the industry rankings*. With further aspirations, MÜSİAD argued that all businesses “made gains” under the liberal economic order but it benefitted old business groups much more than “pious ones”.⁷¹ Turkey's first generation family holdings grew under import substitution policies until the 1980s and used their home advantages skilfully to benefit from the Customs Union with the EU that was agreed in 1995. They pursued diverse export markets and internationalisation strategies. Their domination of the top ISO ranking rests on a process of industrial capacity building and capital accumulation over more than half a century. A closer examination of the fastest growing three firms according to net sales on production shows that they all have personal connections (PCF-1) and had a phenomenal rise: climbing 707, 683 and 647 ranks respectively in the list. The top two of them made major gains through privatisations. According to assets, the first and third fastest growing firms again have direct connections (PCF-1) and are in the metal industry where asset size is important. These firms rose 599, 573 and 566 ranks respectively. This growth of AKP connected firms and affiliated business networks suggests a possible break up in old business holdings in coming years, if the party maintains its majority rule. Moreover, state-owned firms in the list are subject to government intervention in favour of AKP linked firms or against their opponents, as seen in the cases of withdrawn favours for Zaman newspaper and Bank Asya.

5. Discussion and conclusion

⁷¹Outgoing chairman Mr Vardan emphasised that MÜSİAD's 3,500 members account for 15 per cent of Turkey's exports, 105 billion USD gross domestic product and that they account for 10 per cent of the top 1,000 firms, half of them are in the first 500. <http://www.dunya.com/son-10-yildir-dindarlar-degil,-devler-buyudu-151791h.htm> (accessed on 2 October 2012).

We have shown that cross-country studies on PCFs are unable to demonstrate the extent to which political ties take shape in emerging economies as they fail to apply their definitions consistently across countries. Understanding the direction of change in business-politics relations requires historical studies. Industry level analyses are also better placed to provide the spread and effects of connections. Our findings show that firms with political connections have had abnormal performance on average over non-connected firms in increase in sales, value added and profit rate under AKP rule. Despite having lower labour production rates, both PCF-1 and PCF-2 operate with higher profit rates on average (this evidence supports H1). They are also less likely to drop in the ranking (this evidence supports H2). The dominance of politically connected firms among the fastest new entrants (since 2003) is another significant indicator of the increasing influence of AKP in business. The type of connectedness through personal ties and institutional networks shows performance variations among firms. The core group of firms (PCF-1) are connected to the Prime Minister and his close allies in the party. The second group (PCF-2) are linked to institutions of pro-government business support networks. The former appears to be the dominant case for the fastest growing large firms. Its influence over the economy has also been increasing, especially through new public contracts and privatisations.⁷² The latter allows small and medium-sized businesses to have access to resources. TUSKON emerges as more effective than MÜSIAD in retaining and cultivating business performance (this evidence supports H3).

The phenomenal performance of politically connected firms did not lead to a substantial weakening of old business groups. This finding does not fully support H4. Nevertheless, the overall composition of the largest industrial firms, the narrowing gap between the old generation capitalists and the AKP linked firms and the dynamic entry structure to the top 1,000 company ranking show that Turkey has more room for business growth opportunities than is seen in other countries. This contrasts with Russia where market concentration is extremely high and business-politics relations are much more tightly structured.⁷³ In emerging markets, a similar but less dramatic outcome implies that old business groups maintain their domination without much challenge from the rank and file of growing SMEs.⁷⁴ This point needs further empirical research as industry structures and scales vary greatly. Turkish business groups are also smaller than their emerging market counterparts, indicating relatively slow capital accumulation, poor energy resources and late internationalisation. Only the Koç

⁷² See Authors' research on energy privatisations. Öniş, 2011.

⁷³ Guriev and Rachinsky 2005.

⁷⁴ Khanna and Palepu 1999; Ramamurti 2000; Salas-Porras 2005; Khanna and Yafeh 2007.

