

Economic development and social policies in Mexico

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Abstract

Since the mid-1980s Mexico has implemented a radical reorientation of its development strategy away from state-led industrialization and trade protection. This reform has drastically reduced the role of the state in the economy in favour of market mechanisms, and changed the orientation of social policies towards targeting and decentralization. The article examines the effects of this reform on Mexico's social and economic development, and finds that its results have been far from stellar. Indeed, notwithstanding the reduction of inflation and the downsizing of the state, the economy has expanded at a slow rate way below its growth in needs. The authors conclude that if Mexico is to succeed in its quest to enter a path of robust long-term development it will need to modify its social and economic policies.

Keywords: social policies; Mexican economy; economic development; social development; neoliberal reforms; NAFTA.

Introduction

Over the twenty-five years since the international debt crisis of 1982 Mexico has been involved in a radical reorientation of its development strategy. This process has had consequences not only for its economic policy but also for

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social welfare. Mexico's abandonment of its traditional development model based on import substitution and state-led industrialization was also accompanied by a shift from policies aimed at universal welfare provision. In its place it adopted a neo-liberal agenda of trade and financial liberalization, a reduced role for the state in the economy and the introduction of social policies based on means-tested, targeted programmes. Government officials, as well as a number of mainstream economists, argued at that time and well into the 1990s that reforming economic and social policies was essential if Mexico was to achieve rapid and sustainable economic growth along with a substantial reduction of poverty.

As is by now well known, these expectations were not fulfilled, although the reforms did result in annual inflation stabilizing at single digit levels, while the budget deficit was also eliminated. However, Mexico's growth has been sluggish and subject to periodic financial crisis, and it has failed to create the number of jobs required by the labour force – estimated at between 800,000 and one million per year. The very limited expansion of employment that has occurred has put enormous pressure on the system, exceeding the capacities of the targeted social policies to improve significantly the living standards of the vast proportion of the population living in poverty. In fact, as we argue in this and other contributions, the reduction of poverty achieved in the last ten years has been determined much more by the increase in the proportion of economically active population – associated with Mexico's demographic transition – than by the impact of social policies including those aimed at relieving poverty through cash transfers. While these programmes of targeted social expenditure have improved the education and health indicators of many poor families, they are not able fully to compensate Mexican society for the adverse social consequences of the slow expansion of employment and economic activity. Indeed, given Mexico's slow economic growth, it may be argued that without the 'demographic bonus' even the best-designed, best-funded and best-administered social policies would fail to bring significant improvement in the living standards of the poor. The purpose of this article is to present the main characteristics of Mexico's shift to neo-liberal economic and social policies and to examine their overall impact. The Mexican case has been seen as a paradigmatic example of a drastic and thorough implementation of the neo-liberal reform agenda, so it is important to identify some reasons why these reforms failed to meet the expectations that accompanied their introduction in the mid-1980s.

As we shall argue, the downsizing of the Mexican state led to a contraction of public investment that was not compensated for by the private sector. The consequent collapse of the investment ratio made it more difficult to modernize and expand the capital equipment necessary to increase the international competitiveness of the domestic economy. The tendency of the real exchange rate to rise contributed to a worsening of the growth potential of the export sector. In this context of an overall economic slowdown and poor employment performance, Mexico's social policy seemed to be running up

a down escalator, having to deploy additional resources just to keep pace and so avoid a massive deterioration of social conditions.¹ A key characteristic of the Mexican case, shared by most Latin American countries in the 1990s, is that the neo-liberal reforms failed to put the economy on a path of sustained and robust expansion. In these conditions, social policies were incapable of fully compensating for the adverse effects of the economic slowdown and the lack of job opportunities.

Background: Mexico's traditional economic development strategy (1950s–81)

In the period after the Second World War, Mexico's pursuit of economic development relied upon public sector intervention to foster industrialization via import substitution industrialization (ISI). This economic strategy was complemented by social policies aimed at universal coverage of basic social services – health, education, water and sanitation. ISI strategy was designed to protect Mexico's domestic market for manufactures from the pressure of the competition of imports. Trade protection was achieved by applying tariff duties on imports, by imposing the requirement of permits prior to importation and by prohibiting the entry to the domestic market of a wide variety of imported goods. In turn, direct foreign investment was strictly regulated, being accepted as a minority partner in some areas while it was excluded in so-called strategic areas.

In addition, active industrial policies and subsidies were used to strengthen the manufacturing industry, especially in the production of consumer and intermediate goods (Ros, 1994).² Other channels through which manufacturing received additional and special support from the government included: 1) high wholesale domestic prices for final products due to trade protection; 2) subsidized, low-cost energy and other utilities; and 3) easy access to credit from development banks and tax exemptions on certain imports of machinery and equipment (Moreno-Brid & Ros, in press). An original element of Mexico's ISI strategy was the Maquiladora programme. It was put in place to stimulate, through tax exemptions and import incentives, the establishment of labour-intensive, in-bond assembly plants along the northern border region situated to favour exports to the United States. Finally, during these decades many public enterprises were created in order either to intervene in key markets or to avert the bankruptcy of certain private firms and thus to protect employment (Rogozinsky, 1996).³

In the late 1970s, Mexico's economic expansion lost momentum as the ISI strategy entered the phase of attempting to substitute imports of high-technology machinery and equipment at the same time as the world economy slowed due to the oil shocks. In 1977 the Mexican government launched an ambitious development programme funded by the vast inflow of oil revenues and external debt. The programme boosted Mexico's economy. In 1977–81 its

real GDP expanded at an average annual rate that was over and above 8 per cent, but fiscal and foreign exchange revenues became critical and increasingly dependent on petroleum exports as imports of intermediate and capital goods soared. The collapse of the international oil market in 1981 coupled with the rise in US interest rates triggered a balance of payments crisis in Mexico that forced President López Portillo to declare a moratorium in August 1982 on external debt service payments. This action ended nearly forty years of Mexico's steady economic expansion and ultimately led to the demise of ISI and the abandonment of state-led industrialization.

It was, however, acknowledged that ISI and its social policies had positive impacts on Mexico's development. Indeed, in its four decades of implementation, Mexico's per capita real GDP grew at an annual average rate over and above 3 per cent. Such dynamism, essentially driven by the impulse of manufacturing industry, transformed Mexico from an agrarian to an urban, semi-industrial society, and the incidence and depth of poverty decreased. However, notwithstanding such merits this strategy had been unable to remove key obstacles on Mexico's road to development. The first was the unequal distribution of the benefits of economic growth. Indeed, despite four decades of continuous economic expansion, the distribution of income and wealth in Mexico remained extremely uneven and poverty still stood at unacceptably high levels.

A second obstacle was that, with the exception of the Maquiladora and the special development programmes applied to a few industries, the strategy had not been able to build a strong non-oil export sector or a competitive domestic capital goods industry. The third was the failure to implement fiscal reform that would strengthen tax revenues and thus reduce the public sector's dependence on oil and external debt. Weak fiscal revenues reflect a weak public sector and state. A fourth obstacle was that social policies were never backed by sufficient fiscal revenues to be able to achieve the goal of universal protection of basic needs for the rapidly expanding population. Moreover, the design and benefits of social insurance schemes were tightly linked to the evolution of formal employment,⁴ marked by an inadequate system of pension and health contributions that did not guarantee their long-term solvency. All these limitations proved fatal.

The end of ISI and the shift to neo-liberalism

The government of Miguel de la Madrid (1982–8) initiated the process of radical macroeconomic reform, with policies of trade and financial liberalization, market deregulation, privatization and the sharp reduction of the state's intervention in the economy. By the mid-1980s, numerous tariff and non-tariff restrictions on imports were removed, and Mexico had become a full member of GATT. Public expenditure was slashed. President Salinas de Gortari's administration (1988–94) accelerated these reforms by rapidly and

significantly opening the domestic financial market to foreign competition, carrying out a vast wave of privatizations of public enterprises (including the sale of the telephone company and the domestic banking system) and eliminating many restrictions on FDI in manufacturing except in the production of explosives and basic petrochemicals (Clavijo, 2000; Moreno Brid & Ros, in press).

The jewel in President Salinas' drive to deepen economic liberalization was the launch of the North America Free Trade Agreement (NAFTA) between Mexico, Canada and the United States in 1994.⁵ It went into effect on 1 January 1994, eliminating, over the next ten to fourteen years, virtually all tariff and non-tariff barriers to intra-regional trade and further easing restrictions on FDI. NAFTA formally institutionalized Mexico's trade liberalization and gave it a long-term perspective. Since then Mexico has joined the OECD and the WTO, and has signed free trade agreements with numerous countries, including Chile (1991), Costa Rica (1994), Colombia, Venezuela (1994), Bolivia (1994) and Japan (2004). Today, except for phytosanitary regulations, Mexico keeps very few trade restrictions. In fact, in 2008, all non-tariff restrictions on trade on agricultural goods, including maize, were lifted.

The reforms brought about a fundamental shift in industrial policy, eliminating all sectoral development programmes and substituting them with so-called 'horizontal' policies applied across the board. Credit and tax subsidies, trade protection schemes and other policies aimed at strengthening selected industries or sectors were cancelled. Instead of trying to 'pick winners', the new policy focused on simplifying administrative procedures, cutting red tape and speeding up tax deduction of depreciation allowances (Clavijo, 2000). Presidents Zedillo (1994–2000) and Fox (2000–6) advocated a certain reorientation of industrial policy. Though explicitly rejecting any notion of going back to trade protectionism, they argued that trade liberalization had led to an excessive de-linking of some productive chains in the Mexican manufacturing sector. They concluded that some sectoral-specific programmes were required to increase Mexico's international competitiveness. However, their exhortations ended up being merely rhetorical as they failed to allocate sufficient funds to create and implement such programmes.

It is too early to assess Calderón's administration (2006–12) but so far it has followed a similar macroeconomic strategy to its predecessors – namely, it is committed to NAFTA and fiscal balance – while still shying away from active industrial policies. It should be noted, however, that at the beginning of 2008 the President and the Minister of Finance announced the launch of a strong public investment work programme geared at trying to reduce the impact of the adverse external shocks caused by the slowdown of the US economy. How significant will this programme be in practice? Will it imply a change in policy towards a renewed, more active participation of the state in modernizing infrastructure and thus strengthening the international competitiveness of the Mexican economy? These are still open questions.

In Mexico, as elsewhere in Latin America, the economic reforms were accompanied by changes in social policy, in terms of their goals as well as in their key instruments. As noted, social policies were previously centred on gearing public expenditure and subsidies to expanding the supply of health, education and other basic services premised on an ambitious but far from realized goal of guaranteeing universal social protection. Such social protection tended to be strongly dependent on the formal employment of the beneficiaries. The reforms were gradually reoriented to subsidizing demand, with an emphasis on focusing social expenditure on a targeted sector of the population in poverty. The government also began to rely on conditional cash transfers to increase the human capital of the poor in the hope of improving their long-term labour and economic prospects.⁶ Though their human capital has certainly improved through these initiatives, the latter expectations concerning their better insertion in the labour market are yet to be fulfilled.

Mexico's economy after the neo-liberal reforms

The positive outcomes: low inflation and booming exports

The neo-liberal macroeconomic reforms together with NAFTA had positive effects on Mexico's fiscal performance, domestic inflation and participation in global markets. As is amply documented, the reduction of state intervention in the economy was also marked by a slashing of public investment and a strong commitment to avoid fiscal deficits. However, the federal government's fiscal revenues remained weak. In 2007 they represented only 12 per cent of GDP when oil is excluded, and 17.5 per cent if it is included, revealing a heavy dependency on oil income. Monetary policy tends to maintain a constant nominal exchange rate which helps to reduce inflationary expectations but leads to persistently overvalued real exchange rates.

The macroeconomic reforms undoubtedly had a significant impact on Mexico's foreign trade. On the one hand, exports soared after their implementation, and their composition changed dramatically. Indeed, in the late 1970s Mexico was basically an oil-exporting economy, but by 1988 manufactures provided more than 50 per cent of total exports. Today, even though the price of crude petroleum oil has significantly increased the share of oil exports, the share of manufactures in total exports exceeds 80 per cent (see Figure 1).

Parallel to this export boom, there has been a surge in imports. In fact, applied econometric studies reveal that in the last fifteen to twenty years Mexico's economy has significantly increased its structural dependence on imports (see, *inter alia*, Pacheco-López, 2005; Moreno-Brid, 2001, 2002). The results indicate that in the last twenty years Mexico's long-term 'income elasticity' in the demand for imports has more than doubled. Traditionally its

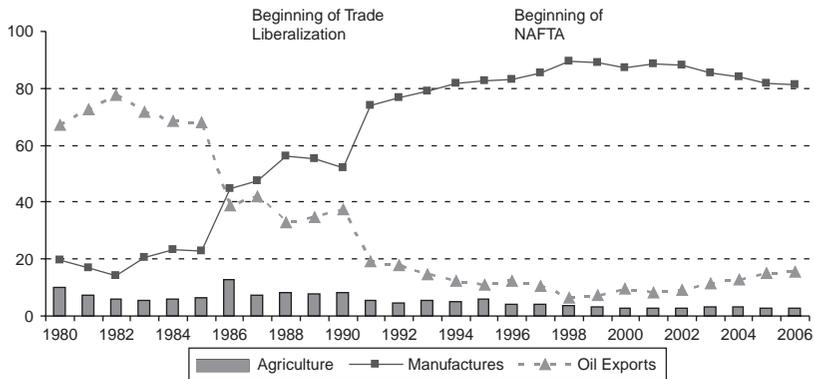


Figure 1 Composition of total exports, Mexico 1980–2006 (%)

Source: Authors' elaboration based on INEGI (2007).

value stood between 1.2 and 1.5, but it has since risen to levels close to 3.0. This implies that if Mexico's real income is to grow at an annual average long-term rate of 5 per cent, its imports in real terms would tend to expand by 15 per cent. To keep the trade deficit in check as a proportion of income, Mexican exports should expand by at least 15 per cent per annum. Such rapid export growth seems unlikely to be sustained in the long run, especially now that the US economy is experiencing a slowdown that could be long-lasting. Given this binding external constraint, it should not come as a surprise that Mexico's economic growth after the macroeconomic reforms has been disappointing. In fact, its real gross domestic product (GDP) expanded during 1990–2006 at an average rate way below its historical average in 1950–80. Moreover, it has remained incapable of generating sufficient jobs.

Figure 2 illustrates how trade liberalization along with other macroeconomic reforms has failed to put Mexico on a path of strong export-led growth. It shows that, for the economy as a whole, the relation between trade performance (measured by the trade deficit as a percentage of GDP) and economic growth has deteriorated. Indeed, during 1971–81, Mexico's real GDP expanded at an annual average rate of above 7 per cent and registered a trade deficit of 2.7 per cent. The collapse of the oil boom forced an economic slowdown in the 1980s concomitant with a significant trade surplus. The first years after NAFTA – excluding 1995 – saw real GDP expand at more than 5 per cent annual average. This recovery was short-lived. The real appreciation of the peso and the slowdown of the US economy in 2001 put an end to the dynamism of this short period of export-led growth. Moreover, in 2001–6, the Mexican economy barely grew (less than 3 per cent on an annual average rate), registering a trade deficit of close to 1 per cent. In other words, although exports have been extremely dynamic since the reforms, they have been increasingly unable to pull the rest of the Mexican economy along a path of strong expansion. This is starkly illustrated by the evolution of its income per capita relative to the US. As

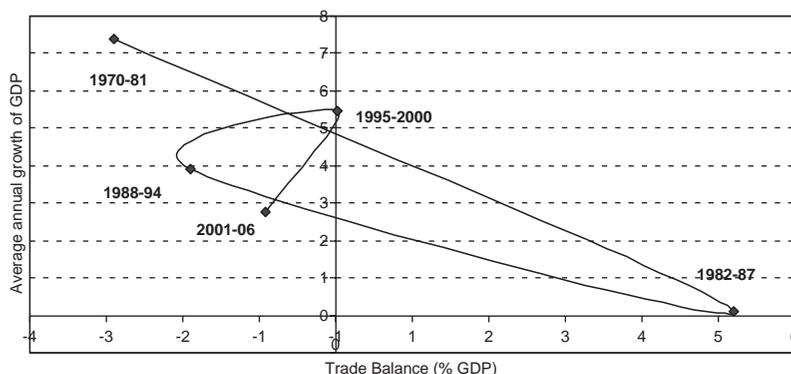


Figure 2 Trade balance and real GDP growth in Mexico, 1970–2006

Figure 3 shows, in the early 1980s the gap between the two countries widened. While it narrowed slightly in the late 1980s, it widened again after the economic crisis of 1995. Since then, notwithstanding the macroeconomic reforms, it has not recovered and in 2006 stood at a level comparable to that of the 1950s.

Summing up, Mexico’s shift towards a neo-liberal strategy has had mixed but rather disappointing results. On the positive side, it did help to reduce the fiscal deficit and to achieve stable, low rates of inflation. It brought about a surge of non-oil exports and of foreign direct investment. Indeed, in the last twenty-five years Mexico went from being just an oil-exporting country to becoming a major export platform of manufactured goods, including vehicles, auto parts, ready-made clothing and electronic products, to the United States. But on the negative side, overall economic growth has been too slow. Moreover, the various foreign exchange crises have prevented the consolidation of a sustained and robust economic expansion.

Part of the explanation for this failure lies in the fact that an overall upturn in investment did not accompany the reforms associated with the new macroeconomic environment. Indeed, fixed capital formation has remained at a level equivalent to less than 22 per cent of GDP. This percentage is way below the 25 per cent benchmark identified by UNCTAD as the minimum investment ratio required to sustain a medium-term annual economic expansion of 5 per cent. This lack of investment is to a certain extent explained by the sharp fall in public investment.

In addition, although financial liberalization brought about a deep restructuring of Mexico’s banking sector, domestic credit availability for productive activities and investment has been severely rationed for the last ten years. As a share of GDP, banking credit to support productive activities shrank between 1996 and 2006 by more than 15 points. Thus Mexico’s economy has been acquiring the characteristics of a dual structure. There are a few very large firms and activities whose links with transnational corporations and easy access to foreign capital have helped them to become relevant players

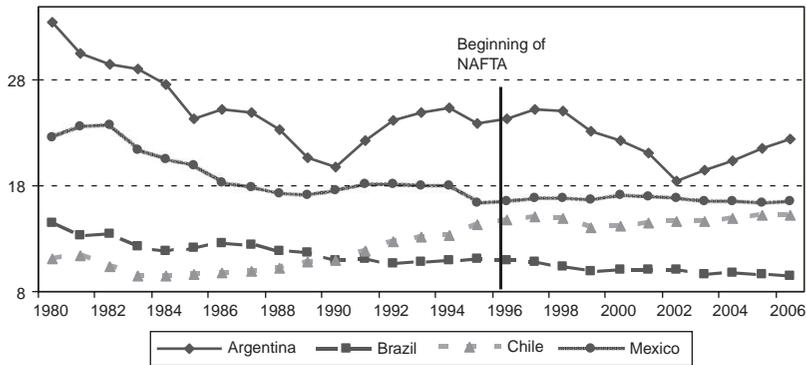


Figure 3 Mexico and other countries: real GDP per capita (relative to the USA) 1980–2006 (USA GDP per capita = 100, measured in constant 2000 US\$)

Source: Own elaboration based on World Bank, World Development Indicators (2006).

in world markets. But there is a vast number of medium and small firms and thus a large informally-employed population, struggling to survive the intense pressure from their external competitors.

Job creation in Mexico after the reforms has been disappointing. There has been some re-composition in favour of export-related activities but, all in all, employment growth has been far from dynamic. In 2006, open unemployment reached its highest level in years, with a vast proportion of the employed being accounted for by the informal sector. The earnings and wage gap between the qualified and the unqualified labour force has widened. The weak labour absorption capacity of the economy has fuelled migration flows to the US, with approximately 400,000 Mexicans – in net terms – migrating abroad each year.

Key aspects of Mexico's social policies after NAFTA

After the cancellation of some social programmes put in place during the oil bonanza and drastic cuts in public social spending throughout the severe external and fiscal crises faced by the De la Madrid administration (1982–8), social policy became a key axis of the Salinas administration's political strategy (1988–94). Fiscal expenditure has since been reoriented to social development.⁷

Table 1 shows selected indicators of Mexico's public expenditure on social development and poverty alleviation for the Zedillo (1995–2000) and the Fox administrations (2001–6). This shows that in both periods government expenditure on the social sector expanded at a faster rate than real GDP. Its pace, however, slowed down from 6.6 per cent in 1995–2000 to 3.7 per cent in 2001–6. This also indicates that social spending rose as a share of GDP from an average of 8.9 per cent to 10.1 per cent. This increase in social spending has not been concentrated solely in the programmes earmarked for poverty

Table 1 Mexico: selected indicators of public expenditure in social development 1995–2000 vs. 2001–6

	1995–2000	2001–6
Real GDP growth (average, %)	3.5	2.4
Public expenditure: social development (%, GDP)	8.9	10.1
(average annual growth, %)	6.6	3.7
Public expenditure: poverty alleviation (% of GDP)	1.1	1.4

Source: Cabrera (2007), based on official data.

alleviation. Indeed, as a share of GDP, these latter expenditures rose from a low average of 1.1 per cent of GDP in the Zedillo administration to an average of 1.4 per cent under Fox.