Group was listed in the 2011 *Fortune 500*, as opposed to 7 firms from Brazil, 14 from South Korea, 8 from India, and 3 from Mexico.⁷⁵

The continuing domination of older generation family holdings along with multinational and state-owned firms in key industries is an outcome of a half a century of uninterrupted industrial growth. The largest firms, which once enjoyed government support, are now not in need of close political connections to maintain their business prowess. They have more resources to manage different political stakeholders at home and abroad.⁷⁶ However, following the popular Gezi protests against the AKP government, Turkey's largest family holding, Koç, came under fire because of the refuge given to wounded demonstrators by its hotel in Istanbul. In the following weeks, tax auditors raided several Koç companies and rumours about Erdoğan's intent to demolish the economic power of the group emerged in the media.⁷⁷ Similarly, Erdoğan's former ally, the Gülen Movement, and its affiliated businesses are threatened by AKP's recent judicial and bureaucratic "cleansing" measures to cover up corruption allegations against leading members of the party, including Erdoğan and his family. In the coming years AKP connections may significantly alter the ranking if the party maintains its majority control in parliament and fends off growing societal discontent and polarisation.

Choi and Thum (2009: 608) suggested that, "a regime may face a critical-mass problem in setting up a system of politically-connected firms." The Islamic political movement reached this critical mass since it first expanded its business base at the local government level throughout the 1990s. As the governing party, AKP has dominated the process of economic liberalisation with increasing FDI, privatisation and major infrastructure projects for more than a decade. This resulted in the growth of a parallel and antagonistic capitalist power vis-a-vis the old business groups and the political establishment through the ideological mobilisation of political Islam.

Our findings have significant implications for studying the long-term economic and political effects of business ties under deepening single party control. As Bucheli and Kim (2012) show, being closely associated with one political ideology, leader or an authoritarian regime brings legitimacy problems for foreign

⁷⁵ http://money.cnn.com/magazines/fortune/global500/2012/full_list/ (accessed on 17 October 2012)

⁷⁶ Keillor and Hult 2004.

⁷⁷ See, Semih Idiz, "The AKP shoots its goose", *Hurriyet Daily* 30/July/ 2013. <http://www.hurriyetdailynews.com/the-akp-shoots-its-geese-.aspx?pageID=238&nID=51639&NewsCatID=416> (accessed on 5 August 2013)

firms when such systems go through major changes. The same argument applies to politically connected domestic firms. Businesses that do not comply with demands of political actors get reprisals. Those closely linked to the political class face threats of losing their benefits when key agents leave their positions.⁷⁸ Worse, under major political changes, formerly favoured firms can fall from grace and lose their fortune entirely. Thus, although they may compensate for institutional uncertainties, political connections are a liability for firms in the long run. Under attack from its former ally, TUSKON affiliated firms' uncertain future is the case in point. Even if these firms manage to shift their political alliances periodically, allocating resources through political favouritism limits management choices, distorts firm performance and brings long-term economic and societal costs.

If organised around capable technocratic cadres and industrial policies, as seen in post-war South Korea and Japan, close ties between businesses and the state can nurture successful innovations and stable political regimes.⁷⁹ However, there is also a clear danger of political entrenchment through excessive business control and government intervention. Many studies have shown how politically connected firms are not more efficient or competitive than their non-connected counterparts.⁸⁰ In our analysis, connected firms demonstrate that they achieve higher operating profits despite having larger employment and lower asset turnover. None of these fastest growing firms are in high technology areas. This evidence points out the issues of misallocation of resources through political clientelism and corruption.⁸¹

Deepening business-politics ties bring hazardous effects on political institutions and economic freedoms.⁸² We showed here that party ideologies and leadership styles are important as they determine institutional workings.⁸³ A close association between authoritarian leadership and business diverts resources to an uneven distribution of property rights in favour of a few private actors as seen in Mubarek's Egypt.⁸⁴ Hankla's (2006) observation on India's Congress Party is a telling example of the danger of political deepening in multi-party parliamentary regimes. Although it appeared as if it was part of socialist ideology, Indra

⁷⁸ Johnson and Mitton 2003.

⁷⁹ As Hankla 2006 observed in the case of Gandhi in India.

⁸⁰ See for example Khwaja and Mian 2005; Claessens et al. 2008.

⁸¹ This point has become more pertinent since the 17 December 2013 corruption scandals. See also Adly, 2009; Abdel-Baki, 2012; Li and Tang 2012.

⁸² Acemoglu and Robinson 2006.

⁸³ See for example Fisman 2001 on Indonesia and Adly 2009 on Egypt.

⁸⁴ Adly, 2009.

Gandhi's economic policy decisions essentially aimed to develop new sources of patronage to stabilise her electorate linkages. "Having centralized the Congress Party under her personal leadership, Gandhi and her associates managed India's patronage networks personally, targeting largess for the maximum political benefit. This system, with a few changes, remained largely in place through the 1970s and 1980s, and, according to many observers, significantly slowed India's potential economic growth".⁸⁵ Similarly, Erdoğan's AKP follows an ideologically motivated strategy to nurture a patronage regime in order to secure long-lasting electoral success. A concern is also growing about its true intentions of replacing Turkey's multi-party democracy with a majoritarian single party rule.

Further studies might benefit from detailed firm level analyses as well as large samples. They might also illuminate new dimensions of performance and political connectedness by examining government privatisation schemes, large construction and infrastructure investments and economic rejuvenation projects. Current studies mostly deal with large stock listed companies that are subject to a degree of corporate governance and these should be expanded further. The spread and depth of business-politics ties, their economic value to the firm, impact on political institutions and the welfare costs of such ties to society remain under-researched in business literature. The lack of transparency in government and businesses continues to be the biggest methodological hindrance for national and international studies, particularly in emerging markets. Researchers need to rely on more grounded data sources. Our contribution to this debate demonstrates the benefits of further analysis.

Acknowledgements to follow

References

- Abdel-Baki, Monal A. 2012. "Coalitions within the Egyptian Banking Sector: Catalysts of the Popular Revolution". *Business and Politics* Vol 14(1): 1-26.
- Acemoglu, Daron and James A. Robinson. 2006. *Economic origins of dictatorship and democracy*. Cambridge: Cambridge University Press.
- Acemoglu, Daron, Simon Johnson, Amir Kermani, James Kwak and Todd Mitton. 2010. "The Value of Political Connections in the United States." Cambridge, Mass.: National Bureau of Economic Research.

⁸⁵ Hankla, 2006: 22.

- Adly, Amr Ismail. 2009. "Politically-Embedded Cronyism: The Case of Post-Liberalization Egypt." *Business and Politics* Vol. 11(4): 1-28.
- Atacan, Fulya. 2005. Explaining Religious Politics at the Crossroad: AKP-SP *Turkish Studies* Vol. 6(2): 187-199
- Atasoy, Yıldız. 2009. *Islam's Marriage with Neoliberalism: State Transformation in Turkey*. New York: Palgrave – Macmillan.
- Bayırbağ, Mustafa K. 2011. "Pro-Business Local Governance and (Local) Business Associations: The Case of Gaziantep." *Business and Politics*, 13(4), 1-37.
- Bertrand, Marianne, Francis Kramarz, Antoniette Schoar and David Thesmar. 2007. "Politicians, Firms and the Political Business Cycle: Evidence from France." Unpublished working paper, University of Chicago.
- Bhagwati, Jagdish, N. 1998. "The Capital Myth: The Difference between Trade in Widgets and Dollars." *Foreign Affairs*, 77(3): 7-12.
- Bilgic, Taylan. 5 Feb. 2014. "Bank Asia Penalised in Erdogan-Gulen Brawl Over Graft Probe." Bloomberg.com
- Boubakri, Narjess, Jean-Claude Cosset and Walid Saffar. 2012. "The Impact of Political Connections on Firms' Operating Performance and Financing Decisions." *Journal of Financial Research*, 35(3): 397-423.
- Boubakri, Narjess, Jean-Claude Cosset and Walid Saffar. 2008. "Politically Connected Newly Privatized Firms." *Journal of Corporate Finance*, 14: 654-673
- Boubakri, Narjess, Sattar A. Mansi and Walid Saffar. 2013. "Political Institutions, Connectedness, and Corporate Risk-Taking." *Journal of International Business Studies*, 44: 195-215.
- Bucheli, Marcelo, and Min Young Kim. 2012. "Political Institutional Change, Obsolescing Legitimacy, and Multinational Corporations: The Case of the Central American Banana Industry." *Management International Review* 52(6): 847-877.
- Buğra, Ayşe. 1995. *State and business in modern Turkey: A comparative study*. Albany: State University of New York Press.
- Chen, Charles J. P., Yuan Ding, and Chansog Kim. 2010. "High-Level Politically Connected Firms, Corruption, and Analyst Forecast Accuracy around the World." *Journal of International Business Studies*, 41; 1505-1524.
- Choi, Jay Pil, and Marcel Thum. 2009. "The Economics of Politically Connected Firms." *International Journal of Tax and Public Finance*, 16: 605-620.
- Claessens, Stijn, Erik Feijen, and Luc Laeven. 2008. "Political Connections and