The increase in public expenditure for social development has been a feature common to the Latin American region over the last two decades (CEPAL, 2004).⁸ In Mexico, although the increase was slightly higher than the average in the region, social spending as a proportion of GDP is still below Latin America’s average. Moreover, it falls way short of guaranteeing universal protection or coverage in the social security system. Today the majority of Mexican households do not have a single member enrolled in the social security system. As Diaz Cayeros, *et al.* (2008), quoting a World Bank study, state: ‘75 per cent of the non poor, 39 per cent of the moderately poor and zero per cent of the extreme poor are covered either by the *Instituto Mexicano del Seguro Social* (IMSS) or by the *Instituto de Seguridad y Servicios Sociales de los Trabajadores del Estado* (ISSSTE).’

What lies behind this increase in social expenditure in Mexico? On the one hand privatization, deregulation and the elimination of industrial policies brought about by the neo-liberal reforms gave room for an increase in public expenditure for social purposes. In addition, the resumption of economic growth, however modest, since the early 1990s brought more fiscal revenues and thus increased the resources that could be devoted to meet social needs. Finally, there has been increased pressure from civil society to allocate more resources to ameliorate the living conditions of the poor population after the severe deterioration suffered during the 1980s. This pressure may have increased *pari passu* with the deterioration in employment prospects. In any case, as in the rest of Latin America, Mexico’s transition to more democratic forms of government since the late 1990s went along with a strengthening of social policy as well as of special programmes oriented to alleviation of poverty.⁹

The education challenge

Public education is a cornerstone of Mexican social policy and the most important in terms of government social expenditure. For 2006, the allocation

for the Ministry of Public Education represented 6.9 per cent of the total federal budget. If we take into account the funds allocated to the federal entities and municipalities the percentage rises to 9.2. When combined with resources invested by the private sector in education, Mexico's total expenditure on education is today equivalent to approximately 6.6 per cent of its GDP.

Although education policy has not reached its full potential as a tool for poverty reduction, recent data confirm some progress. The number of student enrolments, (preschool to postgraduate studies), jumped from 13 million in 1970 to 32 million in 2002. In the same period, the average number of years of school attendance rose from three to seven. Children who started elementary school in 2002 are expected to complete, on average, eleven grades of school, a significant increase over the 2.6 grades completed in 1960. Despite good coverage for basic education, demographic changes are placing enormous demands on high school and university education. Mexico needs to invest massive resources in order to widen the coverage of higher education. The other challenge is to improve the quality of Mexico's public education system. The Programme for International Student Assessment (PISA) test for 2003 was taken by more than a quarter of a million students in forty-one countries, to assess their skills in mathematics, reading, science and problem-solving (OECD, 2003). On average, Mexico ranked thirty-eighth in the three sections of the test. In mathematics, Mexico was placed in the bottom group with 375 points, way below the top performers: Korea and Finland (550 points). Moreover, only one-third of the group of 15-year-old students who participated in the PISA test 2003 had adequate basic skills in mathematics.

Mexico's poor results are explained not so much by the quantity of resources it dedicates to education as by its inefficiency in using them. Indeed, in 2003, Korea's total expenditure in education – by the public and the private sectors – was equivalent to 7.5 per cent as a proportion of GDP. Mexico's was somewhat lower at 6.8 per cent, but more than two points higher than Spain's (4.7 per cent) and Ireland's (4.4 per cent). However, the latter two countries' average scores in mathematics were more than 100 points higher than Mexico's. The OECD study reveals that, of Korea's total expenditure in education in 2003, 59 per cent was carried out by the public sector and 41 per cent by the private. In the US, the share of the public sector was 72 per cent, and in Mexico it was even higher at 82 per cent, with Spain at 89 per cent and Ireland at 93 per cent. In addition, Mexico shows marked differences in the composition of public expenditure (between current and fixed capital formation) compared to the other countries. While in Mexico only 3 per cent is dedicated to investment (i.e. 97 per cent is current expenditure), in Ireland it is 8 per cent, in Spain 9 per cent and in Korea 19 per cent.

On the other hand Mexico and Slovakia are the countries with the smallest expenditures on education. Data from the OECD show that Mexico spends an average of US\$15,000 (measured at constant purchasing power parity) to cover education from age 6 to 15. Greece spent twice as much; Ireland, Korea, Spain

and Portugal three times as much; Italy, Denmark, the United States, Switzerland more than five times as much (OECD, 2004). The 2003 PISA results suggest that most Mexican children are not receiving sufficiently high educational skills to bring their human capital up to international standards. Thus public and even private education are in danger of failing to break the inter-generational cycle of poverty.

Other key elements of social expenditure in Mexico

As in the rest of Latin America, programmes of targeted conditional cash transfers have proliferated in recent times. Pronasol was the first of this kind in Mexico. It was established by the Salinas administration as a national anti-poverty programme to offer funds for public works conditional on the beneficiary communities' active participation and on municipal or state governments' cooperation through matching grants. This programme was marked by discretionary, publicized allocations of public spending in selected poor regions. It was used by President Salinas to exploit the political gains of social expenditure. Indeed, his government sought to legitimize its revolutionary credentials with Pronasol and to strengthen the control of the ruling party (the Partido Revolucionario Institucional) over the results of the electoral processes (Díaz Cayeros *et al.*, 2008). However, when President Salinas's popularity collapsed with the 1994–5 foreign exchange crises, Pronasol was harshly criticized and seen as a political manoeuvre designed to buy the votes of the poor.

In 1997, the Zedillo administration replaced Pronasol with Progresá, a human development scheme that combined cash transfers to poor households in rural areas conditional on their children attending local schools and the family attending regular checks at regional health clinics. These conditional cash transfers and the selection of beneficiaries are calculated on a formula-based targeting scheme, and given to the woman of the household independently of whether or not she is its head. In 2002 President Fox changed the programme's name to Oportunidades. He retained the multi-dimensional approach of targeted subsidies combined with obligatory school attendance and medical clinic visits, but introduced some changes. He widened the programme's coverage to include urban areas and also subsidized three more years of education, thus covering elementary, junior high and high school (twelve years of education), just short of university. A third change was the creation of the spin-off programme Jóvenes con Oportunidades (Youngsters with Opportunities), which provided a savings account for children of beneficiaries if they were performing satisfactorily in the last three years of high school. The funds could be accessed only after graduation in the hope that they would assist in meeting the costs of university or of opening a small business. The number of beneficiaries of Oportunidades jumped from 2.5 million families in 2000 to 5 million after 2004, with 68.8 per cent of the

beneficiaries located in rural areas, 17.2 per cent in semi-urban regions and 14 per cent in urban centres. By 2006, the beneficiary households were receiving an average transfer of US\$45 per month. The programme also provided nutritional supplements for pregnant and breast-feeding mothers, as well as for children under the age of 5.

Independent evaluations have systematically confirmed the positive and significant impact of Oportunidades in improving the nutrition, health and education of its beneficiaries (see, *inter alia*, de Janvry & Sadoulet, 2006; Behrman, Sengupta & Todd, 2002). In 2006 Mexico's National Institute of Public Health prepared an independent evaluation whose major findings are summarized in Table 2. Every three years there is a verification process to investigate whether beneficiary families are still meeting its targeting requirements. The 2006 exercise concluded that 20,000 families had, so to speak, graduated from Oportunidades. They stopped living in poverty and had incomes high enough to satisfy their food, health and education needs. This number represents barely 0.4 per cent of the total of 5 million families covered by Oportunidades, a rather low percentage for the programme to be considered an effective instrument in eradicating poverty. Even if the percentage of 'graduation' were five times higher, i.e. 2 per cent, it would imply that, *ceteris paribus*, this transfer scheme would take at least five decades to eradicate poverty.¹⁰

Table 2 Evaluation of Oportunidades 2006

Area	Achievements
<i>Education</i>	Reduced fail and drop-out rates, and improved likelihood of students (especially females) continuing their education from elementary to high school and from high school to college. Improved educational achievement and greater willingness of parents to promote continuous schooling for their children and the fulfilment of their school obligations. (The positive effects were usually greater for girls).
<i>Health</i>	Reduced mortality rates in mothers and children. Municipalities incorporated in the programme reported on average lower rates (11% and 2%, respectively). Large increase in the use of public outpatient health services for all ages and reduction in the use of private services, thus generating savings for beneficiaries.
<i>Nutrition</i>	Reduction in the high proportion of anaemia. Increase of height and weight of children in their early years. Children aged 24 to 71 months in the beneficiary communities grew on average somewhat more than the control group, and the high proportion of low weight was reduced by 12.4%. Incidence of anaemia was reduced in rural children of 2 and 3 years. The motor abilities of girls and boys from 3 to 6 years increased by 10% and 15%, respectively, and there was an improvement of 9% in the social behaviour of girls. Improvement in the diet of beneficiary households, allowing them to buy products of animal origin and provision of nutritional supplements for a large proportion of children.

Source: Cruz, de la Torre & Velázquez (2006).

The improvements in education and in nutrition due to this programme are apparently increasing the capabilities and human capital of beneficiary children. Such benefits, however, are not automatic but depend in particular on the quality of the education received. If the school does not have adequate infrastructure, good and motivated teachers and educational material, the merits of the conditional cash transfer programme as far as human capital formation is concerned are questionable. In any case, whether these changes are significant or sufficient to guarantee the beneficiaries better access to quality jobs that may enable them to escape poverty is an open question. Moreover, the answer depends not so much on *Oportunidades per se*, but on whether the Mexican economy can grow rapidly and create enough jobs. So far this has not occurred and, given the current economic situation in the United States, it is unlikely to occur in the short and medium term.

Oportunidades has improved the human capital of many poor families and has reduced, though not necessarily eliminated, the politically discretionary character of transfers to poor families. However, its impact on reducing long-term poverty, as evidenced by the low rates of 'graduation' of poor families among its beneficiaries, seems to be insignificant. In any case, it would be erroneous to expect that a poverty alleviation programme would significantly reduce the incidence or depth of poverty in an economy with the features characteristic of that in Mexico. In these conditions, no social programme by itself will significantly improve the living conditions of the poor. Apart from the need for sustained levels of growth required to produce the conditions that would break the inter-generational cycle of poverty, many more resources need to be allocated to poverty reduction, and this is unlikely given insufficient fiscal revenues, inefficiencies in their allocation and, crucially, the persistent deterioration in the conditions of employment due to the lack of dynamism of the Mexican economy. Insufficient public funding is and will be an obstacle for some years to come, unless another fiscal reform is implemented.

Social development in Mexico under two different development strategies

Poverty

Figure 4 depicts the evolution of poverty in Mexico based on official data from the Ministry of Social Development (SEDESOL) differentiating between three groups from the bottom to the top. The bottom group is associated with the notion of nutritional poverty. The middle group, defined as resource poverty, includes all people classified under nutritional poverty, together with those lacking access to basic health and education services. The top group defined as monetary poverty encompasses the population suffering nutritional

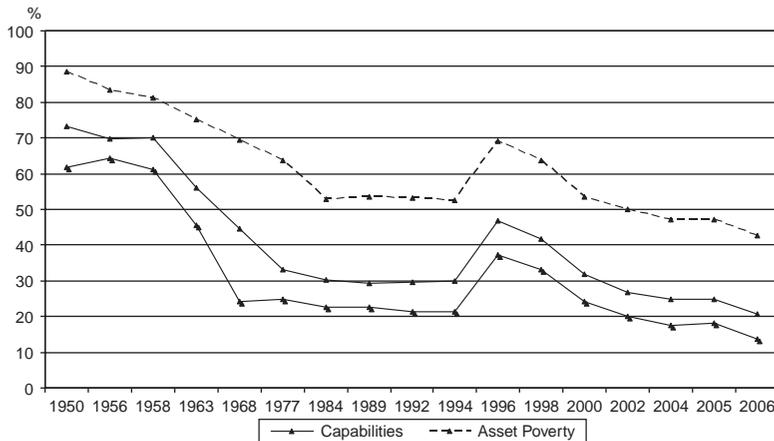


Figure 4 Poverty in Mexico, 1950–2006 (percentage of total population)

Source: Székely (2005) and CONEVAL.

Note: The three lines represent, from bottom to top: food poverty, poverty in access to basic services and poverty of overall resources.

and asset poverty, and also covers individuals with incomes insufficient to meet clothing, housing and public transportation needs.

From 1950 to 2006 there is a decline in the percentage of the population living in poverty, as measured by the three different indicators, though with periods of drastic change. From 1950 to the early 1980s – when the economy was following a strategy of state-led industrialization and ISI – the three indicators of poverty show a significant fall. This reduction was interrupted in the aftermath of the collapse of the oil bonanza in the mid-1980s. From then onwards, until the mid-1990s, there was virtually no advance in tackling poverty. This is not surprising given that in this period the Mexican economy remained practically stagnant.

Moreover, the crisis in 1995, when real GDP in Mexico shrank by almost 7 per cent, had a brutal impact on the socioeconomic conditions of a large proportion of the Mexican population. In fact by 1996 the incidence of poverty, as measured by each of the three distinct indicators, jumped more than fifteen points relative to its level in 1994, reaching levels comparable to those of the early 1960s. In 2000–6, moderate economic growth combined with an increase in the percentage ratio of the economically active population has led to a reduction of poverty (see Table 3). The rural areas, where most poor people are located, saw a decline in the three indicators of poverty from 2000 to 2006, and the same trend is evident in urban areas. At the national level, over these five years, the proportion of the population with nutritional poverty fell nearly ten points, that in poverty of access also fell about ten points and the resource poverty rate slightly more.¹¹

Table 3 Urban, rural and national poverty in Mexico, 2000–6

	Percentage			
	2000	2002	2004	2006
<i>National</i>				
Nutritional poverty	24.1	20.0	17.4	13.8
Poverty of access	31.8	26.9	24.7	20.7
Resource poverty	53.6	50.0	47.2	42.6
<i>Rural</i>				
Nutritional poverty	42.4	34.0	28.0	24.5
Poverty of access	49.9	42.6	36.2	32.7
Resource poverty	69.2	64.3	57.4	54.7
<i>Urban</i>				
Nutritional poverty	12.5	11.3	11.0	7.5
Poverty of access	20.2	17.2	17.8	13.6
Resource poverty	43.7	41.2	41.1	35.6

Source: Elaboration with data of CONEVAL: www.coneval.gob.mx/coneval/programameas%20pobreza/Cuadros%20de%20resultados.xls.

Inequality

Income distribution – as measured by the Gini coefficient – has been showing a long-term improvement since 1950, but with a U-pattern somewhat different from that of poverty (see Figure 5). In the 1950s to the early 1960s, income distribution became more concentrated. From then until the mid-1980s income was distributed more evenly, but the trend changed again when trade liberalization and macroeconomic reforms began to be implemented. For the next fifteen years, a more concentrated pattern of income is indicated. By 2004 the Gini stood at 0.46, which is above that reached in 1984 and above the world average (0.40). In addition, as in most developing countries, in Mexico the concentration of wealth is much higher than that of income. Such a high concentration of income is alarming taking into account the vast proportion of the population living under conditions comparable to those prevailing in much poorer countries.

This inequality in income distribution is also reflected regionally. On the one hand, the federal entities (*estados*) in the south are typically much poorer than those in the north. On the other, there is also considerable intra-state inequality, with acute differences in income and socio-economic indicators even within the same state, a difference that is frequently associated with rural–urban polarization. Such differences are mirrored to some extent in the indicators of access to basic services, health and schooling and in general human development indicators (UNDP, 2004).

Mexico also shows a somewhat strong and inverse correlation between economic growth and poverty.¹² In other words, in the last forty years, periods of

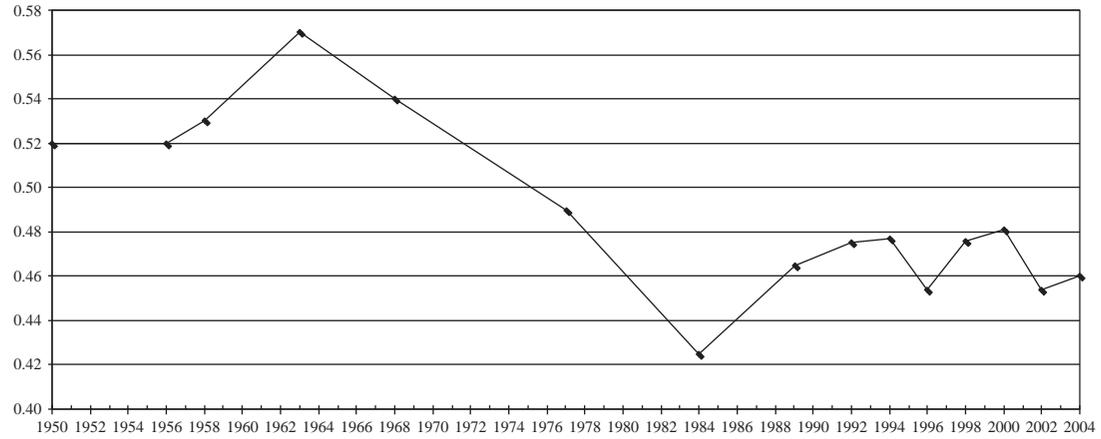


Figure 5 Inequality in Mexico 1950 – 2004 (measured by Gini coefficient)

Source: Szekely (2005).

strong economic expansion have tended to be associated with a more progressive distribution of income and a decrease in poverty. Moreover, episodes of balance of payment crisis and drastic contractions of economic activity have caused a sharp deterioration in the living conditions of the population, dramatically increasing the incidence of poverty and widening the gap between the haves and the have-nots. Particularly worrying is the fact that the adverse impacts on poverty due to economic crisis have not been fully compensated for by the effects of the subsequent resumption of economic growth. Thus, the volatility of economic growth has had an adverse and significant impact on the poor. This ratchet effect has implied, for example, that, even though Mexico's real per capita income in 2000 was 20 per cent higher than in 1984, the percentage of those in poverty for both years was very similar (see Uthoff, 2007).

There is a consensus that in Mexico trade liberalization has been a significant force behind the increase in inequality in the last twenty years.¹³ Indeed, it did contribute to the widening of the wage gap between skilled and unskilled workers. In addition, it also contributed to reducing the income elasticity of employment given that the economy's most dynamic sectors became highly dependent on the use of imported inputs, thus weakening their backward linkages.

In brief, approximately twenty-five years of neo-liberal reforms in Mexico have been accompanied by a reduction, albeit insufficient, in poverty and an increase in income inequality in the overall context of an economy marked by low rates of inflation and fiscal deficits and a slow rate of expansion. Part of the reason for such insufficient progress in social development in the last decades is the failure of the economy to enter a path of long and sustained expansion. It is important to examine to what extent this insufficient social advance is or is not linked to the evolution of the social policies implemented since the shift towards a neo-liberal development agenda. Moreover, as Moreno-Brid and Ros (in press) and recently the OECD show, the reduction in poverty in the last ten years, achieved in the midst of a laggardly performance by the Mexican economy, is actually a result of the 'demographic bonus'. Indeed, as we have stated in some of our previous work, a major cause of the decline in poverty in Mexico during this period is the rise in the ratio of economically active population; more precisely, in the average number of people employed per household, and not so much by an improvement in average real remunerations or by the effect of income transfers.

Conclusions

After more than twenty years of neo-liberal reforms the lack of robust economic growth has plainly become a major obstacle for social development. Among the reasons behind this failure stand the elimination of industrial policies, the reduction in public investment and the tendency of the real exchange rate to rise, all factors which have become common features of

Mexican policy. As long as strong economic growth and job creation are wanting, social policies, whether targeted or not, will be unable to bring about major improvements in poverty and inequality indicators.

Mexico's structurally weak fiscal situation was left uncorrected by the macroeconomic reforms of the 1990s. As noted, fiscal revenues represent a small proportion of GDP, in terms of international comparisons. Even more worrying, between 30 per cent and 40 per cent is derived from oil income. Such an under-funded state will find it increasingly difficult to improve the social and economic conditions of the poor not only in remote rural areas but also in urban areas. Starved of resources, the Mexican state increasingly runs the risk of being unable to maintain the minimum functionality of its key institutions and may begin to experience an erosion of its effectiveness and legitimacy.

For Mexico, as well as for emerging economies in general, the reduction of poverty and inequality is not only an ethical matter, but also a prerequisite for achieving a high rate of economic expansion. The neglect of these issues affects not only the poor but also the middle classes who have become increasingly frustrated by their unfulfilled expectations of improving, or at least maintaining, their standard of living. Large proportions of Mexico's middle class believe that their standard of living is lower than that of their parents, and fear that their own children will face still harsher economic conditions.