- Preferential Access to Finance: The Role of Campaign Contributions.” *Journal of Financial Economics*, 88: 554–580.
- Çokgezen, Murat. 2000. “New Fragmentations and New Cooperations in the Turkish Bourgeoisie.” *Environment and Planning C: Government and Policy*, 8: 525-544.
- David, Thomas, Stephanie Ginalski, Andre Mach, and Frederic Rebmann. 2009. “Networks of Coordination: Swiss Business Associations as an Intermediary between Business, Politics and Administration during the 20th Century.” *Business and Politics* 11(4).
- Dinç, I. Serdar. 2005.” Politicians and Banks: Political Influences on Government-Owned Banks in Emerging Countries.” *Journal of Financial Economics* 77: 453-479.
- Dombey. D. (18 March 2014) “Turkey: The Erdogan-Gulen showdown” *Financial Times*.
- Faccio, Mara. 2006. “Politically Connected Firms.” *American Economic Review*, 96(1): 369-386.
- Faccio, Mara, Ronald W. Masulis, and John J. McConnell. 2006. “Political Connections and Government Bailouts.” *Journal of Finance* 61: 2597-2635.
- Fan, Joseph P. H., T. J. Wong, and Tianyu Zhang. 2007. “Politically Connected Ceos, Corporate Governance and Post-Ipo Performance of China’s Newly Partially Privatized Firms.” *Journal of Financial Economics* 84: 330-357.
- Fisman, Raymond. 2001. “Estimating the Value of Political Connections.” *American Economic Review* 91: 1095-1102.
- Goldman, Eitan, Jörg Rocholl, and Jongil So. 2009. “Do Politically Connected Boards Affect Firm Value?” *Review of Financial Studies* 22(6): 2331–2360.
- Guriev, Sergei and Andrei Rachinsky. 2005. “The Role of Oligarchs in Russian Capitalism.” *Journal of Economic Perspectives* 19(1): 131-150.
- Gülalp, Haldun. 1999. “Political Islam in Turkey: The Rise and Fall of the Refah Party.” *The Muslim World* 89(1): 22-41.
- Hankla, Charles Robert. 2006. “Party Linkages and Economic Policy: An Examination of Indira Gandhi’s India.” *Business and Politics* Vol. 8(3).
- Harvey, Benjamin and Bentley, Mark 2010. “Erdogan Like Ataturk Roils Elite as Kiler Rises With AK’s Power.” *Bloomberg Report*, 13 September 2010.
- Hicken, Allen. 2011. Clientelism. *Annual Review of Political Science* 14, 289-310

Hoşgör, Evren. 2011. "Islamic Capital / Anatolian Tigers: Past and Present." *Middle Eastern Studies* 47(2), 343-360.

Johnson, Simon and Todd Mitton. 2003. "Cronyism and Capital Controls: Evidence from Malaysia." *Journal of Financial Economics* 67: 351-382.