The magnitude of Mexico's development challenge is such that it requires a new social pact to engage the key political actors and economic and social agents committed to actively supporting it. Dealing with poverty and equality as secondary problems, detached from democratic processes and citizenship-building, will in all likelihood also fuel trends of political alienation, anomie and social disintegration. Social policy cannot be divorced either from economic policies and objectives or from the new demands for citizenship that call for increased diversity in the provision of welfare programmes, and call for more efficient and effective action by welfare services, particularly in health, education and social security. At the same time however, the principle of universal basic coverage and security should not be renounced. In essence this entails some compromise between efficiency and universalism which leaves some scope for targeted interventions. Beyond these key criteria is the question of how to decide the state's legitimate role in articulating and solidifying social cooperation as the basis of an integrated welfare state, instead of the truncated one that currently exists. We must approach this task through building new forms of solidarity from new or renewed social capital that connects communities, regions, cities and local governments with the state. This implies overcoming the current gulf between social and economic policies.

Mexico's economic growth is closely tied to circumstances beyond its national borders. With 88 per cent of its exports destined for US markets, the fortunes of economic growth and employment will be deeply affected by the performance of the US economy. To what extent Mexico's productive structure can be modernized if the process of integration with the US economy continues, and whether it will diversify to other markets in Europe

and Asia, are open questions. For some analysts, the road ahead is the currently far from any realistic possibility of adopting a regional economic development agreement with the US on the lines inspired by the European Union. Others point instead to the need to diversify Mexico's trade and investment markets, seeking greater synergies with Asia (especially China) while relying much more on developing domestic and regional markets. In any case, as the displaced population from the traditional agricultural system look for job opportunities beyond their locality, illegal emigration to the US will continue to be an obvious choice, albeit with declining rewards under present economic conditions.

Returning to the points raised at the beginning of this article, it seems that economic policy should aim to achieve not only a low rate of inflation and balanced fiscal accounts, but, above all, a high and sustained rate of economic expansion, matched by adequate job-creation rates in terms of number and quality. High and variable inflation should certainly be avoided, but 'stop and go' patterns of economic expansion that result in an average real GDP growth rate well below its potential trajectory must be avoided. Finally, Mexico urgently needs to integrate social and economic policy so that the short and long-run objectives of the latter – regarding, *inter alia*, inflation and economic growth – are tied to selected indicators of social development. One option would be to establish minimum levels of satisfaction of certain key basic needs, based on selected indicators of human or social development, and to condition macroeconomic policies to guarantee their satisfaction independently of the economic cycle. Such measures would establish a floor for human capital and automatic stabilizers for fiscal policy management. This would exert a countercyclical influence on economic activity, similar to that achieved by the introduction of the unemployment benefit in developed countries. The level and scope of such basic needs would have to be politically determined and fully backed by a social pact that achieved agreement of the relevant political and economic actors and of society as a whole. An indispensable input for this approach is a fiscal reform that aims, simultaneously, at ensuring a significant increase in non-oil public revenues as well as the adoption of mechanisms to monitor their transparent and efficient use to promote economic and social development. Building this social pact is perhaps Mexico's greatest challenge.

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Notes

1 We are grateful to one anonymous referee for having suggested this metaphor to illustrate the daunting challenge of social policies in the neo-liberal era: trying to avoid a deterioration of the living conditions of the poor provoked to a large extent by the incapacity of these reforms to usher in a new phase of high and sustained expansion of output and employment.

2 The most successful programmes during this period were in the auto industry, computerware and pharmaceuticals (Moreno-Brid, 1999).

3 In 1982, the peak year of Mexico's strategy of ISI and state-led industrialization, there were 1115 public enterprises. These enterprises had operations in forty-one out of a total of forty-nine branches of economic activity. Some of these forms had significant market power (Moreno-Brid, 1999) and carried out investment projects that the private sector could not or would not undertake. By 1994 only seventy such enterprises remained active.

4 These systems are sometimes defined as 'truncated welfare states, because the majority of the population especially the poor do not receive those benefits' (See Díaz Cayeros *et al.*, 2008).

5 When NAFTA negotiations started in 1990 Mexico was one of the economies most open to foreign trade (OECD, 1992).

6 As Díaz Cayeros *et al.* (2008) point out, conditional cash transfer programmes have various advantages: 1) effectiveness in targeting the poor, 2) immediate as well as longer-term impacts on poverty (the first is due to the cash transfer mechanism that augments the household's disposable income, the second is associated with the increased technical, nutritional and health conditions in the family) and 3) constraining the discretionary power of politicians to tailor the funds for poverty alleviation according to other needs. But these programmes also have major limitations given that they: 1) fail to reach a significant group of the extreme poor who live far away from clinics or schools, 2) have insufficient funds given the magnitude of the challenge of poverty alleviation and 3) have an uncertain impact on the employment-generating capacities of their beneficiaries. Moreover when the quality of the educational services of the poor is not up to par, the merits of such programmes may be questionable.

7 For a recent, comprehensive analysis of Mexico's social policy in recent decades, see Cordera and Cabrera (2007).

8 The upward trend in social spending is also evidenced when measured in constant US dollars in absolute as well as in per capita terms (see CEPAL, 2004).

9 In addition, the main international financial organizations began increasingly to condition their financial support on the drafting of poverty reduction strategy programmes (PRSP).

10 For an in-depth critique of Oportunidades, see Boltvinik (2004).

11 SEDESOL argues that these changes are the result of: 1) a slight improvement in real incomes; 2) increased macroeconomic stability; 3) an expansion of social programmes such as Oportunidades; and 4) an increase in the value of family remittances, i.e. money orders sent home by Mexican workers in the United States. In 2006, family remittances from abroad exceeded US\$23 billion, most of it sent to rather low-income population.

12 See Uthoff (2007) for a recent comparative analysis of the evolution of poverty and inequality in Mexico within the Latin American context.

13 For an interesting and recent illustration of the evolution of inequality after trade liberalization in Mexico and in other Latin American countries see Davis *et al.* (2007).

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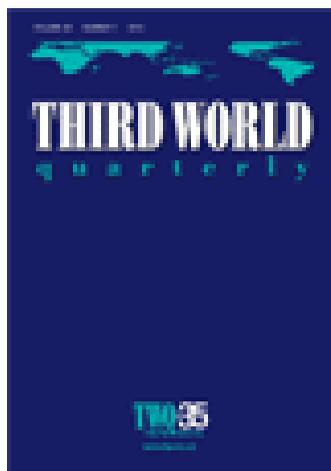
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Rising Powers in a Changing Global Order: the political economy of Turkey in the age of brics

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Rising Powers in a Changing Global Order: the political economy of Turkey in the age of BRICS

ZIYA ÖNIŞ & MUSTAFA KUTLAY

ABSTRACT The rise of BRICS presents a major challenge to the existing global order. A second category of emerging powers, which may be labelled near-BRICS, have also displayed increasing pro-activism in recent years in terms of influencing the regional balance of power politics, in addition to their growing presence in international organisations and global affairs. It is in this context that we aim to examine Turkey as a striking example of a ‘near-BRIC’ power, a country that has adopted an increasingly assertive and independent style of foreign policy with aspirations to establish itself as a major regional actor. Using the Turkish experience as a reference point, this paper aims to understand the extent to which near-BRIC countries possess the economic capacity, sustainable growth performance and soft-power capabilities needed to establish themselves as significant regional and global actors. The recent Turkish experience clearly highlights both the potential and the limits of regional power activism on the part of emerging powers from the ‘global South’.

One of the ‘great debates’ of international politics today revolves around the global shifts taking place within the inter-state system. Students of international politics have increasingly engaged in a lively discussion, sparking alternative views on the dynamics, nature and consequences of a possible transformation from a US-centred system to a multipolar global order.¹ Many scholars argue that we have already entered a post-American world,² which crystallised after the global financial crisis triggered by the bankruptcy of Lehman Brothers, one of the world’s biggest investment banks, in September 2008.³ The strikingly high post-crisis growth performance of the emerging non-Western powers, especially Brazil, Russia, India and China (BRICS) and near-BRICS countries (Mexico, South Korea, Turkey, Indonesia and Malaysia),⁴ in comparison with the weak recovery in the USA and the deepening crisis in the EU, have accelerated the ‘West vs the rest’ debate.⁵

The international system passes through an interregnum period and, as Gramsci has put it, the old order is dying but the new cannot be born. The

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current phase of transformation from unipolarity to a multipolar system is characterised by three simultaneous developments. First, the power diffusion in the international political economic system is not accompanied by a parallel process of reallocation of power. It is quite clear that the USA is no longer an example of the ‘textbook definition of hegemony’; that is, it lacks the ability to shape single-handedly the political and economic governance structures of the interstate system, as it used to. Yet the power shift from the USA has so far not been accompanied by a re-accumulation in the hands of another potential hegemonic actor. The power transition is proceeding in a diffused manner, covering a group of challengers. The second striking development, following closely the trend noted above, concerns the increasing tendency towards regionalisation in the global political economy.⁶ The globalisation wave of the past 30 years has unleashed a new wave of regionalisation, which is paving the way for the emergence of autonomous regional security orders.⁷ The third development in this context involves the rise of new regional powers and ‘catch-up states’.⁸ Accordingly the arduous reshuffling of the global order and the uncertainty stemming from the waning hegemonic check and balance mechanisms are enabling regional powers to assume more autonomy in their domestic and foreign affairs. The complex interaction of these three developments has led to a political economy structure in which regional powers enjoy greater room for manoeuvre to pursue their own regional agendas and invest in more assertive foreign policy strategies, rather than passively adapting themselves to roles otherwise attributed to them by the great powers. The rise of BRICS and near-BRICS in the regional orders and the international system is a clear illustration of this trend.

In times of global power transitions an overriding question centres on the underlying capacities of the rising powers to play increasingly ambitious regional and global roles. A related question in this context is whether such countries have the capacity to generate high rates of economic growth on a sustainable basis: to what extent is current proactivism and regional assertiveness sustainable for regional powers, especially when taking into consideration domestic political economy challenges? This article addresses these questions by assessing Turkey’s credentials to play an assertive regional leadership role, probing into its key political economy fundamentals. We believe that Turkey constitutes a critical case for studying a more general phenomenon—that is, the potential and the limits of emerging power influence in a rapidly shifting global order. We outline the possible risks and challenges pertaining to Turkey’s ability to match its rising aspirations with its actual power resources and capabilities. While we recognise the limitations of single-country case studies for the purposes of large-scale generalisations,⁹ we believe that the Turkish experience provides a strong basis for shedding light on the principal theme of this paper. Turkey is clearly an interesting country from a broader comparative perspective, especially when considering its recent economic and political transformation, its long-standing Western orientation and membership of the transatlantic security alliance, as well as its quest to play a more independent regional role in the greater Middle East, without necessarily jeopardising its traditional alliances.

The article proceeds as follows: the next section provides a brief critical overview of the dynamics of Turkey’s rising regional presence in the international

system heading towards multipolarity. The third section concentrates on the underlying political economy fundamentals of Turkey's current foreign policy proactivism and explores the risks and challenges associated with the ongoing systemic transformations. The final section attempts to generate broader insights into the debate concerning the degree and depth of influence that rising or emerging powers are likely to exercise in an era of profound global power shifts.¹⁰

Turkey: A new 'benign regional power' in the making?

Turkish politics during the past decade has been dominated by the right of centre, the Justice and Development Party (Adalet ve Kalkınma Partisi, AKP), distinguished by its moderate Islamist heritage.¹¹ Over the course of the AKP era Turkey has struggled increasingly to position itself as a 'benign regional power', especially in the Middle East, North Africa and the Balkans.¹² Turkey's current foreign policy reflects a more multidimensional and regionally oriented outlook in comparison to the strictly Western-oriented policies it pursued during the Cold War and the early phase of the post-cold war era. Turkey now considers itself an 'insider' in the Middle East and North Africa region, so much so that its Prime Minister, Recep Tayyip Erdoğan, even declared the Syrian civil war to be 'an internal affair of Turkey'.¹³ In fact, significant segments of the elites as well as the public at large in the Arab Middle East have shown a positive reception of Turkey's relatively assertive and independent foreign policy approach. According to recent research, 73% believe that 'Turkey has become more influential in Middle Eastern politics', while 66% think that 'Turkey can be a model for countries' in the region.¹⁴ However, this positive view is counterbalanced by the fact that this new foreign policy activism is also regarded in some circles, both at home and abroad, as a reflection of the revival of 'neo-Ottomanism', which contrasts with the vision of a benign regional power.¹⁵

Turkey's increasing engagement with the region has naturally attracted the attention of students of Turkish foreign policy. Not surprisingly explanations about the dynamics of rising proactivism vary significantly. One group of analysts has developed an identity-based explanation, by placing special emphasis on the ideological orientation of the moderately Islamist AKP, and has identified Sunni Islam-driven 'civilizational geopolitics' as the constituting foreign policy paradigm.¹⁶ A second group of scholars, on the other hand, has developed an alternative, interest-based explanation, which underlines the changing security dynamics of the international and regional orders. Thus, wars in Afghanistan and Iraq have triggered a power vacuum around Turkey's sphere of interest, and Turkish policy makers have responded proactively to this transformation, especially after the triumphant rise of the conservative AKP in the early 2000s.¹⁷

We argue that these explanations are not necessarily mutually exclusive. One cannot understand the AKP's active engagement in the greater Middle East without taking its moderate Islamic identity into consideration. However, simply concentrating on the civilisational dimensions of the 'new' Turkish foreign policy would miss out on the deeper domestic, regional and international political

economy dynamics at work. Hence there is a need to combine these different perspectives to provide a coherent and holistic explanation of the more assertive Turkish foreign policy over the past decade, taking into account the interplay of external dynamics and domestic transformations. Along these lines we offer an analytically eclectic perspective that combines the interactions between agents and structure, rather than relying on mono-causal explanations.¹⁸

At the systemic level the hegemonic power transformations have provided a window of opportunity for regional actors to act relatively more independently in comparison with periods when systemic control mechanisms were tight and robust. The declining power of the USA after the wars in Afghanistan and Iraq, accompanied by the rise of BRICS, has paved the way for a period of structural indeterminism, especially in the greater Middle East, so that regional actors like Turkey have had the opportunity to act in a relatively autonomous manner. A structure-oriented approach, however, is inadequate for explaining Turkey's rising regional proactivism *per se*. One has to add the agent-level dynamics into the equation so as not to overlook the details beneath the surface. In this context Ahmet Davutoğlu, Prime Minister Erdoğan's chief adviser until 2009 and subsequently Minister of Foreign Affairs, played a crucial role in formulating the current parameters of Turkish foreign policy, which in the era before the Arab upheavals involved a proactive engagement strategy by way of 'combining economic interdependence and cultural affinity with no explicit agenda for democracy promotion'.¹⁹ With the onset of the Arab Spring, however, the promotion of democracy has become a central pillar of Turkish foreign policy in the region. The current proactivism in Turkish foreign policy, therefore, increasingly relies on two pillars: economic interdependence, and explicit pro-democracy rhetoric. The Turkish government's grand strategy is to position Turkey as a soft-power driven, 'benign' regional player that promotes and utilises economic interdependence and democratisation. Davutoğlu has defined this foreign policy strategy as follows: 'In the economic realm, as an emerging economic power, we need to act as businessman ... [In the political realm] we would be the staunch supporter of human rights and democracy.'²⁰

Major reforms in the economic and democratisation spheres have constituted the basis of the AKP's soft-power driven foreign policy over the course of the past decade. In the economic realm the AKP government has built on the foundations laid during the coalition government in the aftermath of the 2001 economic crisis, whose impact on the Turkish economy had been quite devastating. The country's financial system was restructured in the wake of the crisis. Public finance was put in order and a suitable environment was created for domestic and foreign investors.²¹ Turkey during this period also benefited from a favourable global liquidity environment and managed to attract significant inflows of long-term foreign direct investment for the first time in its recent economic history. As a result, the Turkish economy and its GDP per capita grew more than threefold at current prices, in addition to a fourfold increase in Turkish foreign trade over the past decade (see Table 1). Parallel developments took place in terms of democratisation. Especially during the 'golden age' of Europeanisation (1999–2006), under the strong influence of the drive towards full membership in the EU, the AKP government accomplished major democrati-

TABLE 1. Turkey's economic performance over the past decade (2002-12)

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
GDP (US\$ billions, current prices)	232.7	304.6	393	484	529.9	655.9	742.1	617.6	735.8	772.3	794.5
GDP per capita (US\$, current prices)	3403	4393	5595	6801	7351	8984	10 745	8559	10 067	10 469	10 609
Real GDP growth (%)	6.2	5.3	9.4	8.4	6.9	4.6	0.7	-4.7	9	8.5	2.2
Investment (% of GDP)	17.1	17.4	20.7	21.4	22.6	21.8	20.2	17.2	18.9	23.8	20.6
Savings (% of GDP)	18.3	15.1	15.6	15.7	16.2	15.8	6.8	13.1	12.6	13.8	14.7
Imports (US\$ billions)	51.5	69.3	97.5	116.8	139.6	170.1	201	140.9	185.5	240.8	236.5
Exports (US\$ billions)	36.1	47.3	63.2	73.5	85.5	107.3	132	102.1	113.9	135	152.5
Current Account Balance (CAB) (% of GDP)	-0.27	-2.47	-3.67	-4.57	-6.02	-5.75	-5.25	-2.24	-6.49	-9.7	-6
FDI (US\$ billions)	1.08	1.75	2.79	8.97	19.26	19.94	16.96	6.86	7.81	16	12.6
Fiscal balance (% of GDP)	-11.5	-8.8	-5.22	-1.3	-0.61	-1.62	-1.8	-5.5	-3.6	-1.4	-2
Public debt (% of GDP)	74	67.7	59.6	52.7	46.5	40	40	46.1	42.4	39.2	36.1
Unemployment (%)	10.3	10.5	10.3	10.3	9.9	9.9	11	14	11.9	9.8	10.1

Source: Turkish Statistical Institute database, at <http://www.turkstat.gov.tr/UstMenu.do?metod=femelist>; and IMF World Economic Outlook database, at <http://www.imf.org/external/pubs/ft/weo/2013/01/weodata/index.aspx>.

sation reforms. The depth of the reform process is indicated by the fact that two constitutional and nine legislative packages were enacted.²² One of the most dramatic changes during this era involved the abandonment of the official state policy of denying the existence of Kurdish identity, which encouraged a peaceful solution to the deep-seated Kurdish problem to appear on the political horizon.²³

Turkey's economic success in the aftermath of the 2001 crisis clearly laid the foundations for a more assertive foreign policy and Ankara's rise as an increasingly influential regional power. Indeed, there appears to be a similar pattern in this realm to other members of the BRIC grouping, such as China and Brazil. During the period in question, we observe the rise of Turkey as a 'trading state',²⁴ with economic linkages gradually constituting bridges of mutual interaction with the key countries in the region. Turkey's trade volume nearly quadrupled over the past decade, and its economic relations with the neighbouring countries intensified in parallel to global economic power shifts. For example, in 2002 Asia received only 15% of Turkey's total exports, but by 2012 this ratio had grown considerably, to 35.3%. Similarly the Middle East has become a promising destination with increasing importance in terms of market diversification. Between 2002 and 2012 Turkey's exports to the region increased from just US\$3.4 billion to \$42.4 billion. On the other hand, the share of the EU in Turkey's total exports, which had been around 56% in 2002, slumped to an unprecedentedly low level of 38% in 2012.²⁵

The onset of the Arab upheavals clearly presented a major challenge to this benign scenario based primarily on the notion of mutual economic interests. Turkish foreign policy has experienced a process of adaptation in the highly uncertain environment of the Arab Spring with democratisation and concern with human rights emerging as fundamental ingredients of Turkey's approach, which targeted brutal authoritarian regimes such as the Qaddafi regime in Libya and the Al-Assad regime in Syria on the basis of a combination of economic interests and democratic concerns. Turkey was confronted with a major and inevitable dilemma, which was clearly absent in the pre-Spring era when the focus of policy was single-mindedly on mutual economic interdependence, with no visible concern for regime transformation.²⁶

In the medium term the process of political change in the Arab Middle East has created a window of opportunity for Turkey because Ankara has the potential to contribute to the process of economic and political restructuring in the region, as well as the potential to benefit from this process. One also needs to recognise, however, that the ongoing Arab revolutions have entailed costs for Turkey, in the short run notably in Syria and Libya, not only in the economic realm, but also in terms of a deterioration of relations with key neighbouring states. The Syrian crisis, in particular, constituted an important test case for Turkey's capacity to perform the role of a benign regional power. Arguably, Turkey's ability to play a constructive role in resolving the Syrian crisis has been constrained and undermined as a result of its excessive involvement in Syrian domestic politics. In retrospect the Syrian crisis also highlights the limits of emerging powers like Turkey to exert a decisive impact in terms of resolving

major regional crises, through unilateral action, in a context where global and other regional powers are heavily involved.