Johnson, Simon and James Kwak. 2010. *13 Bankers: The Wall Street takeover and the next financial meltdown*. New York: Pantheon Books.

Jones, Benjamin F., and Benjamin A. Olken. 2005. "Do Leaders Matter? National Leadership and Growth Since World War II." *Quarterly Journal of Economics* 120: 835-864.

Junisbai, Barbara. 2012. "Improbable but Potentially Pivotal Oppositions: Privatization, Capitalists, And Political Contestation in the Post-Soviet Autocracies." *Perspectives on Politics* 10: 891-916.

Karadağ, Roy. 2010. "Neoliberal Restructuring in Turkey from State to Oligarchic Capitalism." Max Planck Institute for the Study of Societies, Discussion Paper 10/7.

Keillor, Bruce D., and G. Tomas M. Hult. 2004. "Predictors of Firm-Level Political Behavior in the Global Business Environment: An Investigation of Specific Activities Employed by US Firms." *International Business Review* 13: 309-329.

Kettering, Sharon. 1988. The Historical Development of Political Clientelism. *The Journal of Interdisciplinary History*, 18:(3), 419-447.

Khanna, Tarun and Krishna Palepu. 1999. "Policy Shocks, Market Intermediaries, And Corporate Strategy: The Evolution of Business Groups in Chile and India." *Journal of Economics and Management Strategy* 8(2): 271-310.

Khanna, Tarun and Yishay Yafeh. 2007. "Business Groups in Emerging Markets: Paragons or Parasites?" *Journal of Economic Literature* 45: 331-372.

Khwaja, Asim Ijaz and Atif Mian. 2005. "Do Lenders Favor Politically Connected Firms? Rent Provision in an Emerging Financial Market." *Quarterly Journal of Economics* 120: 1371-1411.

Kurban, Dilek and Ceren Sozeri. 2012. "Caught in the Wheels of Power: The Political, Legal and Economic Constraints on Independent Media and Freedom of the Press in Turkey". TESEV, Istanbul

Li, Jiatao and Yi Tang. 2013. "The Social Influence of Executive Hubris: Cross-Cultural Comparison and Indigenous Factors." *Management International Review* 53(1): 83-107.

Nam, Chang-Hee. 1995. "South Korea's Big Business Clientelism in Democratic Reform." *Asian Survey*, 25(4): 357-366.

Öniş, Ziya. 1997. "The Political Economy of Islamic Resurgence in Turkey: The Rise of The Welfare Party in Perspective." *Third World Quarterly* 18(4): 743-766.

Öniş, Ziya. 2011. "Power, Interests and Coalitions: The Political Economy of Mass Privatisation in Turkey." *Third World Quarterly* 32(4): 707-724.

Polat, Necati. 2013. "Regime Change in Turkey." *International Politics* 50(3): 435-454

Pradhan, Jaya Prakash and George Lazaroiu. 2011. "Rise of Emerging Economies: An Introduction." *Economics, Management, and Financial Markets* 6(1): 8-18.

Ramamurti, Ravi. 2000. "A Multilevel Model of Privatization in Emerging Economies." *The Academy of Management Review* 25(3): 525-550.

Roberts, Brian E. 1990. "A Dead Senator Tells No Lies: Seniority and the Distribution of Federal Benefits." *American Journal of Political Science* 34: 31-58.

Robinson, James. A. and Thierry Verdier. 2002. "The Political Economy of Clientelism." Centre For Economic Policy Research, Discussion Paper No: 3205.

Salas-Porras Alejandra. 2005. "Changing the Basis of Political Support in Mexico: Pro-Business Networks and the Market Reform Agenda." *Review of International Political Economy* 12(1): 129-154.

Sapienza, Paola. 2004. "The Effects of Government Ownership on Bank Lending." *Journal of Financial Economics* 72: 357-384.

Spence, Michael. 2011. *The Next Convergence: The Future of Economic Growth in A Multispeed World*. New York: Farrar, Straus and Giroux.

Tuğal, Cihan Ziya. 2009. *Passive Revolution: Absorbing the Islamic Challenge to Capitalism*. Stanford University Press, Stanford, California.