The political economy of Turkey's quest for regional power influence

The performance of the Turkish economy over the past decade has been rather impressive, judged by its own historical standards and the performance of the region as a whole. Having argued that soft-power-driven regional power strategy has become the central pillar for Turkey's quest to undertake a more active regional role and to present itself as a model for the wider Middle East, we probe more deeply into the underlying dynamics of Turkey's recent political economy success. A key question to consider here is whether Turkey's capabilities actually match the expectations of the AKP elites. Since Turkey's aim is to position itself as a 'benign regional power' relying on the pillars of economic penetration and democratic deepening, the robustness of these building blocks needs to be investigated in further detail. We argue that the sustainability of Turkey's economic success and democratic credentials is by no means self-evident and that there are significant political economy challenges ahead. Indeed, Turkey faces two proximate and two structural challenges in its quest for regional power influence, which tend to place the country on a kind of knife-edge equilibrium.

Turkey's economic challenges: two Achilles heels

There are two interdependent proximate challenges creating imminent fragilities for Turkish political economy, namely, chronic current account deficit and extensive energy dependence. The current account deficit reached an alarmingly high level of almost 10% of Turkey's GDP in 2011, making Turkey potentially defenceless against sudden stops of capital inflows. The root causes of Turkey's current account deficit are deep-seated. Savings rates, historically quite low, have followed a negative downward slope over the past decade, and current savings rates in Turkey (about 14%) are exceptionally low, especially in

TABLE 2. Turkey vs BRIC, basic indicators (2011)

	Brazil	China	India	Russia	Turkey
GDP (US\$ billions)	2,493	7,298	1,827	1,850	774
GDP per capita (US\$, PPP)	11,769	8,386	3,662	16,735	14,392
Total investment (% of GDP)	20.6	48.6	35	23.2	23.8
Gross national savings (% of GDP)	18.5	51.3	31.6	28.5	13.8
Value of oil imports (US\$ billions)	37.49	235.75	141.75	0	54.11
Value of oil exports (US\$billions)	5.17	25.12	56.32	277.52	6.53
Unemployment rate (%)	6	4.1	9.8	6.5	9.8
Population (millions)	194.9	1,347.3	1,206.9	142.4	74.7
Government gross debt (% of GDP)	64.9	25.8	67	11.7	39.2
Current account balance (% of GDP)	-2.1	2.7	-3.4	5.3	-9.9

Source: IMF World Economic Outlook database, at <http://www.imf.org/external/pubs/ft/weo/2013/01/weodata/index.aspx>.

comparison to BRICS (see Table 2). This ratio has been around 19% over the past decade, which is well below the average of emerging and developing markets—that is, 27.5%.²⁷

Since savings fall short of investments, Turkey needs foreign capital to finance its current account deficit. This Achilles heel places certain structural limits on Turkey's economic growth, primarily driven by inflows of foreign capital. Overdependence on foreign capital, on the other hand, increases the vulnerability of the country, because it makes the economy increasingly sensitive to external shocks,²⁸ especially at a time when serious economic recession continues to persist at the very centre of the global system. Historically informed analysis of the Turkish economy highlights quite conclusively that economic crises follow a similar sequencing: high economic growth exacerbates the current account deficit, and a sudden cessation of capital inflows for any reason triggers economic crises.²⁹ The crisis–growth–current account deficit–crisis circle still constitutes an inherent fragility of the Turkish economy, despite improvements in budgetary performance and a relatively tightly regulated banking and financial system.³⁰ The second and interrelated proximate challenge for the economy is centred on Turkey's overdependence on energy. In 2011 the country imported more than 90% of its total liquid fuel consumption, comprising an energy import bill of around \$55 billion. Moreover, according to a recent International Energy Agency report, Turkey's imports are expected to double over the next decade.³¹

High degrees of energy dependence and low savings rates, combined with low technological capacity, together constitute the major structural root causes of Turkey's chronic current account deficit. These constraints, in turn, significantly restrict Turkey's foreign policy proactivism, since they lead to a kind of asymmetric power relationship with other key actors involved in the region that could be classified as 'coercive regional powers'. For example, the asymmetric balance of power relationship, which is clearly evident in the case of Turkish–Russian and Turkish–Iranian relations, places important restrictions on Turkey in terms of developing independent strategies in key regional conflicts and exerting an even more powerful influence in the direction of democratisation and regime transformation in the region. Low technological capacity, on the other hand, curtails Turkey's soft-power credentials by raising questions about its capacity as a trading state. The composition of Turkish foreign trade sends

TABLE 3. Exports with a high technology content (% of manufactured goods)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
OECD members	24.40	23.20	21.90	20.65	20.33	20.40	20.48	16.88	16.26	17.12	16.20
Brazil	18.73	19.25	16.52	11.96	11.59	12.84	12.08	11.87	11.65	13.20	11.21
China	18.98	20.96	23.67	27.38	30.06	30.84	30.51	26.66	25.57	27.53	27.51
India	6.26	6.97	6.24	5.95	6.00	5.80	6.07	6.40	6.78	9.09	7.18
Russia	16.07	14.04	19.16	18.98	12.92	8.44	7.78	6.88	6.47	9.23	8.85
Turkey	4.83	3.87	1.79	1.93	1.90	1.47	1.85	1.89	1.62	1.74	1.93

Source: World Bank, Development Indicators database, at <http://data.worldbank.org/indicator/TX.VAL.TECH.MF.ZS>.

mixed signals in this regard. While the share of goods based on natural resources and low technology in Turkey's total exports was 63% in 2002, this ratio declined to 56% in 2010. Additionally, the share of mid-tech manufactured goods rose to 44%, a number that in 2002 was only 37%.³² However, the share of high-tech goods in Turkey's total exports declined to just over 2%, which is an exceptionally and alarmingly low ratio in comparison to BRICS and OECD averages (see Table 3).

Long-term structural challenges: the two traps argument

The proximate challenges constitute just one side of the coin. Turkey stands at the crossroads of two traps that have great potential to impede the sustainability of its regional power credentials. The first structural political economy constraint concerns the middle-income trap and the challenge of institutional transformation. The middle-income trap refers to the slow-down tendency in fast-developing countries after their per capita GDP has reached a certain threshold.³³ Research on the middle-income trap reveals that, for most of these countries, it becomes an arduous task to improve their GDP per capita from middle to high income levels. The World Bank's research estimates that, of the 101 middle-income countries in 1960, only 13 reached high-income-level status by 2008.³⁴ The overwhelming majority were unable to accomplish the jump and became stuck in the middle. As the economy moves from labour-intensive, low-cost exports toward capital-intensive production, labour is reallocated from agriculture to manufacturing sectors. This leads to the slowing down of economic growth, because productivity growth from sectoral reallocation and technology import disappears. Countries that reach middle-income level, therefore, must develop more sophisticated strategies and associated institutions to overcome this trap.

Turkey's GDP per capita, which is around \$10 500 at current prices, suggests that the Turkish political economy is indeed approaching a crossroads in terms of a possible middle-income trap.³⁵ The broad empirical evidence on this issue indicates that economic and political institutions need to be transformed into 'inclusive' institutions to promote long-term economic growth.³⁶ The institutionalist literature proposes that the most effective way to get out of the middle-income trap and to sustain long-term growth is to improve the institutional structure for education policies, the justice system and general infrastructure in an inclusive manner, so as to reap the maximum human capital potential in the country. Acemoğlu and Robinson succinctly put the issue as follows:

Inclusive economic institutions that enforce property rights, create a level playing field, and encourage investments in new technologies and skills are more conducive to economic growth than extractive economic institutions that are structured to extract resources from the many by the few and that fail to protect property rights or provide incentives for economic activity. Inclusive economic institutions are in turn supported by, and support, inclusive political institutions, that is, those that distribute political power widely

TABLE 4. Turkey's institutional development performance (2011)

	Ranking				
	Turkey	Brazil	Russia	India	China
Indicator (number of countries included)					
Corruption perception index (182)	61	73	143	95	75
Democracy index (167)	88	42	102	35	138
Competitiveness index (142)	59	53	66	56	26
Human development index (187)	92	84	66	134	101
GDP per capita (183)	64	58	55	141	91
Literacy (205)	132	126	15	177	106
GDP (210)	17	7	11	9	2

Sources: Transparency International at <http://cpi.transparency.org/cpi2011/results/>, Economist Intelligence Unit at http://www.economist.com/media/pdf/DEMOCRACY_INDEX_2007_v3.pdf, World Economic Forum at http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2010-11.pdf, UNDP at <http://hdr.undp.org/en/reports/global/hdr2011/download/>, World Bank at <http://data.worldbank.org/indicator/NY.GDP.PCAP.CD>, UNESCO at <http://www.uis.unesco.org/Literacy/Pages/default.aspx> databases.

in a pluralistic manner ... Extractive economic institutions are synergistically linked to extractive political institutions.³⁷

The long-term sustainability of Turkey's development performance is closely linked to the development of inclusive political and economic institutions. The existing institutional structures in Turkey, however, resemble those of a semi-extractive country in Acemoğlu and Robinson's terminology. Turkey is lagging far behind in the human development index, an oft-cited proxy indicator for measuring countries' development level. Turkey ranks 92nd among 187 countries; it is barely in a better position than China and India and lags behind Brazil and Russia.³⁸ The figures on competitiveness, institutional quality, corruption perception, and literacy indices also imply a similar mediocre performance (see Table 4), especially for a country that positions itself as a democratic variant of those included in BRIC or the near-BRIC category.

The discussion about institutional quality leads us to the second important structural challenge for Turkey in positioning itself as a benign regional power, namely, the transition from a 'procedural' to a 'substantive' democracy. An essential part of Turkey's regional power capacity stems from its institutionalised democracy and pluralistic socio-political order, as a secular country composed of an overwhelmingly Muslim population. Civil-military relations in Turkey have undergone a significant transformation over the course of the past decade, and the improvement in human rights standards is by no means negligible. The widespread democratisation reforms during the intense Europeanisation period between 1999 and 2006, the democratic opening that has addressed Turkey's deep-seated Kurdish question, and the constitutional reform attempts are all important indicators of democratisation.³⁹ Furthermore, the *éminence grise* of Turkish politics—the military—no longer holds absolute power in its hands to shape the political direction of the country. All these developments are clearly necessary, but not sufficient steps towards the consolidation of substantive democracy in Turkey. The central question currently revolves around the

nature and ultimate result of this power shift: how will the elected authorities use the power accumulated in their hands?

Democratisation theories point towards the establishment of robust checks and balance mechanisms as a crucial component in distributing political power and consolidating democratic governance as ‘the only game in the town’.⁴⁰ In this context, parallel to the middle-income trap argument, Turkey stands at a critical juncture as well. A central problem faced by the democratisation process in Turkey in its current stage is the very absence of adequate checks and balance mechanisms to curb an excessive concentration of power at the very centre of the political system. This Gordian knot constitutes the essence of the present debate regarding Turkish democracy, because democratisation of the civil sphere still needs to be strengthened, despite the successful transformation of civil–military relations in favour of civilian authority. The current situation puts Turkey into a grey zone,⁴¹ swinging between electoral democracy and selective democrats.⁴² Serious charges have been levelled that a narrow, majoritarian understanding of democracy has been emerging in Turkey towards the end of the AKP decade, especially when judged in terms of the virtual absence of judicial autonomy and the weak tolerance of opposition and press freedom, as well as a lack of genuine respect for political pluralism.⁴³ Indeed, the popular protests against the AKP in May and June 2013, and the use of excessive force to counter these protests, which attracted widespread international media attention, seem to reflect both the entrenchment of and growing reaction against illiberal democracy in Turkey.⁴⁴

Improvements in the quality of democratic consolidation and human rights performance are significant objectives in their own rights and should not be conceived in instrumental terms, serving only as an intermediate step in the process of achieving other objectives. This observation, however, should not detract from the fact that Turkey’s ability to establish a ‘substantive democracy’ is also essential for its ability to combine sustainable economic growth with a socially equitable pattern of development. Turkey’s ability to overcome the middle-income trap is to a certain degree based on its ability to deepen a genuinely inclusive and pluralistic democratic order. The proposition that democracy and economic development in the Turkish context are parallel and interdependent processes is clearly highlighted by the fact that the deep-seated problems of the Turkish political economy—such as an exceptionally low female labour participation rate (around 28%), which constitutes almost half of the EU average, major regional imbalances and a comparatively high degree of income inequality (with a Gini coefficient of around 0.40)—can only be effectively resolved with the help of improved democratic governance. Moreover, progress in these spheres would have direct consequences for Turkey’s foreign policy strategy, because the country needs to improve its democratic credentials and economic capacity to sustain and deepen its soft-power driven, proactive regional power ambitions.

A comparative perspective suggests that Turkey constitutes an interesting case of a near-BRICS that is trying to combine economic growth with a democratic form of government. Hence, at least in principle, it is following in the footsteps of the democratic variants within BRICS (Brazil and India),⁴⁵ rather than of its authoritarian members (China and Russia), even though Turkey continues to fall short of a consolidated liberal democracy. The important point to recognise,

however, is that the changing global context may not necessarily create a favourable environment for democratic deepening in Turkey. Furthermore, the EU, which itself is suffering a deep economic and identity crisis, has been losing its soft power over Turkey. Recent evidence indicates that, with the weakening of the formal Europeanisation process associated with EU membership, a pronounced retrogression in democratisation reforms has occurred. At a time when the EU appeared to be less attractive as a model than before, the AKP leadership has been increasingly influenced by the more authoritarian members of BRICS, given the outstanding economic performance of China, both in pre- and post-crisis contexts, and the growing strategic relationship with Russia, based on steadily expanding economic interactions over the past two decades. Indeed, Prime Minister Erdoğan has recently pronounced his desire for Turkey to abandon its long-standing EU aspirations and become a member of the Shanghai Cooperation Organization.⁴⁶ Clearly, this marks a shift in Turkey's orientation, reflecting 'conservative globalism' characterised by an eastern orientation, and an emphasis on economic and political stability with a minimalist understanding of democracy, as opposed to the Western focus of the early years of the AKP at the height of the EU-driven democratisation reforms. This shift may have fundamental implications for the quality of Turkish democracy and reduce its value as a possible model combining elements of a successful economic transformation with strong democratic credentials.

Turkey's shifting political economy landscape in the post-crisis era: elements of a neo-developmental turn

Having underlined the possible economic and political constraints on Turkey's regional power capacity, we identify certain changes that have gathered momentum in the post-global crisis era. In the post-2001 period Turkey developed a robust regulatory state compatible with the fundamental principles of the post-Washington Consensus.⁴⁷ Accordingly the Turkish financial system was placed under a strict surveillance framework via independent regulatory institutions, including the Banking Regulation and Supervision Agency.⁴⁸ The regulatory policies pursued were quite effective, considering that Turkey is one of the rare countries that did not have to bail out its domestic banks during the 2007–08 global financial crisis.⁴⁹ The regulatory shift in the financial system, however, was not complemented by a pronounced industrial transformation strategy; as a result, Turkey has continued to pursue non-selective industrial policies in line with the dicta of orthodox liberalisation.⁵⁰

During the early phase of the AKP government the emphasis was on the regulatory rather than the developmental aspect of state capacity. The transformations taking place in the post-crisis global political economic landscape, however, seem to have triggered a reshuffling in Turkish policy makers' cognitive mind-set as well. Turkey is currently trying to formulate a proactive industrial strategy, which embodies elements of a neo-developmental turn. Prime Minister Erdoğan, clearly with an implicit agenda of matching and even emulating East Asia's developmental success, openly invited Turkey's top business groups 'to produce domestic cars' at one of the meetings of the Turkish Indus-

try and Business Association (TÜSIAD). The Minister of Science, Industry and Technology similarly shared his ambition to create ‘Turkey’s own Renault, Fiat and Ford’.⁵¹ The prime minister even set an overambitious target for Turkey’s industrial transformation strategy: ‘By 2023’, declared Erdoğan, ‘we want Turkey to be one of the top ten economic areas of the world...Over the next 15 years we want to increase the per capita income from \$10 500 to \$25 000.’⁵²

Not only the rhetoric, but also the policies implemented demonstrate that there are elements of a neo-developmental turn in Turkey’s industrial policy. First, the *Turkish Industrial Strategy Document: Towards EU Membership* was adopted in 2011 under the auspices of the Ministry of Science, Industry, and Technology, along with the involvement of the relevant public and private bodies.⁵³ The long-term goal of the industrial plan is set to position Turkey as ‘the production base of Eurasia in medium- and high-tech products’. In line with this overall objective, three basic strategic targets have been determined: 1) to increase the ratio of mid- and high-tech sectors in production and exports; 2) to transition to high-value-added products in low-tech sectors; and 3) to increase the weight of companies that can continuously improve their skills. These industrial policy objectives are first and foremost designed to mitigate Turkey’s proximate and structural challenges highlighted in the previous section.

The second aspect of Turkey’s neo-developmental turn involves the implementation of investment stimulus packages. In 2012 the AKP government announced a new package to encourage investments that aims to reduce dependence on imported intermediate goods, thereby alleviating the current account deficit, improving the research and development (R&D) base of the domestic economy, and mitigating regional imbalances within the country. The stimulus package, which divides Turkey into six regions, enables each one to receive different amounts of incentives, proportionate to regional socioeconomic inequalities, including corporate tax incentives, cuts in social security premiums, free land, and access to cheap credit. According to official figures, the incentive certificates issued amounted to \$32 billion in 2012 alone, comprising the most comprehensive amount of its kind in the country’s economic history.⁵⁴ The investment stimulus package, in fact, complements already-existing R&D policies, through which AKP governments have poured considerable amounts of money into research and innovation over the past decade. Official figures indicate that R&D expenditures tripled between 2002 and 2011, jumping from \$3 to \$9.6 billion. The full-time equivalent number of R&D personnel increased from 28 964 to 92 801, and the number of researchers rose from 23 995 to 72 109.⁵⁵ The industrial strategy document and the accompanying investment stimulus package are intended to build Turkey’s R&D capacity by developing the necessary institutional framework and allocating much needed financial resources.

The third aspect of Turkey’s neo-developmental turn is related to the changing nature of state–business relations. Research suggests that state–business relations in Turkey have traditionally been overly fragmented, ideologically antagonistic and conducted *ad hoc*.⁵⁶ Therefore institutionalised cooperation mechanisms between relevant state bureaucrats and business representatives remain rather weak. A relatively isolated, rather than insulated economic

bureaucracy and a short-term-oriented, polarised relationship between economic interest groups and policy makers characterise the main dynamics of state–business relations in Turkey. Furthermore, the relationship among different private economic interest groups is generally antagonistic, because major business associations are organised along ideological lines. The recent state proactivism towards capacity-enhancing reforms hints at certain structural changes in this realm as well. First, the institutional structure of the Turkish economy is being reorganised. The Ministry of Industry has been restructured and renamed the Ministry of Science, Industry and Technology, in order to make the role of ‘science’ and ‘technology’ more explicit for Turkey’s industrial transformation strategy. Second, a separate state institution—namely, the Ministry of Development—has been created in order to coordinate Turkey’s economic development policies. Further, the industrial strategy document acknowledges the importance of the ‘embedded autonomy’ of the state,⁵⁷ by underlining state–private business cooperation, as well as the internal coherence and synchronisation of state bureaucracies:

To ensure the effectiveness of the industrial strategy, it is important to establish a high-level cooperation between the public and private sector... [Moreover] the cooperation and coordination among the public institutions is as important as the cooperation between the public and private sectors.⁵⁸

To this end, deliberation councils that incorporate different stakeholders, such as representatives of employers and employees, are being established. In addition, the relationships among private interest groups seem to be undergoing a gradual transformation. It is noteworthy in this context that the two leading business organizations—TÜSIAD, representing the pro-secular economic establishment, and the Independent Industrialists’ and Businessmen’s Association (MÜSIAD), representing the conservative Anatolian bourgeoisie—which had never before come together, met twice after 2010. Moreover, TÜSIAD has recently veered towards a more inclusive approach to Anatolian capital. At TÜSIAD’s 43rd General Assembly, Muharrem Yılmaz, known as one of the representatives of ‘Anatolian capital’, was elected the organisation’s new president, along with four other representatives of the Anatolian bourgeoisie on the board of directors.⁵⁹

These developments indicate that economic stakeholders in Turkey are aware of the ‘rise of global developmental liberalism’ in the post-crisis political economy landscape.⁶⁰ Similarly the state is investing in capacity-enhancing measures, not only in the regulatory, but also in the industrial realm. In short, these recent shifts signify a major response to deal with some of the major structural weaknesses and fragilities of the Turkish economy. It remains to be seen, however, whether the responses outlined will be sufficient to generate the kind of impact needed on the momentum of Turkey’s long-term development performance.

Conclusion: the potential and limits of ‘benign’ regional power influence

Opportunities have opened up for emerging powers to follow in the footsteps of rising powers like BRICS, as the world moves towards a new post-hegemonic

age. In this novel international environment the Turkish experience is illuminating for at least three major reasons. First, it displays how rising powers or near-BRIC countries are able to take greater advantage of the given conditions in order to pursue more proactive and assertive regional agendas in the rapidly shifting global landscape. This paper has clearly illustrated both the potential and the limits of emerging power influence, with special reference to the Turkish experience.