Tuğal, Cihan Ziya. 2012. "Fight or acquiesce? religion and political process in Turkey's and Egypt's Neoliberalizations." *Development and Change* 43(1): 23-51

Uygur, Selçuk. 2009. "The Islamic Work Ethic and the Emergence of Turkish SME Owner-Managers." *Journal of Business Ethics* 88 (1): 211- 225.

Yalçın, Soner. 2012. *Samizdat*. Doğan Yayıncılık, Istanbul.

Yavuz, Hakan M. 2004. *Islamic Political Identity in Turkey*. Oxford University Press, Oxford.

Wank, David L. 2002. "Business-State Clientelism in China: Decline Or Evolution." In *Social Connections in China: Institutions, Culture, and the Changing Nature of Guanxi*, Edited by D. Gold, D. Guthrie and D. Wank. . Cambridge: Cambridge University Press.

Zhang, Qi and Mingxing Lui. 2010. "Local Political Elite, Partial Reform Symptoms, and the Business and Market Environment In Rural China." *Business and Politics* 12(1): 1469-3569.

Figure 1. The composition of PCF in the fastest rank ascends and drops (Net Sales)

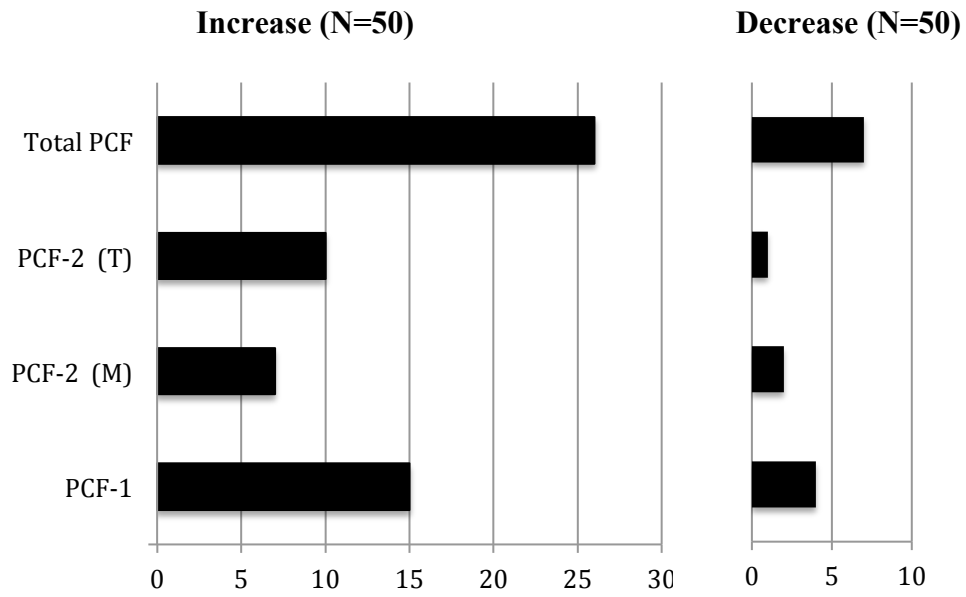


Figure 2. The Composition of PCF in the fastest rank ascends and drops (Assets)