Second, we have drawn attention to how the rise of BRICS itself has influenced the mind-set of political elites in other emerging political economies. Political parties such as the AKP in Turkey are much more willing to pursue a proactive foreign policy, with some degree of ‘autonomy thorough diversification’,⁶¹ by keeping their traditional alliances at arm’s length. They are also willing to use active state power to strengthen their domestic political powers, a development that is openly highlighted in our discussion of the neo-developmental turn in Turkey, notably in the aftermath of the global economic crisis. Nevertheless, our analysis also pointed to a kind of expectations–credibility gap. Middle powers in the emerging global context face the risk of overestimating their leverage, especially in terms of unilateral action. The Turkish case constitutes a good illustration of this paradoxical tendency, where over-confidence on the part of the architects of foreign policy has not been matched by adequate power resources and the ability to influence actual outcomes.

The third implication of our paper concerns the future of liberal democracy. In the current global setting liberal democracy is confronted with serious challenges in its heartlands, the USA and western Europe, in the midst of a severe and continuing economic crisis. The rise of BRICS presents an uncertain future for liberal democracy, in the sense that some of the key BRIC members have deeply rooted authoritarian regimes, which are unlikely to be dismantled in the short or medium term. In this context countries such as Turkey are significant because they represent the democratic variant among BRIC or near-BRIC countries. The ability of such countries to combine economic success with liberal political values will be crucial for other countries following in their footsteps, particularly in their own neighbourhood.

Our paper has, finally, demonstrated that, while combining economic success with democratic deepening is possible, the continued existence of this combination is by no means self-evident and faces formidable challenges. From a broader perspective we should not discount the possibility that the rise of China and the economic success associated with the authoritarian version of the BRICS model may influence the mind-sets of political elites in near-BRIC countries like Turkey, with the obvious risk of side-tracking democracy in a more authoritarian direction, or at least in the direction of a persistent regime of illiberal democracy. This tendency, as this paper has argued, constitutes a major obstacle in terms of Turkey’s ability to play the role of a benign regional power on a sustained basis. Turkey’s claim to be a supporter of democracy and human rights in the Middle East is not likely to generate the desired response, especially in the presence of major democratic deficits in the realm of its own domestic politics.

Notes

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Varieties of Populism in a Changing Global Context: The Divergent Paths of Erdoğan and

Kirchnerismo

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Neoliberal globalization as an on-going process since the mid-1970s consists of distinct phases. The early years of neoliberal reforms associated with the rise of the “Washington Consensus” displayed a widespread optimism in the dominant policy and academic circles concerning the benefits of liberalization and free markets. The expectation was that the rise of the free market and the parallel retreat of the state would help to generate rapid growth, overcoming the stagnationist tendencies embodied in import-substitution regimes, the benefits of which would trickle down to wide segments of society. There was no need, according to this scenario, to be directly concerned with income inequality, given the positive effects of growth on poverty alleviation.

The early optimism associated with the Washington Consensus experienced a serious reversal during the course of the 1990s, however, due to two principal reasons. First, the frequency of the financial crises experienced in the global south pointed towards a crucial weakness of financial and capital account liberalization, often engineered without adequate safeguards in terms of building regulatory institutions. Second, neoliberal reforms have been highly inegalitarian in their impact in most national contexts.¹ These factors have produced a serious backlash in many parts of the global south, leading to a new phase of neoliberalism: the “post-Washington Consensus.” The policies of key international institutions during this new phase focused much more explicitly on the need to regulate markets and to improve the income

distributional profile through active interventionism, though within specified budgetary limits and constrained by the broad contours of the neoliberal paradigm.²

During this age of the post-Washington Consensus Latin America has been marked by a pronounced leftist-populist turn.³ The literature on Latin America has focused on different variants of this pronounced shift and has tried to classify it in terms of the softer, more market-friendly version associated with the Kirchners in Argentina or Lula in Brazil versus the more radical version often identified with Venezuela under Chávez.⁴ What is interesting, however, is that the shifts or reversals of neoliberalism are not unique to Latin America, but are also visible in other parts of the emerging world. In this context, the Turkish experience during the incumbency of R. Tayyip Erdoğan's Justice and Development Party (AKP) constitutes a striking case for comparison with the soft versions of the leftist-populist turn in Latin America.

We argue that high public discontent accompanying the difficulties and crises associated with the policies of the Washington Consensus has generated a variety of populist responses in the global south. While the literature on populism is rich on specifying the characteristics of populist movements that distinguish them from non-populist ones, much less attention has been paid to distinguishing between different types of populist movements.⁵ Our central objective is to understand and classify these populist responses and highlight elements of divergence as well convergence by focusing on the cases of Argentina and Turkey. We consider Argentina under the incumbency of Néstor Kirchner (2003–07) and Cristina Fernández de Kirchner (2007 to present) and Turkey under Erdoğan (2002 to present) as prototype examples of left-of-center and right-of-center populism, respectively. Beyond identifying divergent strands of populism in two national contexts, we also explain the mix of domestic and external factors that accounts for this contrasting pattern.

Erdoğan and the Kirchners as Populists

Following Robert R. Barr, we define populism as “a mass movement led by an outsider or maverick seeking to gain or maintain power by using anti-establishment appeals and plebiscitarian linkages.”⁶ This minimal definition of populism is particularly appealing because it eschews from conflating populism with closely related but distinct concepts such as opportunism and demagoguery and does not link it with particular economic policies, socioeconomic structure, or social constituency.⁷ Populists could target different constituencies in different contexts, for example, depending on “where the construction of the ‘us versus them’ conflict will most likely take hold.”⁸ Thus, targeting a particular constituency cannot be a core component of populism. Similarly, charismatic leadership is a valuable asset for mobilizing masses not just for populists but for any political movement. The proposed definition also refrains from associating populism with any specific organizational form while the emphasis on plebiscitarian linkages suggests an absence of autonomy within the organizational structure of the populist movement.

The definition that we adopt emphasizes three aspects of the populist phenomenon. First, populist politicians frequently employ rhetorical appeals against the power elite, referred to as anti-establishment politics. Such appeals are especially attractive for mass mobilization during times of crises and seek to convey a view of society “where ‘the people’ (commoners) are pitted against the power elite.”⁹ Second, in order for a politician’s claim of being the people’s voice against the entrenched power elite to be credible, he or she must be considered either an outsider to the political establishment (i.e., an independent politician or someone associated with a newly competitive party) or a “maverick” (i.e., a politician associated with an established party who then either abandons or thoroughly transforms it). The final defining aspect of populism is its

emphasis on plebiscitary linkages between the political actors and the citizens where the latter do not have a meaningful control over the political processes or party platforms and are frequently left with “take it or leave it” choices.

While we employ a strictly political definition of populism to distinguish populists from non-populists, we focus on economic policies in order to identify different strands of populism. Populist leaders typically rise to power following severe economic crises, and their tenure and legacy are oftentimes characterized by their economic policies, which vary substantially (e.g., Juan Perón (1946–55) and Carlos Menem (1989–99) in Argentina). We exploit this variance in economic policies, specifically along the left-right dimension that we elaborate later, as a differentiating factor between different populist movements. The benefits of such an approach have been acknowledged in the literature. Kurt Weyland, for example, highlights that an “economic definition of populism is confusing for political analysis,” and populism should be situated in “the sphere of domination, not distribution.”¹⁰ At the same time, he suggests that economic policies as instruments for gaining and exercising power might help to distinguish different populist movements. Similarly, Cristóbal R. Kaltwasser notes that a minimal definition of populism establishes a “lowest common denominator” around the core features of populism that facilitates cross-regional research and identification of its subtypes.¹¹ As an example of the importance of economic policies for delineating different populist movements, he stresses that the European right-wing populism is distinguished primarily by a neoliberal economic program.¹²

In order to designate a government or political movement as populist, then, the three aspects of the populist phenomenon highlighted by Barr —leadership by an outsider or a maverick, heavy use of anti-establishment appeals, and emphasis on plebiscitarian linkages—

must apply. From this perspective, we argue that the political movement of *kirchnerismo* embodied by the successive Kirchner governments in Argentina can be safely labeled as populist. First, even though the candidacy of Néstor Kirchner during the 2003 presidential election was endorsed by the Peronist interim President Eduardo Duhalde, as the governor of a small Patagonian province he was little known to the public.¹³ This marginal character of the Kirchner name, especially in comparison to the other well-known political figures of the day, allowed him to present himself as an outsider and resonated well with the public spirit against the political establishment following the 2001–02 crisis, incarnated in the popular slogan of “*¡Que se vayan todos!*” (“All of them must go!”).¹⁴ Moreover, during the 1990s Néstor Kirchner repeatedly clashed with and distanced himself from the leading Peronist figures by forming *Corriente Peronista*, an initiative that attracted Peronist leaders who questioned Menem’s neoliberal model.¹⁵ The ascent of Cristina Kirchner to the presidency in 2007, on the other hand, did not result from intra-party competition but was all but certain when her then highly popular husband announced that he would not seek a re-election and supported her candidacy.

Second, the ability of the Kirchners to present themselves outside of the Peronist establishment allowed them to credibly use anti-establishment appeals, which they employed extensively. Néstor Kirchner tried to establish himself as the leader of “*el pueblo argentino*” (“the Argentine people”) and articulated a discourse contrasting “the people” against “its enemies” who were embodied by, among others, *Menemismo*, the IMF, international creditors of the Argentine debt, the multinational oil corporations, and the mainstream media.¹⁶ Cristina Kirchner closely followed this discourse; during the conflict between her government and the agricultural sector in 2008 following her decision to raise export taxes, she accused the dissident farmers of “a hidden coup attempt” (“*se esconde un intento golpista*”) accompanied by some

media “generals” (“*acompañados por algunos ‘generales’ multimediatícos*”). In turn, she pleaded that she “needed the strength of the Argentine people” (“*necesito la fuerza del pueblo argentino*”) to “defend Argentina” (“*defender a la Argentina*”).¹⁷

Finally, the tenures of Néstor and Cristina Kirchner also display the third characteristic of the populist rule, namely the emphasis on plebiscitary linkages between “the people” and the ruler, as they greatly increased executive power at the expense of other institutions. Steven Levitsky and M. Victoria Murillo note that Néstor Kirchner “governed at the margins of Congress and other institutions of horizontal accountability” and encroached on judicial independence.¹⁸ As an indicator of executive power concentration, Néstor Kirchner signed a total of 270 decrees of necessity and urgency (DNU), in effect assuming powers which belong to the Congress.¹⁹ With an average of sixty DNUs per year, he remains the Argentine president who used this prerogative most frequently. Both Néstor and Cristina Kirchner rarely talked to reporters or gave press conferences during their tenures; Cristina Kirchner closed her presidential campaign of 2011 without giving a single interview and was reported not to hold Cabinet meetings anymore.²⁰ In a recent dispute regarding a new media law, she criticized the judiciary and asserted that the Supreme Court should “respect the popular will” (“*respete la voluntad popular*”), again emphasizing the supremacy of vertical accountability.²¹

The tenure of Erdoğan as the Prime Minister of three consecutive AKP governments in Turkey displays the characteristics of populist rule as well. Before his rise to power Erdoğan could credibly claim to be both an outsider to the political establishment of the time and a maverick within the political movement with which he was associated. He was outside the mainstream political community during the crises-ridden 1990s and became known to the public only after being elected as the mayor of Istanbul with 25 percent of the votes in a very tight race.

During his tenure he got a reputation for being a competent service provider, and his popularity began to cause unease among the political and bureaucratic elite.²² In 1998 he was given a ten month prison sentence and was banned from politics on the grounds of provoking public conflict by reciting a poem with militant Islamist tones. This sentence not only helped to reinforce his outsider status but also allowed him to present himself as a victim of the political establishment. Erdoğan began to distance himself from the then mainstream Islamist movement (*Milli Görüş*) in the aftermath of the 1997 military memorandum against the government and assumed a leadership position in a new political faction that culminated in the AKP.²³

The frequent use of anti-establishment appeals and a discourse contrasting “the people” against “the elite” as characteristics of populist rule is especially salient in the case of Erdoğan. He frequently refers to his humble socio-economic background and tries to depict himself as a “man of the people.” Here the contrast is with the “Republican elites” who are disconnected from popular values.²⁴ This dichotomy is articulated quite succinctly by Erdoğan himself:

My story is the story of this people. Either the people will win and come to power, or the pretentious and oppressive minority—estranged from the reality of Anatolia and looking over it with disdain—will remain in power. The authority to decide on this belongs to the people. Enough is enough, sovereignty belongs to the people!²⁵

This characterization of Turkish politics as a struggle between “the people” and “the elite” resonates well with a plebiscitary view of democracy and a concomitant disdain for institutions of horizontal accountability. In the eyes of Erdoğan, it is precisely these institutions of “the political establishment,” such as the Constitutional Court and the High Judiciary, that “formed an alliance to prevent people from achieving power.”²⁶ Accordingly, he and the AKP leadership

have embraced a strictly majoritarian understanding of democracy whereby democracy is equated with popular will, and only majorities in the ballot box epitomize “the will of the nation.”²⁷ This view permeates the discourse of Erdoğan, e.g., “the degree of one’s power solely relies on the number of votes received from the people. A minority should not overpower the majority.”²⁸ As he continues to win elections, he is facing fewer checks and balances, and analysts have increasingly begun referring to Turkey as “Erdoğan’s Turkey.”²⁹ It should also not come as a surprise that most observers point out the diminishing intra-party democracy within the AKP, where Erdoğan increasingly appears to be the sole decision-maker.³⁰

Divergence within the Populist Pattern of Rule

By employing a minimalist definition, we showed that both the Kirchner governments in Argentina and the Erdoğan governments in Turkey display the core characteristics of populism. Despite sharing a distinctly populist pattern of rule, however, a close analysis of the Kirchner and Erdoğan governments’ policies reveals that the two cases represent quite different strands of populism. Specifically, we argue that while the Kirchner governments characterize a left-wing type of populism, the Erdoğan governments’ policies suggest right-wing populism. To clarify our characterization of left-wing versus right-wing typologies, following Steven Levitsky and Kenneth M. Roberts, we designate “political actors who seek, as a *central programmatic objective*, to reduce social and economic inequalities” as left-wing.³¹ Such actors increase state expenditures, extend the coverage of social programs, put emphasis on employment, and frequently intervene in the labor market to expand workers’ benefits and rights.³² Right-wing political actors, on the other hand, do not place redistributive policies and social equality at the

top of their programmatic agenda; instead, they prioritize economic stability and physical security.

In the case of Argentina, we argue that the three features that give Kirchners' policies a left-wing populist character are (1) emphasis on a competitive real exchange rate to support domestic industry and employment, (2) support for labor, and (3) frequent and substantial state intervention in the economy through regulations, subsidies, social programs, and nationalization. It should be noted that the fundamentals of Kirchners' macroeconomic policies were put in place during the interim presidency of Eduardo Duhalde (2002–03) who rejected orthodox stabilization programs and abandoned convertibility.³³ Thus, the reform process in post-crisis Argentina was well under way, and the worst part of the crisis had already passed when Néstor Kirchner, who had campaigned on a clearly anti-neoliberal program, was elected as the president in May 2003. Still, during his and his successor Cristina Kirchner's terms, the state began to take a bigger and more active role in the economy in line with a left-wing agenda.³⁴

One of the main factors behind the rapid growth of the Argentine economy under the Kirchners was the official policy aimed at preserving a stable and competitive real exchange rate (SCRER) through controls and interventions in the foreign exchange (FX) market.³⁵ The exchange rate proved a critical tool of government policy during this period. The central bank frequently intervened in the FX market to prevent the peso from appreciating in value, and purchased nearly forty-five billion US dollars from the market during the tenure of Néstor Kirchner. Additionally, the government introduced controls on the capital account in 2005. As a result, while most emerging market currencies significantly appreciated against the US dollar until the global crisis of 2008–09, the Argentine Peso diverged from this trend (Figure 1).

[FIGURE 1 ABOUT HERE]

The SCRER policy had significant positive effects on economic activity, employment, and external and fiscal accounts.³⁶ By effectively subsidizing and thus increasing the competitiveness of the domestic industry, the SCRER encouraged the expansion of industrial production, employment, and investment. Labor-intensive sectors disproportionately benefit from such a policy because a competitive parity favors labor-intensive activities and promotes the substitution of expensive inputs in favor of labor. Moreover, while the resulting expansion of the exports and positive trade surplus eased balance of payment concerns, the accumulation of international reserves by the central bank increased local confidence in the economy. The real exchange rate depreciation was the key factor in improving the trade balance, and Argentina recorded a 7.6 billion USD surplus in 2006 compared to a 14.5 billion USD deficit in 1998.³⁷

The SCRER combined with an expansionary monetary policy that emphasized growth facilitated the government's alliance with labor—the second feature of the Kirchners' economic policies. Upon taking power in May 2003, Néstor Kirchner was already courting the support of social groups that would share his anti-neoliberal critique and he took a distinctly pro-labor stance in labor conflicts and collective bargaining.³⁸ The Kirchner governments did not quickly exercise their right to call for mandatory conciliation in labor conflicts to allow union protest and were reluctant to use force against labor demonstrations. In addition to tolerating and encouraging labor conflict, the Kirchner governments facilitated collective bargaining as well: while the annual average of finalized collective bargaining agreements stood at 176 for the period of 1991–02, it soared to 1083 during the period of 2003–11.³⁹ For the first time since the neoliberal reforms of the 1990s, the government directly intervened in wage policy by raising the

minimum wage and stipulating wage increases in the private sector. As a result, both the real average wage and real minimum wage in Argentina took off during the Kirchner governments (Figure 2).

[FIGURE 2 ABOUT HERE]

The third characteristic of the Kirchners' economic policies that suggests a left-wing type of populism is the frequent use of state interventions in the economy in the form of regulations, subsidies, social programs, and nationalization. Economic recovery of Argentina is accompanied by inflationary pressures, and the Kirchners' approach to address this problem has been the introduction of ad hoc policies such as periodic limitations on exports and negotiations with supermarkets and producers for "voluntary" price controls.⁴⁰ Additionally, the Kirchners have introduced extensive subsidies on a wide range of public services and wage goods.⁴¹ Néstor Kirchner significantly expanded the scope of the utility rate freezes and subsidy programs first implemented by Duhalde. Between 2003 and 2006 government spending on energy and fuels increased sevenfold, while transportation expenditures more than tripled. By 2010, federal spending on utilities subsidies reached 7.5 billion US dollars, around 10 percent of the budget.⁴² Finally, the Kirchner governments compensated food producers for part of their costs to control domestic prices of wage goods like beef and wheat.⁴³

The scope of the social transfers, services, and pensions were expanded significantly during the Kirchner administrations.⁴⁴ Néstor Kirchner extended pension coverage to the previously unprotected workers outside the formal labor market, and by the end of his term the pension system was virtually universal. In 2009 Cristina Kirchner expanded the existing

universal family allowances by establishing the Universal Child Subsidy and a conditional cash transfer program that covered 30 percent of the population under the age of eighteen. Upon her re-election in 2011, she announced that she would continue to deepen redistributive policies. The Kirchners also engaged in a substantial nationalization effort of state-owned enterprises that were privatized in the 1990s.⁴⁵ While Néstor Kirchner nationalized the main water utility company and the national post office, Cristina Kirchner nationalized the private pension system, the main national airline, and the nation's largest oil company. All these policies steadily and significantly increased the revenue requirements of the government: while in 2002 general government revenues constituted 23 percent of GDP, they almost doubled to 40 percent by 2012 (Figure 3).

[FIGURE 3 ABOUT HERE]

In parallel to Argentina, the year 2001 marked a critical juncture in the Turkish political economy as well. The February 2001 economic crisis resulted in one of the deepest economic recessions in Turkey's history and hit all segments of the society.⁴⁶ Perhaps ironically, it was this very depth and breadth of the crisis that ushered in a new round of structural reforms aimed at addressing some enduring institutional weaknesses of Turkish capitalism. The crisis broke the resistance of the ruling coalition government against an ambitious reform program backed by the IMF and created a pro-regulation momentum.⁴⁷ When voters punished the existing political elite by throwing all the parties in the coalition government out of the parliament and bringing Erdoğan's AKP to power in November 2002, the positive effects of the program were already palpable: the economy had grown by 6.2 percent in 2002, inflation was trending sharply downward, fiscal balances were fast improving, and interest rates were declining.

Just as Néstor Kirchner of Argentina followed the policy fundamentals of Duhalde, Erdoğan pragmatically chose to commit himself to this inherited reform drive; however, the direction of the economic policies was quite different. In contrast to the left-wing character of the Kirchners' policies, we argue that Erdoğan's policies suggest a right-wing strand of populism because of (1) the retreat of the state to a primarily regulatory function, (2) the emphasis on pro-capital policies and a general neglect of labor interests, and (3) a rather reactive and conservative macroeconomic policy-making. We should stress that by characterizing the Erdoğan governments as right-wing we do not imply that they refrained from redistributive policies completely or that the poor segments of the Turkish society did not benefit from economic growth. Rather, the AKP's approach to redistribution emphasizes private charity, informal networks, and conditional cash transfers as preferred mechanisms, and centers around "helping the poor" without a focus on systematic income redistribution — not unlike many Christian Democratic parties in Europe.⁴⁸

While the state assumed a significant role in the political economy of Argentina after the 2001 crisis, in the Turkish case we observe a retreat of the state to a regulatory role in line with the principles of "regulatory neoliberalism."⁴⁹ This move entailed taking the control of economic assets and decision making away from publicly elected bodies by forming autonomous regulatory organizations for the management of key sectors of the economy and privatizing state-owned enterprises (SOEs).⁵⁰ The economic reforms stipulated the enactment of several laws that strengthened the autonomy of the regulatory agencies in key sectors. A strong commitment to the privatization of SOEs constituted the second leg of the retreat of the state. While privatization was on Turkey's economic agenda since the mid-1980s, its pace had been extremely slow until the early 2000s.⁵¹ Erdoğan was determined to reinvigorate the privatization efforts and more than

20 billion US dollars were raised in privatization revenues from 2005 to 2007 alone, an amount that is more than double of what had been raised during the previous sixteen years. The privatized SOEs included companies in the infrastructure industries such as telecommunications, electricity distribution, highways, and ports.⁵² As a result, while in 2002 the SOEs employed close to 400 thousand people, this figure dropped to 170 thousand by 2011.⁵³

The second characteristic of Erdoğan's rule that suggests a right-wing type of populism is its emphasis on pro-capital policies and a relative neglect of labor's demands and concerns. The AKP governments dismantled administrative barriers to investment, reduced the corporate tax rate, and improved the overall legal protection of foreign investors.⁵⁴ The party's 2002 election manifesto declared that one of its aims would be to make Turkey "an international brand [for investors]," and the government boasts that it brought the number of days required to start a business down from thirty-eight to nine, well below the OECD average of twenty-five days.⁵⁵ The new foreign direct investment (FDI) regime included important incentives such as easy access to real estate, guarantees to transfer proceeds, and no minimum capital requirement.⁵⁶ As a result of these pro-capital policies, as well as a favorable economic and political environment, FDI inflows to Turkey reached a record level of 51.6 billion US dollars between 2005 and 2007, while they amounted to less than 1 billion US dollars annually before 2004.⁵⁷ Overall, the big business in Turkey, represented under the umbrella of the Turkish Industry and Business Association (TUSIAD), had been quite satisfied with Erdoğan's economic policies, especially during his first term.⁵⁸

In contrast, the AKP governments' stance towards labor interests has been much less favorable. Just six months after Erdoğan's inauguration, a new labor law (No. 4857) was adopted that was heavily criticized by the labor unions for sanctioning temporary and flexible

employment. In several cases the government remained silent on employers' disregard for workers' right to unionize, and "the postponement of legal strikes has been a telling feature of Turkish industrial relations under the [Erdoğan] government."⁵⁹ The number of strikes steadily decreased during this period; there were just nine strikes in 2011 compared to 27 when AKP took office in 2002.⁶⁰ In addition to this overall deterioration in the institutional rights of the working class, real wage increases in Turkey have been quite modest during Erdoğan's tenure, especially when compared to increases in Argentina (Figure 2).

Conservative and rather reactive macroeconomic policy-making is the third characteristic of Erdoğan's policies that point to right-wing populism. The AKP governments were committed to fiscal discipline and tight monetary policies as demanded by the IMF, especially until the 2008–09 global financial crisis. The public sector's primary surplus averaged 4.7 percent of GDP over the period of 2003–07, and, unlike in Argentina, general government revenues as a percentage of GDP remained quite stagnant (Figure 3). Even during the height of the 2008–09 crisis, the AKP government refrained from sizeable stimulus packages and other interventionist measures observed in many emerging economies.⁶¹ In contrast to the SCRER policy of the Kirchner governments, Turkish authorities allowed the Turkish Lira to appreciate by implementing an anti-inflationary policy of strong currency via high real interest rates.⁶² This appreciation in turn contributed to the increase in the share of imported inputs in industrial production from an average of 15–20 percent in the late 1990s to an average of 35–40 percent in the mid-2000s, and, while the average current account deficit stood at 0.55 percent of GDP between 1990 and 2002, it jumped to 5.2 percent of GDP for the period 2003–11.⁶³

In sum, while it is appropriate to characterize both the Kirchner and Erdoğan governments as populist, a closer look at their policies suggests that they represent different

types of populism, namely a left-wing type in the case of the Kirchners and a right-wing type in the case of Erdoğan. In Argentina, a combination of strategies, including a competitive exchange rate and frequent state interventions in the economy in the form of regulations, subsidies, social programs, and nationalization, significantly increased the redistributive capacity of the state and strengthened traditional industrial sectors. In contrast, in Turkey the monetary and fiscal policy regime of the AKP governments prioritized the interests of capital and the state retreated to a mainly regulatory function. Additionally, a politically mobilized labor movement was a key component of the Kirchners' populist coalition, while the AKP governments were characterized by a conspicuous neglect of labor's interests.

Factors behind the Divergence

What accounts for the Kirchner and Erdoğan governments' divergent paths within the populist pattern of rule? We argue that four factors are essential for understanding why the Erdoğan governments followed a right-wing strand of populism while the Kirchner governments had a strongly left-wing tone. These factors are (1) the perceptions of the causes of previous economic policies' failure that culminated in the crises of 2001–02 in both countries, (2) integration patterns into the international economy, (3) the strength of labor, and (4) regional dynamics.

In Turkey the responsibility for the policies that led to the collapse of the economy in 2001 was attributed to domestic political actors. The country had experienced a series of “boom and bust” cycles during the 1990s, when weak coalition governments pursued hot-money policies of high real interest rates to attract short-term capital in order to finance bloating government expenditures.⁶⁴ The results of these policies were “large fiscal deficits, chronically high rates of inflation, an unsustainable balance of payments situation, falling international

reserves, and the inevitable encounter with the IMF.”⁶⁵ Accordingly, the economic crises in Turkey were typically domestically generated, where the fiscal crisis of the state as a result of reckless spending by the governments played a central role. In turn, external actors such as the IMF and the World Bank frequently intervened in the economy to restore equilibrium, since the domestic actors were unable to do so.⁶⁶

The systematic collapse of 2001 was just the most severe of the busts that Turkey experienced repeatedly during the 1990s. The depth of the 2001 crisis and the perceived lack of will and capacity of the political actors to impose fiscal discipline for sustained economic growth changed the balance of power in Turkey in favor of transnational and domestic actors advocating liberalization with regulatory reforms.⁶⁷ The IMF (in addition to the EU) emerged as a powerful external anchor for fundamental fiscal and institutional reforms to achieve macroeconomic stability and a clean break with the previous era.⁶⁸ Thus, in Turkey the perception of domestic responsibility for past economic crises facilitated the Erdoğan governments’ implementation of policies that emphasized retreat of the state to a regulatory function and conservative macroeconomic policy-making.

In contrast, in Argentina the blame for the crisis was directed primarily towards the external actors who were influential in the design and implementation of the policies during the 1990s. Argentina had emerged as a “neoliberal success story” during the early 1990s, and the policies implemented during this period were designed in close collaboration with the IMF.⁶⁹ Upon assuming the presidency in 1987, Carlos Menem engaged in a series of neoliberal reforms encompassing trade and financial liberalization, a massive privatization program including social security and public utilities, and deregulation of the labor market. Additionally, he implemented a fixed exchange rate regime to combat hyperinflation and to impose a strict monetary and fiscal

policy (the Convertibility Plan). The structural reforms of this period were supported by the international financial institutions and the U.S. Treasury, and both then Minister of Economy Domingo Cavallo and Menem were “darlings of the IMF.”⁷⁰

While the neoliberal reforms were quite successful and popular in the short term, they proved to be fateful for the disastrous crisis of 2001.⁷¹ Unlike Turkey, in Argentina the perception was that the primary responsibility for the economic failure that culminated in the 2001 crisis rested with the international financial institutions that had strongly supported the neoliberal reforms. The economic crisis was accompanied by a massive wave of protests, in which the IMF was a major target along with the government. This sentiment is also shared by the IMF itself as its then First Deputy Managing Director Anne Krueger remarked that “[Argentina] faithfully applied many of the lessons that we thought we had learned from the previous crises of the mid and late 1990s—but a combination of new mistakes and some old ones brought it to grief all the same.”⁷² Thus, in the post-crisis Argentina neoliberal policies of the previous decade were discredited, and this disrepute empowered the subsequent Kirchner governments to adopt leftist policies.

The second factor that led to a divergence in policies is the countries’ distinct integration patterns into the international markets in the post-2002 global economic environment. The period from 2002 until the financial crisis of 2008–09 was characterized by exceptionally favorable conditions with record capital and trade flows, low interest rates, and strong demand for emerging market assets. Historically, Turkey’s growth episodes have almost always been financed by capital inflows, and thus the AKP government had strong incentives to pursue pro-capital policies for attracting foreign capital to finance the credit-financed, domestic demand-driven growth.⁷³ During this period Turkey offered one of the highest real interest rates among

the emerging markets, and the cumulative portfolio investment of foreigners exceeded 100 billion US dollars as of 2007 compared to just 10 billion at the beginning of 2003.⁷⁴ The widening current account deficit, which rose from 2.5 percent of GDP in 2003 to 9.9 percent of GDP in 2011, rendered the Turkish economy quite vulnerable to shifts in global market sentiments, and the AKP government pursued orthodox monetary/fiscal and pro-capital policies to ensure the continuation of capital flows.⁷⁵

In contrast to Turkey, Argentina's growth during this period was not dependent on capital flows, and this absence of external constraints was a historically rare occurrence.⁷⁶ The single most important impact of the international economy on Argentina during the Kirchner governments was the global boom in commodity prices that began around 2003.⁷⁷ As one of the world's major agricultural producers, Argentina's receipts from agricultural exports—which accounted for over half of Argentina's total merchandise exports—soared to 45 billion US dollars in 2011 from 12 billion in 2002.⁷⁸ The Kirchner governments exploited this situation judiciously by undervaluing the exchange rate to promote agricultural exports and then heavily taxing them to raise revenue.⁷⁹ As a result, taxes on exports alone accounted for 63 percent of the federal administration's primary surplus of 3.5 percent of GDP in 2006, and the primary balance of the federal administration averaged 2.6 percent of the GDP for the period 2003–08.⁸⁰ Crucially, Argentina consistently recorded current account surpluses during this period, which eased its dependence on capital flows and reduced the risks of expansionist monetary policies.⁸¹ As a result, the Kirchner governments did not need to court international capital to promote growth, and the receipts from the commodity taxes facilitated the increase in state expenditures to pursue left-wing policies.

The difference in labor movements' strength in the two countries when Erdoğan and Kirchner came to power is the third factor explaining the divergent policy paths. The Turkish labor movement is historically characterized as weak, dispersed and dominated by the state.⁸² It also lacks a political ideology equivalent to Peronism in Argentina that identifies itself with the working class. The military coup of 1980, which initiated a neoliberal restructuring program, dealt an additional blow to labor: strikes were forbidden, social rights abolished, collective agreements suspended, and many unions were disbanded (Laws 2821 and 2822). The subsequent 1982 Constitution made it harder for workers to become unionized, increased the state's political and financial influence on the unions, put a number of limitations on strikes, and prohibited the unions to participate in political activities. Accordingly, Erdoğan faced no incentives to pursue pro-labor policies and to ally himself with labor. The declining political clout of the Turkish labor movement is reflected in union membership numbers as well: while there were 2.5 million unionized workers in 1980, by 2010 that number dropped to 650 thousand.⁸³

Even though Argentina experienced a radical economic liberalization period in the 1990s, unions were able to maintain their associational power.⁸⁴ Labor unions were an important constituency of the governing Peronist Party that implemented the market reforms in the 1990s, and they were able to obtain important concessions that preserved their institutional resources. The unions prevented major changes to collective labor laws, retained monopoly of representation at the shop floor and the collective rights of centralized wage bargaining. Furthermore, sectors that boomed in this period were highly unionized. Thus, although the market reforms of the 1990s undoubtedly weakened the Argentine labor movement, the unions were able to hold on to important institutional resources that "could be called on in the immediate context of economic recovery and a friendlier government" when Néstor Kirchner

took power.⁸⁵ The strength of the labor movement motivated Kirchner governments to court their support and facilitated the implementation of left-wing policies. This strategy returned significant political dividends. When Néstor Kirchner called for a large demonstration to mark his third year in power, for example, the unions were among the main actors in the street demonstrations.⁸⁶ Similarly, during Cristina Kirchner's conflict with the agricultural sector, the unions were again on the streets to support the government.⁸⁷

Finally, we argue that regional dynamics were instrumental for the divergent policy paths as well. In Turkey, the post-crisis IMF program was legitimized and justified by convergence to the European Union (EU) policy framework. Kemal Derviş, the then Minister of Economy, had emphasized that “the economic program is prepared in full compliance with the National Program to the EU. . . . Indeed, our economic program represents the economic dimension of the National Program to the EU.”⁸⁸ Moreover, in the post-9/11 global environment, the US foreign policy was increasingly orientated towards the Middle East, and the stability of Turkey in the region was an important consideration.⁸⁹ The IMF was willing to lend several multiples of Turkey's quota at the Fund and provided favorable repayment conditions to facilitate the reform process.

The Kirchner governments' tenure, on the other hand, coincided with the rise of leftist-populist parties throughout Latin America.⁹⁰ Commodity exports during this period provided the Latin American governments with the hard currency they needed for expansionist and redistributive policies, and reduced their dependency on the international financial institutions. Karen L. Remmer reports that the odds of electing a leftist-populist president in the region was positively associated with improvements in the terms of trade, supporting the argument that decreased dependence on capital flows enabled the implementation of left-wing policies.⁹¹ The

region-wide shift towards leftist rule bestowed further legitimacy to the Kirchners' left-wing policies and it also facilitated their desire to strengthen Argentina's position vis-à-vis the international institutions through closer relations with other Latin American countries.⁹²

Conclusion

Our emphasis in the present article has been on highlighting and accounting for divergent trajectories of the populist practice in two major emerging democracies. We contend that both the Kirchner governments of Argentina and the Erdoğan governments of Turkey closely fit to the populist pattern of rule, yet their policies point to a left-wing type of populism in Argentina and a right-wing type in Turkey. A mix of domestic and external factors was crucial for this differentiation. Specifically, we stress the importance of the legacy of failed economic policies preceding the rise of populist leaders, distinct integration patterns into the global economy, the strength of labor, and regional dynamics that legitimized certain policy trajectories. While much of the literature on populism has focused on Latin American cases, we introduce a cross-regional dimension to the study of populism, a framework which could be useful for evaluating different populist patterns of rule elsewhere.

We should not assume that the left- or right-wing versions of populism depicted in the present study are necessarily stable. A major challenge to the populist equilibrium concerns the question of sustainability. In Turkey, the Erdoğan governments clearly benefited from large-scale capital inflows, especially during the favorable global liquidity environment between 2002 and 2008. The interruption of these inflows during the crisis of 2008–09, however, dealt a serious blow to the Turkish economy and to the support for the AKP government. The economy contracted by a startling rate of 14.7 percent in the first quarter of 2009, and, in the March 2009

local elections, AKP registered one of its lowest levels of support during its ten-year rule. While capital inflows resumed in the aftermath of the crisis, the continuation of this pattern of growth is not assured given the precarious condition of the global economy. Indeed, there are signs that Turkey's externally driven growth pattern is reaching its limits, and the country may be entering into a new phase of slow growth. The example of the 2009 local elections suggests that a protracted period of slow growth may present serious challenges to AKP for maintaining its broad-based electoral coalition.

A similar challenge is faced by Argentina whose populist model has also been dependent on favorable external conditions, notably on the revenues generated by commodity exports. A change in world market conditions, such as a major commodities slump, would significantly weaken the foundations of redistributing income, a key element of the Argentine left-wing populism. Cristina Kirchner has already had to significantly curb public spending by reducing utilities subsidies and discretionary transfers to provinces and municipalities.⁹³ Additionally, chronically high inflation has become a major issue—unofficial estimates put it at around 25 percent as of 2012.⁹⁴ In response, Cristina Kirchner asked unions to hold back calls for higher wages and to stage fewer strikes; yet, union leaders rejected such appeals, and, by the end of November 2012, Kirchner faced the first general strike of her term.⁹⁵ An anti-government march, the largest since Néstor Kirchner took office in 2003, took place in the most important urban centers of several provinces in September 2012, followed by an even bigger one in early November.⁹⁶ The distancing of labor and growing public discontent with government policies suggest that the sustainability of *kirchnerismo* is all but certain.

Yet another challenge concerns the democratic deficits associated with both versions of populism. The plebiscitarian view of democracy and the accompanying disdain for institutions of

horizontal accountability that is evident in the Turkish and Argentine cases do not bode well for a genuinely pluralistic, liberal democratic order. Instead, they fit Guillermo O'Donnell's model of "delegative democracy," characterized by an elected executive who considers himself as entitled to govern as he sees fit.⁹⁷ Both the Erdoğan and Kirchner governments, especially during their latest phases of rule, have been increasingly criticized for authoritarian tendencies, most notably in the realms of the freedom of the press, judicial processes, excessive concentration of power in the executive, and a lack of tolerance for the opposition.⁹⁸ These observations suggest that while the left- and right-wing versions of populism may follow quite different trajectories in terms of their substantive policies, they are confronted with similar challenges of sustainability and over-centralization of power.

NOTES

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³⁴ Upon assuming the presidency, Cristina Kirchner closely followed her husband’s policies—in fact, when elected in 2007, she kept nine of the fourteen ministers of Néstor Kirchner. This continuity in policies is so great that scholars frequently analyze the two periods together under the term *kirchnerismo*. Here we follow this tradition and focus primarily on Néstor Kirchner’s term when the policies were first implemented. To read more on this continuity, see Sebastián Etchemendy and Candelaria Garay, “Argentina: Left Populism in Comparative Perspective, 2003–2009,” in Levitsky and Roberts, eds., 283–305; “Cristina Kirchner repite el Gobierno de su marido,” *El País*, November 15, 2007.

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Approaching Islam and politics from political economy: a comparative study of Indonesia and Malaysia

Vedi R. Hadiz and Khoo Boo Teik

Abstract The article traces the trajectories of Islamic politics in Indonesia and Malaysia in relation to the changing political economy of these two countries. The approach adopted is to understand Islamic politics less on the basis of Islamic doctrine, or conflicts over its interpretation, than in connection with the changing social bases of politics, the context established by capitalist economic transformations, the evolution of the post-colonial state from the Cold War and its aftermath, and of crises of political economy in the 1980s and 1990s. The exercise reveals important convergences and divergences in trajectories that help to explain the complex historical processes which have shaped Islamic politics in these two cases and possibly beyond. It also reveals the entanglement of Islamic politics in very profane conflicts over power and tangible economic resources over time. In both countries a new form of Islamic populism has emerged as a major articulator of grievances against the secular state and perceived social injustices. However, the same historical processes have enabled the social agents of Islamic politics in Malaysia to contest state power more effectively than their counterparts in Indonesia.

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Keywords Islamic politics; Indonesia; Malaysia; capitalism; political economy; Islamization.

This article explores Islamic politics in Indonesia and Malaysia by linking their trajectories from late colonial emergence to recent upsurge to broad concerns of political economy. The Indonesian and Malaysian trajectories of Islamic politics are tracked in a comparative exercise that goes beyond the case studies to suggest that much of contemporary Islamic politics cannot be explained by reference to Islam alone, but to how Islamic identities and agendas are forged in modern and profane contestation. The main puzzle addressed here is why, in Malaysia, forces of Islamic politics now pose a serious challenge for control of state authority but not in Indonesia. The answer is not to be found in analyses that primarily focus on Islamic ideology in either country. Instead, it is better pursued by understanding the role of religious ideals in forging social coalitions engaged in contests for power and control of tangible resources.

The Indonesian and Malaysian trajectories, from their colonial beginnings, diverged at important points, with consequences for the character and role of Islamic politics. A key divergence appeared when Islamic politics in Indonesia was expressed through parties and parliaments soon after independence, amidst a tumultuous process of post-colonial state-building that included insurgencies. In contrast, the comparatively smooth establishment of the post-colonial state in Malaysia more easily incorporated Islamic politics. With subsequent capitalist transformation and integration due to processes of globalization, Islamic politics provided an ideological resource for articulating social and political discontent. Yet Indonesia's authoritarian state brutally 'demobilized' any such discontent until Soeharto's New Order was overthrown in 1998, while the state's official Islamization in Malaysia managed and constrained Islamic dissent until it was revived between two political crises of capitalism. A major outcome of the state and capitalist transformations that altered the socio-political landscapes of Indonesia and Malaysia was a new Islamic populism rooted in cross-class social bases.