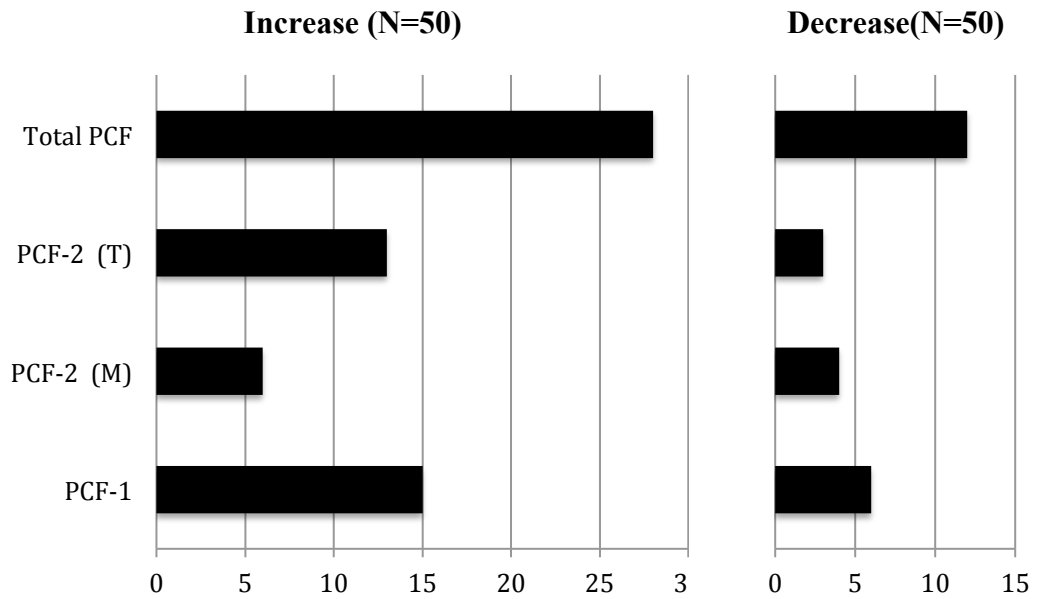


Figure 3. The Composition of PCF in the fastest rank ascend of 25 new entrants (Net Sales and Assets)

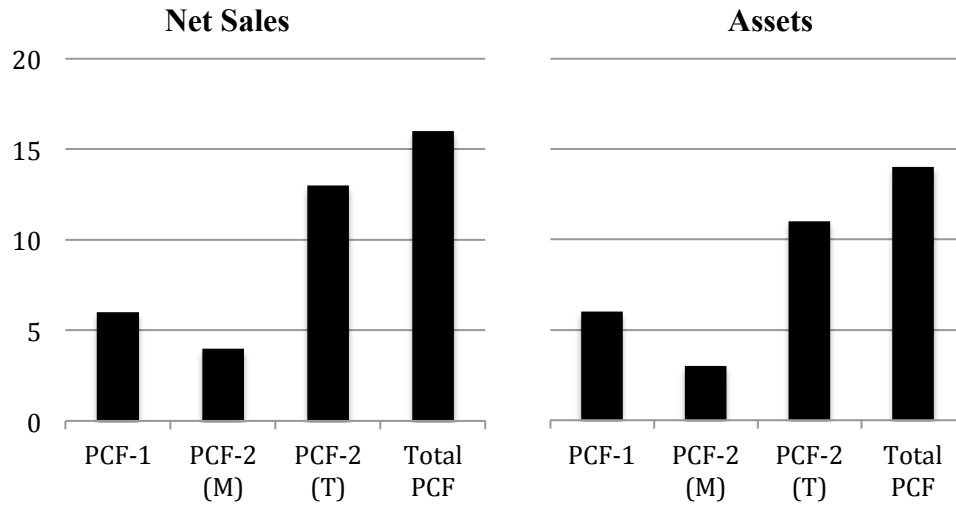


Table 1. Descriptive Statistics of Top 1000 in 2011

Variable	N	Mean	Median	S.D.	Min	Max
Sales (mil.TL ^a)	947	390	160	1100	71	27000
Value added (mil.TL)	671	150	32	930	-480	20000
Export (th. \$)	787	88	29	286	3	4245
Employee	834	816	450	1325	12	14703
Asset turnover	799	1.3	1.1	1	0.05	17
Labour productivity (th.TL)	657	169	78	732	-2167	14000
Profit rate	671	0.057	0.034	0.13	-1.4	1.3
Rank ^d	1000	501	501	289	1	1000

Source: Istanbul Chamber of Industry, the top 500 and the second top 500 industrial enterprises of 2011 based on the authors' own analysis

^a Average exchange rate was 1.68 TL/\$ in 2011.

^b Asset turnover is calculated by dividing net sales to total assets.

^c Labour productivity shows the value added per employee.

^d Rank is based on net sales.