I. Islamic politics: central issues

At least three reasons make it timely to examine how Islamic politics in Indonesia and Malaysia has evolved as part of deeper socio-economic and political transformations.

First, since Southeast Asia emerged as a 'second front' in the USA's so-called 'war on terror', the literature on Islamic politics, particularly in Indonesia but also in Malaysia, has been dominated by security concerns over 'Islamic radicalization' (Gunaratna 2002), the 'Talibanization' of Southeast Asia (Singh 2009) and issues of terrorism and violence. Academia, policy-making circles and the mass media are awash with discussions of purported links between Indonesian and Malaysian 'Islamic terror cells', and between Jemaah Islamiyah and Al Qaeda, that connect 'radicals'

in the two countries to Middle Eastern Wahabi money and ideology (Abuza 2003). Overshadowing this discursive development is a securitization of the study of Islamic politics by researchers who narrowly focus on such matters as pro-*Sharia* resurgence, terrorist bombings and anti-Western declamations. This preoccupation with the symptoms and not the social causes of shifts in Islamic politics hints at a hijack of the field of study. Motivating it is apprehension that organized forces of 'Islamic radicalism' – understood as an ideology and a movement that wants to establish an Islamic state hostile to 'free markets', democracy, and 'the West' – may capture state power directly by electoral means or indirectly via the radicalization of the *ummah* (Muslim community). Like Hamilton-Hart (2005) and Sidel (2007), we regard the security-oriented discourse as being littered with prognostications of the future of Islamic politics that are misleadingly alarmist, especially when Islamic dissent in Indonesia and Malaysia has overwhelmingly abided by the rules of secular state authority.

Second, there is a tendency to monitor Islamic politics by distinguishing between 'moderate' (or 'liberal') and 'radical' (or 'hard-line') Muslims. Even if this distinction serves to stress that Muslims are mostly 'moderate' (Barton 2004), it belongs with an old debate over varieties of Islam that pitted a plural peripheral 'Southeast Asian Islam' against a rigid core 'Middle Eastern Islam'. Thus Islam in Indonesia, despite the sporadic violence of Muslim militants, is held up as an exemplar of moderation, and Indonesia is hailed as a country in which Islam and democracy co-exist admirably. Likewise, despite the unrelieved conservatism of its Islamic officialdom, Malaysia is touted as proof that Muslim nations can overcome economic backwardness by engaging with global capitalism. But separating 'good Muslims' from 'bad Muslims', as Mamdani (2002) has pithily put it, is flawed and forlorn, being premised on nothing more solid than their respective acceptance or rejection of Western security concerns and global capitalism.

Third, when compelled to explain why plural forms of Islam in the broader region have been challenged by 'fundamentalist' tendencies, observers proffer elaborate accounts of a 'battle of ideas', not just between an imagined homogenous Muslim community and a simplistic Huntingtonian 'Western Civilization', but also between the aforementioned 'moderates' and 'radicals' *within* Muslim communities. This scenario, by tracing 'radicalism' to the doctrinal influences and financial resources of external sponsors of religious fundamentalism, confers a certain 'exceptionalism' on 'Southeast Asian Islam': as it were, malignant foreign influences account for the rise of abnormally radical tendencies in its midst (Abuza 2003). Such a perspective, however, offers no advance on a distinguished academic literature that relates the belief systems and socio-cultural life of Muslim communities in Indonesia and Malaysia to political mobilization and organization that did not exclude interaction with foreign doctrinal influences, and not all Islamic ones at that (Farish 2004; Geertz 1971; Kessler 1978; Roff 1967).

II. The approach

In contrast to the above tendencies, this article follows analyses of Islamic politics that address the trajectories of socio-economic change in Muslim societies which generate tensions and conflicts over the control of resources and the exercise of power. Consonant with the idea that ‘The study of Islamic communities cannot be based on a “sociology of religion” alone [but] must, rather, involve a sociology of how religion interacts with other ethnic, cultural and political forces’ (Halliday 1995: 75), several studies have explained the circumstances that made some social agents bearing Islamic commitments more influential than others at particular junctures (Abrahamian 1991, Colas 2004, Halliday 2000, Khoo 2006, Rahnema 2008). Following in this analytical path, we chart the trajectories of Islamic politics in Indonesia and Malaysia in relation to four basic factors:

- the changing social bases of Islamic politics
- capitalism and economic transformation
- the state and Islamization
- crises of political economy and a resurgence of Islamic politics.

This materialist approach allows us to show where and how the Indonesian and Malaysian trajectories, from their geneses in the colonial period, have converged or diverged, and with what consequences for Islam as an ideological resource for mobilization by state agents and their opponents. A second point of comparison is to evaluate how industrialization and structural economic transformation from the 1970s have affected the social bases and normative goals of Islamic politics. A third point is to examine the significance of state-centred religious authority for Islamic politics and the ideological identification of the state with ‘Muslim interests’.

Making such comparisons differs significantly from extant comparative studies that contrast the paths of Islamic politics in Indonesia and Malaysia. For example, in explaining competing discourses of Islamic governance in the two countries, Stark (2004) contrasts the purportedly more liberal ideas of their new middle classes with the rigid notions espoused by Wahabi-inspired activists having international links, especially with Saudi Arabia. Hamayotsu (2002) traces the tension between Islamic ideals and nationhood. In Indonesia, she suggests, nationalist leaders sought to confine Islamic politics to the periphery of the political system but failed to prevent Islamic ideas from resurging as a threat to the modern nation-state. By contrast, nation-building in Malaysia has been more successful because the state acted ‘flexibly’ and ‘pragmatically’ as the guardian of Islamic ideals (Hamayotsu 2002: 356). These surprisingly rare comparative studies of Islam and politics in Indonesia and Malaysia creditably consider how state–civil society relations, changing political alliances, and social transformation have affected the ideas of the actors of Islamic politics. But

their reliance on Islam as the key explanatory variable neglects other factors which might better 'explain how Muslims behave, or how they might/ought to behave' (Halliday 1995: 75).

Here, a summary comparative view of those 'other factors' that affected Islamic politics in Indonesia and Malaysia should clarify our approach. First, the direction of Islamic politics was conditioned by many social conflicts of post-colonial transition. There were contentions over the position of Islam and its social forces in the post-colonial state, but these coincided with the Cold War and violent anti-communist campaigns. Both the anti-communist massacre of 1965–1966 in Indonesia and the 1948–1960 'Emergency' in Malaysia had long-lasting effects, not least by limiting the ideological space open to dissent. From the 1970s, moreover, Malaysia and Indonesia rapidly industrialized, with consequent changes to class structures and the social bases of Islamic politics. A traditional Islamic populism had durably grown out of rural and urban petty-bourgeois constituencies of the late colonial period, primarily moved to halt the steady decline in their socio-economic position. Now a newer populism emerged with the social changes wrought by capitalist transformation. The latter has a variegated social base, combining the traditional and peripheralized petty bourgeoisie, working classes denied the avenues of labour and leftwing mobilization, and disgruntled sections of new urban middle classes bearing few liberal antecedents. Subjected to state surveillance and periodic suppression, the new Islamic populism overwhelmingly operates openly, through political parties, associations, and non-governmental organizations. The espousal of a range of Islamic ideals related to issues of social equity and justice, reflecting the interests of a more diverse social base, pits the new Islamic populism against the state over the directions, outcomes and quality of economic management and political administration. A rare tendency has developed out of these clashes: the resort to terror by small underground groups bent on establishing an Islamic state through violence.

Second, the state in Indonesia and Malaysia has functioned as a vehicle of development and incubator of domestic capitalist classes. Thus, economic policy has been variously shaped by statist-nationalist impulses and pro-global market interests. Economic policy was buttressed by state revenues from natural resources, including petroleum, but it was also influenced by a drive to attract foreign investment into a number of economic sectors. From the 1950s to the 1970s, state policy was inclined to protect fledgling national industries and induce the formation of a domestic bourgeoisie. Its later thrust shifted towards closer integration with global markets, especially through export-oriented industrialization (EOI) and the liberalization of banking and finance. Indonesia embarked on this shift in the 1980s, Malaysia a decade earlier. In each case, the socio-economic changes, inequalities and contentions arising out of expanded opportunities and statist, market-based or private paths of capital accumulation re-shaped the social terrain of Islamic politics.

Capitalist transformation affected the relationship between Islam and the state. In each country, Islamic identities were reshaped by the colonial legacies of a plural society and an ethnic division of labour, the latter being 'part of a class structure [that] has crystallized along ethnic lines' (Wheelwright 1965: 110). After independence, the state claimed a key role in protecting or advancing the socio-cultural position and commercial interests of indigenous ethnic communities, *pribumi* in Indonesia and *bumiputera* in Malaysia, vis-à-vis domiciled ethnic Chinese capital, and foreign capital. The state has performed that role systematically and comprehensively in Malaysia, according to its New Economic Policy (NEP), but only sporadically and haphazardly in Indonesia, for example, via the failed 'Benteng programme' of the 1950s (Robison 1986). Since demography makes 'indigenous' predominantly 'Muslim', promoting *bumiputera* or *pribumi* interests has effectively harnessed Islamic identities to state political discourse, but with one critical difference. The Indonesian state and its institutions have been staunchly secular, despite recent pressure, but the Malaysian state has become an Islamizing agent, while retaining secular institutions.

Greater integration with the global economy has stimulated new social contradictions. The rise of state-sponsored *pribumi* and *bumiputera* oligarchic fortunes – in association or rivalry with ethnic Chinese corporate wealth – has changed the tenor of public debates over social justice and especially the relative economic deprivation of the *ummah*. Since *Reformasi* in 1998–1999, Malaysia's aggrandizing advancement of politically powerful *bumiputera* interests has been much criticized for 'KKN' – *korupsi, kolusi, nepotisme* (corruption, collusion and nepotism), code for the abuse of state power to enrich privileged interests. Indonesia's *Reformasi* started a year earlier in economic collapse and led to popular unrest that helped to overthrow Soeharto. The core of the Malaysian *Reformasi* was a Malay cultural revolt against the Mahathir regime for its persecution of Anwar Ibrahim. In these circumstances, appeals for social justice made in the name of Islam – specifically its egalitarian ideals and a promise of the rule of the pious – resonate readily among poor, dispossessed, and disaffected people disconnected from other ideological alternatives. In this socio-political milieu of state development, capitalist transformation and class formation, an array of parties and organisations parlay Islam as the answer to the degradation of secular rule and democratic politics.

It may seem paradoxical to maintain a distance from Islam to explain more clearly the trajectories of Islamic politics in Indonesia and Malaysia. But this stance is valid: the conflicts that delineated the trajectories were not primarily theological ones that flowed from Islam itself. Instead, the conflicts have much in common with the socio-political trajectories of competition between coalitions of power that take place in other, 'non-Muslim', societies likewise subjected to far-reaching capitalist development (Bellin 2002). To that extent, it is unsurprising, for example, that a leading representative of Hizbut Tahrir in Indonesia should envision that under an

Islamic caliphate, the 'pious' would control key economic activities.¹ More generally, a number of Islamic-oriented political parties in Indonesia, from the 1950s to the present, have oriented their struggles to shifting control over economic resources to *pribumi* entrepreneurs. Similarly in Malaysia, strengthening *bumiputera* interests has been correlated with empowering the *ummah*.

III. Social bases, colonial legacies and post-colonial transitions

The earliest expressions of Islamic politics in Indonesia and Malaysia emerged in the early twentieth century. In this era when nascent nationalism addressed the multidimensional problems of colonial encroachment, religious identity and economic conflict were intricately linked in the first forms of organized Islamic politics.

In Dutch-ruled East Indies, the Sarekat Islam (SI) was the first major mass organization. Although it was founded by urban-based petty traders and was 'modernist' and 'purist' in its outlook, SI attracted support from rural Java, where syncretistic forms of Islam were prevalent. The SI was also supported by members of the Javanese nobility, whose social status and authority had declined. Interestingly, SI had a distinct Left wing supported by workers in urban transport, manufacturing and Dutch-run plantations. This wing broke away to become the Indonesian Communist Party (PKI) (McVey 2006), which in the 1920s housed members who identified with Islam *and* communism. Even so, SI was founded as a call to religious identity underpinned by the economic grievances of small trading and manufacturing interests. The latter was squeezed by Dutch control over key sectors of the economy and ethnic-Chinese incursions into spheres of business in the growing towns (especially of coastal Java) previously controlled by the traditional petty bourgeoisie. Even if it grew into a broader mass movement contributing to incipient nationalism in the Indies (McVey 2006: 8), the SI had intended to protect the interests of Javanese *batik* merchants from competition posed by Chinese merchants.

In Malaysia, Penang- and Singapore-based Kaum Muda reformist *ulama* were the main actors at the turn of the twentieth century. Like their modernist counterparts in Indonesia, they attacked customary and 'superstitious' accretions to orthodox Islam, and proposed 'rationalized formulations of Islamic practice which would better enable them and their coreligionists to compete in the modern world' (Roff 1967: 78). As urban Muslims who reformulated 'Islam in response to the economic and social pressures of contemporary life' (Roff 1967: 79), they criticized the Malay traditional aristocracy that had become dependent on British rule and stripped of real powers except in religious affairs. British rule had created 'the concentration of doctrinal and administrative religious authority in the hands of a hierarchy of officials directly dependent on the sultans for their position and power' (Roff 1967: 72). For the Kaum Muda, the key issues were the

loss of Malay political power, the decline of the Malay economy vis-à-vis colonial capitalism and an ethnic division of labour that rested on an influx of immigrants from China and India.

The Kaum Muda's modernizing tendency pitted its reformism in 'direct conflict with the state religious authorities on a wide range of ritual, doctrinal, and social questions' (Roff 1967: 78), while its purifying tendency alienated it from the Malay peasantry. As such, it could not gain influence with the elite; nor did it secure the mass base that SI enjoyed before coming under intense colonial repression. Even as the SI was superseded in the independence struggle by communists and secular nationalists (led most prominently by Soekarno), it evolved into a political party of the traditional petty bourgeoisie. The SI's role in the 'national awakening' encouraged other Islamic organizations and political parties to claim simultaneous allegiances to the *ummah* and to the nation. The Kaum Muda, however, left no such organizational legacy. Still, representing the Islamic variant of the 'hesitant beginnings of Malay nationalism', a 'modernist Muslim reaction against the native rulers' self-serving control of religion under the British' (Kessler 1978: 23–24), it outlined a template for the Islamic politics of the Hizbul Muslimin, Kesatuan Melayu Muda and PAS (Mohamed Nawab 2007: 11).

The paths of Islamic politics in Indonesia and Malaysia exhibited greater divergences by the mid-twentieth century. Islamic politics in Indonesia came to be expressed through parties and parliaments but also insurgency, while in Malaysia it was structurally incorporated into the evolving post-colonial state. The colonial-era precedent of centralizing authority over religion certainly facilitated this development in Malaysia. Here too the victory of the colonial state over the Malayan Communist Party – always portrayed as a 'Chinese' party – allowed state authority to be effortlessly transferred to a coalition (Alliance) headed by a nobility-led political party (United Malays National Organisation, UMNO) that was self-consciously Malay and Muslim. Such a situation, suited to Britain's needs, was conducive to America's as well while the Cold War raged.

However, Indonesia's 1945–1949 war of independence ensured that the development of the post-colonial state would be a highly contested process within which different representatives of Islamic politics were involved. At one extreme, Islamic politics was marked by the rise of the Darul Islam rebellion. Ostensibly launched to establish an Islamic state, the insurrection initially owed to the disaffection of independence fighters led by the legendary Kartosuwiryo – a former senior official of the Party of the Sarekat Islam Indonesia – over the ceding of West Java to the Dutch during negotiations to end the war. Whether the West Java-based Darul Islam rebellion was ideologically ill-defined (Van Bruinessen 2002), or whether Islam importantly influenced it (McVey 1981), it was conclusively defeated by the Indonesian armed forces in 1962. Loosely affiliated movements in Aceh and South Sulawesi fared no better. With the rebels cast as traitors to the nation, their political heirs were never absorbed into the body politic.

Instead, they continued a tradition of struggles outside state parameters to advance the social position of the *ummah* – often by underground proselytizing activities, sometimes uncovered as those of ‘terror cells’, including lately, as part of the loose Jemaah Islamiyah network (International Crisis Group 2005).

But the mainstream of Islamic politics in Indonesia was represented by the ‘modernist’ party Masyumi and the ‘traditionalist’ and ‘syncretic’ Nahdlatul Ulama. In the 1950s, Islamic parties sought to advance *pribumi* economic interests and, in vain, to enshrine Islam as the ideological basis of the state. Importantly, some Masyumi members were implicated in ‘half-hearted’ separatist rebellions (Harvey 1977) supported by the USA because of its hostility to the left-leaning Soekarno (Kahin and Kahin 1995). Those rebellions expressed the grievances of commodity exporters in the ‘outer islands’ who were undermined by the taxation and inflationary economic policies of the central state. In response, Soekarno banned Masyumi in 1960, but its political and ideological descendants continued to articulate the interests of an eclipsed old petty bourgeoisie based in small trade and manufacturing. They straddled formal (and informal) accommodation and haphazard resistance to secular state authority, especially during Soeharto’s New Order. Many ex-Masyumi members were encountered in groups that included Darul Islam–ists. By the 1980s and 1990s, though, their ideas found support among the new urban poor and middle class, whose aspirations had grown because of access to modern education. The ideologically more pliant Nahdlatul Ulama drew on the support of the patronage networks of rural elites and Islamic clerics, mainly in Java, and managed to establish a secure position through co-operation with the Soekarno and the New Order regimes from the 1960s.

In Malaysia, a critical point came with the formation of Persatuan Islam Se-Malaya (Pan-Malayan Islamic Organization, or PMIP) from UMNO’s breakaway religious wing. The PMIP embraced former members of the Malay Nationalist Party (MNP) and Hizbul Muslimin, the first ‘Islamic party’ in Malaysia, which roughly represented the radical strands of Malay nationalism (Kessler 1978: 172). The party’s nucleus was ‘a number of ulama, imams and conservative nationalists from both within and without UMNO’ (Farish 2004: 72–73). PMIP’s social base included the rural elite, religious teachers, the peasantry, and the lower ranks of the urban middle class. Its cadres were also found among graduates and teachers of the Malay educational stream who objected to educational policies that favoured English-medium schools (Kessler 1978: 170–71). Moreover, PMIP gained support among the peasantry and smallholders because UMNO elites’ new wealth and land acquisition aggravated local ‘peasant anxieties’ (Kessler 1978: 121, 125). In the first post-independence general election of 1959, PMIP won control of two states (Kelantan and Terengganu) out of eleven and gained respectable representation in parliament. Over the next decade, UMNO established itself as the party of the nobility, salaried

officials, and party functionaries that had inherited state power from the British. But as PMIP consolidated its rule in Kelantan, its leaders became distinctly of 'urban, petty bourgeois origins', whose vernacular or Islamic education had disqualified them from the regime's high ranks that, retaining colonial, English-oriented, elitist features, were the preserve of an UMNO-linked 'politico-administrative bourgeoisie' (Kessler 1978: 170–71). Later renamed Parti Islam (PAS, or Islamic Party), PMIP became UMNO's sole serious challenger for Malay-Muslim support.

IV. Capitalism and economic transformation

The social transformations engendered by capitalist development shaped the evolution of Islamic politics in Malaysia in Indonesia, notably by re-making the constituencies potentially available to it. At independence, the peasantries of both countries were locked into subsistence agriculture or unprofitable smallholder cash-cropping. *Pribumi* or *bumiputera* businesses were typically small and unable to penetrate the large-scale primary commodity sector and the import-export trade dominated by European capital. At the level of retail, urban services, and small-scale industry, *pribumi* or *bumiputera* businesses lost out to Chinese-owned businesses. To the extent that the post-colonial economy in both societies was dualist – having a traditional, rural, agricultural sector and a modern, urban, service sector – the former was largely occupied by *pribumi* or *bumiputera* while the latter was not. Particularly in Malaysia, an ethnic division of labour and structure of wealth distribution was erected upon this dualism, creating a society more amenable to ethnic rather than class interpretations of socio-economic inequalities (Puthuchearry 1960). Kessler (1978) showed how a land-deprived and insecure Malay peasantry supported the PMIP in expressions of class interests and frustrations; yet neither pressed towards open class antagonism. The Malay peasantry tellingly played no part in the communist insurrection. Although the division of labour in the Dutch East Indies likewise marginalized the *pribumi*, it did not pre-empt class expressions of politics. In the 1960s, the PKI-led peasant actions ostensibly directed against their better-off neighbours (Lyon 1970) and dominated the labour movement (Hadiz 1997).

However, the class struggle collapsed with the PKI's destruction in the massacres of 1965–1966, conducted by the army with the aid of many Islamic organizations, notably those related to NU, whose elites were distressed by the communist agenda of land expropriation. Subsequently, the army-led corps of state officials that took power built an authoritarian corporatist political structure based on ideas of the cultural authenticity of communitarian, organicist, and state-defined social harmony (Bourchier 1996). Where the forces of political Islam were invited to join in, they did so as mere junior partners. Meanwhile the small but economically significant

Chinese minority became more vital. Its big-business component increasingly developed cronyistic and rapacious alliances with New Order officials. But the Chinese as a community served as a convenient target against which popular anger over social inequalities could be re-directed. In the absence of class struggles, it became habitual to pit Islamic-inspired notions of social justice against the politically vulnerable Chinese community. This tactic of rule exploited old animosities that petty-bourgeois Muslim traders felt against Chinese businesses considered to have been privileged by the Dutch (Sidel 2006).

There was a different dynamic in Malaysia, where the state was virtually Malay-Muslim by being UMNO-dominated. State officials had neither interest in nor need of an 'Islamic state'. But they reserved certain religious initiatives and projects for Muslims because the Malays were their principal electoral constituency. More importantly, they needed to maintain a stable apex of power-sharing between a Malay-led state apparatus, domiciled non-Malay capital and foreign capital. As the guardians of Malay-Muslim interests, they also had to address rural poverty and the commercial demands of the urban petty bourgeoisie. This task was undertaken after the ethnic violence of 13 May 1969 by launching the NEP,² a massive social-engineering project to dismantle the ethnic division of labour. The NEP's *dirigiste* directions were capitalist, albeit moved by impulses of ethnic anxieties, social democracy and economic nationalism.³ A crucial development was the push towards export-oriented industrialization (EOI), which pulled young Malay labour from rural areas into factories in urbanized export-processing zones. Landless Malay peasants were relocated to state-organized land resettlements in a kind of land reform without the expropriation of landowners. Moreover, a massive expansion of public education drew young Malays into schools and tertiary institutions. Most graduates were absorbed by an expanding bureaucracy and state enterprise sector. The state created untold business opportunities for the Bumiputera Commercial and Industrial Community, the official term for a state-sponsored class of mostly Malay capitalists and professionals. Thus were created a large Malay industrial proletariat and a large Malay urban middle class.

What was the effect of these social changes on Islamic politics? As the spatial distribution of the Malay population was altered, PAS's chiefly rural-agricultural base was modified, even diminished. Ideologically and programmatically, PAS had no purchase on Malay nationalism, not with UMNO driving the NEP – reducing Malay poverty, providing educational, training and business opportunities to the Malays, and stringently regulating non-Malay (including some foreign) businesses. Nor did it help PAS that UMNO redefined the parameters of interethnic relations to privilege Malay culture, language and politics. And when it came to religion, the state safeguarded the pre-eminence of Islam vis-à-vis other religions by expanding and deepening its 'official' Islam.

Indonesia's economic transformation took a more complicated route. The New Order broke with Soekarno's anti-imperialist and Third Worldist stances and introduced major policies to re-connect the economy with the West through infusions of foreign capital and investment. More change followed when the oil price increases of 1973–1974 provided the state with windfall revenues. Now the state began to act as an engine of growth, protecting import substituting industries (ISI) and providing largesse that aided giant, largely ethnic Chinese-owned but state-connected businesses (Robison 1986). This phase of state-directed development lasted a decade, before declining oil prices compelled Indonesia to conform to the dictates of the emerging neoliberal global economy by implementing EOI based on low-wage manufacturing.

The Indonesian social landscape, too, was greatly changed as rapid economic growth gave rise to a new urban middle class, a broader working class, including a *lumpenproletariat* sprawled over cities and towns. A stronger Chinese bourgeoisie also emerged, as did wealthy families of officialdom. Old petty bourgeois animosities redirected at the former later merged with new hostility towards the latter. Thus, the potential grew for political Islam to widen its social base by incorporating those who became disaffected by the gap between rising aspirations, engendered by the experience of modernity, and the limits to social mobility dictated by access to resources and power. By the 1980s, mosques had become centres of new communal ties in urban slums (Raillon 1994).

In Malaysia, the Malay community's experiences of far-reaching social change – urbanization, land resettlement, proletarianization, education, and *embourgeoisement* – created social tensions that opened new opportunities for Islamic politics. Yet PAS failed to develop a programme to compete for the support of a transformed Malay community. This was evident, for example, in PAS's attitude towards the growing, young, Malay proletariat (which had a sizeable female component) engendered by the EOI of the 1970s. The sole surviving party of the Left, Parti Sosialis Rakyat Malaysia (PSRM, or Malaysian People's Socialist Party) tried to organize this new Malay Muslim working class based in the new industrial zones, but PAS seemed oblivious to their existence. In fact, PAS hardly had a role in the initial religious resurgence of the 1970s, which was associated with organizations of the new Malay urban middle class, such as the graduate-led, part-*dakwah*, part-activist and part-welfare-oriented Angkatan Belia Islam Malaysia (ABIM, or Malaysian Islamic Youth Movement). ABIM was influential among urban Malay youth and on university campuses, where the Malay student population was rapidly rising. Another movement, Darul Arqam, infused with 'Sufi-millenarian ideals' (Ahmad Fauzi 2009), attracted graduates of university-level Islamic studies programmes, professionals and even civil servants to efforts at building an 'Islamic society' grounded in economically self-supporting settlements (Nagata 1984: 104–06).⁴

An analogous growth of religious consciousness took place among the Indonesian urban middle class of students, engineers, bureaucrats, clerks, lawyers and doctors who – like their Malaysian counterparts – were just one or two generations removed from rural origins and came to make sense of modernity and globalization in increasingly Islamic terms. More ambitious and materially comfortable as the world opened up for them, they resented the New Order's rapacity, cronyism and blatant abuse of power that conceivably limited their prospects. But whereas repression could dispense with political liberalism, it could not eliminate Islam culturally and ideologically. In fact, new social agents of Islamic politics, especially those nurtured in universities as higher education expanded, grew in confidence when Soeharto tried to accommodate them through the Association of Indonesian Muslim Intellectuals (ICMI). Formed in 1990, ICMI became a conduit to bureaucratic authority and political largesse (Hefner 1993) and the site of political socialization of a generation of activists that would form a host of post-New Order Islamic parties.⁵

The above developments occurred in the context of sustained economic growth. In Malaysia, revenue from oil and other commodities streamed in with the EOI and the NEP, defraying state expenditure in the economic and social sectors. Thus, manufacturing transformed the economy while social engineering restructured society. Their combined outcome, rapid growth with meaningful redistribution, undermined PAS's challenge. Moreover, the state protected international capital by prohibiting the industrial working class from unionizing, but mitigated the latter's overall conditions with social policies and welfare measures which, disproportionately benefiting the Malays, strengthened their allegiance. In Indonesia, by contrast, while living standards generally improved before the 1997 financial crisis, there were few welfare-like policies. The Soeharto government was frequently criticized for presiding over an unjust social order, being perceived to favour a select group of capitalists with strong state connections through non-transparent policies, including preferential access to state credit and private monopolies. But the New Order's policies of demobilizing civil society prevented effective anti-regime challenges from emerging until 1998.

An impetus for ICMI's establishment derived from the growing criticism of the New Order in its first two decades, made by Muslim groups, especially those informally linked to old Masyumi and Darul Islam networks. Such criticism had been previously suppressed. In the 1970s, competing Islamic political parties had been forced to merge into the PPP (United Development Party), whose name was bereft of anything remotely Islamic and which was mostly docile.⁶ A decade later, the state simply imposed its ideology of Pancasila⁷ regardless that some Muslims derided it as a secular concoction (Prawiranegara 1983). Further, shadowy groups which the government claimed were pursuing the dream of an Islamic state were brutally crushed when they momentarily surfaced (Van Bruinessen 2002). Tensions between the New Order and political Islam exploded one night in

September 1984, in the working class enclave of Tanjung Priok, North Jakarta. Demonstrators, led by businessman and former Muslim student activist Amir Biki, had emerged from a mosque where sermons were allegedly infused with anti-government agitation. Reportedly, hundreds of the demonstrators, including Biki, were shot dead by security forces (Bourchier and Hadiz 2003: 140). In this environment, many Indonesian Islamic activists were compelled to go incognito. In response to strict control over student organizations, Muslim groups on university campuses organized religious activities that led to political discussion and cadre formation. From such activities the so-called Tarbiyah (educational) movement emerged, which was important in the development of the PKS (Justice and Prosperity Party), the most successful of the post-New Order Islamic parties (Rahmat 2008).

V. The state and Islamization

The Malaysian and Indonesian cases diverged most significantly on the matter of the state and Islamization.

In many Muslim countries, such as Egypt and Algeria, the failure of economic development fuelled the rise of ideologies and movements seeking socio-political solutions based on Islamic ideals. This was not the case in Malaysia, where state-directed economic transformation enabled the successful absorption of rural, mostly Malay-Muslim, migrants within the urban industrial sector (Lubeck 1998: 313). Indeed, the Malaysian state did much more to hold back Islamic challenges. State policies in the 1980s had shifted the decisive arenas of Malay politics – from the countryside to the cities, from culture and language to economy and wealth, from peasant agriculture to the corporate sector, and from subsistence and small business to the commanding heights of the economy. The power of state enterprises, an emerging class of Malay capitalists, and UMNO's senior leadership had eclipsed the influence of Malay-medium schoolteachers, 'men of letters', civil servants, and low-level religious functionaries. Under Mahathir, Malaysia Inc. and privatization benefitted coalitions of political influence and financial power that won lucrative state contracts and projects. Money and power met and merged, and politics and business fused in UMNO, the 'party of the Malays'. The state managed an ethno-corporatist distribution of material benefits. Malay society was awash with state aid – contracts, shares and subsidies for new Malay capitalists; resources and funds for state enterprise managers; scholarships, shares, and support for professionals; and agricultural, infrastructural and other subsidies for the rural population. And, for all Muslims, there were the public construction of houses of worship, provision of religious classes, sponsorship of events, and assistance for the performance of religious duties, including the *hajj*. It seemed then that PAS could not mount a credible 'Islamic alternative'. Nor did it appear that Malay society could be mobilized along lines of

class antagonism, even when its elite captured social policy, intra-ethnic inequalities widened, and the lifestyles of Malay rich and poor diverged irreconcilably.

Ironically, the state itself advanced the course of Islamization. While the state had always striven to shape 'Muslim consent', bolster regime legitimacy, and control Islamic dissent, it also possessed the power and resources to drive its own agenda of Islamization. Moreover, there were historical precedents: official Islamization in Malaysia, *as a process*, originated in colonial rule. British rule, by depriving the Malay rulers and traditional elites of power in all areas save 'Malay religion and customs', concentrated doctrinal and administrative religious authority in the hands of officials dependent on the sultans (Roff 1967: 72). For two decades, the post-colonial ruling elite maintained a decidedly secular and constitutional – if politically illiberal – regime. Their chief agenda was developmental, but political concerns left room for discrete, small-scale and symbolic Islamic projects. These bound Malay allegiance to the state and affirmed an ideological role for Islam in the state's commitment to the anti-communist side of the Cold War.

From the mid-1970s, the state had to contend with an Islamic resurgence, manifest in the ABIM and Darul Arqam's popularity, that later drew inspiration from the 1979 revolution in Iran. With PAS turning more doctrinaire as well, the state was compelled to respond to this spreading, dissenting Islamic resurgence. As it did so, from the 1980s, the state extended the boundaries of Islamic law. A critical moment came when the Mahathir regime took Islamization beyond political response by harnessing Islam to its nationalist-capitalist project. Thus, Islamization came to entail the establishment of Islamic institutions such as Bank Islam, International Islamic University and an Islamic insurance company. An exhortation to 'absorb Islamic values' made its way into official documents and served an ideological function with dual class emphases. 'Islamic values' were to imbue the emerging Malay capitalist and professional classes with an inoffensive equivalent of a 'Protestant ethic', and to impose upon the Malay working classes a strong work discipline required for late industrialization (Khoo 1995).

The state seemed able to steer the course of Islamization, retain secular government, restrain encroachment on the rights of the non-Muslims in the populace, and limit the disapproval of foreign investors. But Islamization reproduced a growing class of religious bureaucrats and professionals whose interests lay in de-secularizing public institutions and regulating social life (Ahmad Fauzi 2009: 7) beyond the ambit of Mahathir's own 'instrumentalist' preferences. Thus, it was never simply that Islamic theology fused state and religion. For long periods, they had been separate enough in public affairs and the personal lives of Muslims. But the state having *infiltrated* religion (Hischkind 1997: 13), religion *rebounded* by percolating through the state.

Nothing of the sort occurred in Indonesia. Dutch colonialism never had the effect of concentrating religious authority on the state (Hefner 2001: 24) so that Indonesian Islam could develop diversity and avert codification. The traditional nobilities, especially the Javanese, continued to represent cultural traditions far more syncretistic than Islamic. Their loss of political power was not compensated for by increased religious authority. Hence, colonial experience provided no precedent to facilitate the incorporation of Islamic politics into the post-colonial state. Although Islam was a major pillar of Indonesia's nascent nationalism, as evident from the SI's legacy, it had to compete with many forms of secular populism. While Islamic groups failed to privilege Islam in the national constitution (Nasution 1992), Islam was superseded by Soekarno's nationalist populism. Besides, the PKI developed a radical populism that threatened the material interests of the key rural and urban petty-bourgeois constituencies of Islamic politics. In response, political Islam turned to the military and supported the bloody campaign against the communists in the 1960s.

However, the military soon curbed its erstwhile Muslim allies for a clear reason: Islamic forces with strong grassroots would undermine the New Order's founding logic to undertake capitalist development based on the political demobilization of society. Not Islam, then, but a state corporatist version of Pancasila was exalted – and this, despite the embrace of Islam by numerous peasants during the late 1960s to escape being branded 'communist-atheists', and the creation of a limited social space for Islamic activists through the expansion of Islamic traditional schools (Sidel 2006: 51, 53). What Islamic political life there was, embodied in the PPP, atrophied within a state corporatist and rigidly controlled party system (Robison and Hadiz 2004).

The arrival of ICMI under the aegis of Vice President B. J. Habibie had rekindled false hopes for creeping Islamization within state institutions. But Habibie was defeated in the first post-Soeharto elections in 1999 and ICMI became irrelevant. Henceforth, Islamic political parties had to contend with a host of others that kept alive the secular nationalism that Soekarno and Soeharto had nurtured in different ways, but within a new democratic environment. In 1999 the ambitious PK (Justice Party) could not muster the threshold two percent of the total vote. Reconstituted as the PKS, the party did much better in 2004 and 2009, winning between seven and eight percent. In the interim, however, it had distanced itself from *Sharia* promotion and emphasized issues of integrity and good governance (Rahmat 2008).

VI. Crises of political economy and the resurgence of political Islam

A final divergence between the Indonesian and Malaysian trajectories may be located in crises of political economy that created opportunities for Islamic politics, though these have not always been seized.

In Malaysia, Mahathir successfully used Islam to legitimize the Malaysian capitalist-nationalist project. In 1986, PAS was reduced to one seat in Parliament, defeated in all other contests against UMNO. Still, the contradictions of NEP-based capitalism wrought their consequences. The Islamization of politics advanced at two moments when the Mahathir regime came close to imploding because of economic recessions that compelled the state to reconstitute Malaysian capitalism. Until the late Soeharto period, by contrast, Indonesia saw a much less systematic attempt to use Islam to legitimize economic development since thorough political demobilization made it unlikely that economic crisis would threaten the New Order. Yet, the crisis of 1997–1998 brought down the entire edifice of political institutions. As with the end of the Soekarno years, a post-Soeharto environment emerged that promised – but did not deliver – opportunities for the representatives of Islamic politics to scale the commanding heights of state and economy.

In Malaysia, recession in 1985 had led Mahathir to liberalize investment, discipline the state sector, and suspend redistribution objectives in favour of growth (Khoo 1995). A political crisis of Malay capitalism resulted when an alliance of smaller Malay business interests, civil servants, and state managers opposed these policies (Khoo 1992). The challenge to Mahathir, narrowly defeated in UMNO's April 1987 election, split the party. Not until 1996 would the breakaway faction rejoin UMNO. Later, the 1997 financial crisis found Mahathir confronting the global financial market, choosing currency and capital controls over further liberalization and deregulation, while his deputy, Anwar Ibrahim, favoured pro-market reforms (Khoo 2003). When Anwar was dismissed from government and imprisoned, popular outrage spawned the *Reformasi* movement. The politics of the two crises of capitalism convulsed the Malay community, loosened UMNO's hold over it, and discredited institutions of state power. At this juncture of weakened state legitimacy a more thorough Islamization of politics truly began.

These crises helped to revive PAS's electoral fortunes. Split in 1976, PAS had quit the BN, lost Kelantan to the Federal government, and was defeated in the 1978 elections. In turmoil, the party turned to the *ulama* – partly trained in foreign centres of Islamic learning – who recast the party's ideology and programme. They Arabised their political idiom and upheld the universalism of Islam by denouncing UMNO's politics of ethno-nationalism. They insisted that an *ulama*-led system of government would have to replace 'secularism' with rule by Islamic law. It may not be redundant, thus, to say of PAS that it had Islamized itself. All the same, as PAS threw its 'Islamic state' gauntlet at UMNO, it did so over economic, social and political matters as much as moral and religious ones.

Between the two crises, PAS mounted an Islamic populist opposition based on an estrangement of a middle-class component from the state,

demands of moral economy, and a model of pious living (Khoo 2006: 147–52). During the 1980s, PAS's Islamist re-orientation won over many Malay students, graduates and urban activists engaged in *dakwah*, seeking solace from the effects of rapid capitalist development. PAS also opposed the corruption linked to the state's non-transparent privatization of 'mega projects' to cronies. By personal example, the top PAS leaders enjoined pious living, pitting morality against the *maksiat* (vices) of the Malay elite. In 1990, PAS returned to power in Kelantan, and nine years later, regained control of Terengganu and became the leading opposition party in Parliament (Khoo 2003). Today PAS is the best-organized component of a three-party coalition that credibly challenges UMNO/BN dominance. PAS was able to project the political crises of capitalism in the 1980s and the 1990s as shocking symptoms of a model of Malay modernization turned moral malaise.

Indonesia, too, suffered a crisis of political economy – in the 1980s, when the fall of oil prices robbed the state of its most important financial base, and again in the Asian Crisis of the following decade – but Islamists were unable to fully capitalize. No doubt, in an otherwise highly orchestrated general election in 1982 (Suryadinata 2002), the PPP did benefit from growing disenchantment with an increasingly corrupt state, which led to a partial backlash against the state's electoral vehicle, Golkar. But the PPP, mainstream Islamic organizations and critical groups on the fringes of social and political life were largely mute on the issue of economic crisis itself; they contributed little to debates on alternative policies. Yet this crisis led to selective 'deregulation' of the economy, mainly in trade and finance, and the promotion of EOI, which signalled a new phase of incorporation into globalization processes. These policies would give politically-connected businesses access to new international sources of finance; in time, their borrowings caused private-sector debt to spiral out of control, and consequently, the Indonesian economy fared the worst when the Asian Crisis struck (Robison and Rosser 2000).

When Soeharto could not steer Indonesia through its gravest economic crisis, Muhammadiyah leader (and ex-ICMI figure) Amien Rais became the public face of *Reformasi*, and KAMMI, a student organization linked to the Tarbiyah, took a leading role in anti-regime protests. Afterwards, however, Islamic political actors did little to distance themselves from the rapacity of New Order elites who prolonged their political lives by reinventing themselves as democrats (Robison and Hadiz 2004). Forming new parties in the newly democratic environment, Islamists became immersed in elite-level wheeling and dealing, punctuated by regular elections and coalition-building that had more to do with disbursing the spoils of power than with governance. Even the PKS – idolized by sections of the upwardly-mobile urban middle class – has been implicated in allegations of corruption. The post-1998 resurgence of Islamic politics in Indonesia, unlike in Malaysia, has occurred without a clear party of the pious.

If the PKS's modest electoral successes can be taken as an indicator of this resurgence, others come from *Sharia*-inspired local government ordinances that regulate such matters as women's dress, but fail to address matters like corruption. The resurgence has been manifest too in paramilitary organizations that claim to protect the *ummah* from vice but are manned by a multitude of street thugs (Van Bruinessen 2002). Among these organizations are the FPI (Islamic Defenders' Front), the FBR (Betawi Brotherhood Front) in Jakarta, and the Korps Hisbullah of Central Java, all known for conducting raids on nightspots. Such organizations draw recruits from the sprawling *lumpenproletariat* of Indonesia's crowded and tough urban centres, where unemployment and underemployment remain rampant long after the Asian Crisis. There is also the Majelis Mujahidin Indonesia, a front organization for a range of groupings, including those that bore the brunt of state repression in the 1980s. Yet, all this is also indicative of the failure of political Islam in Indonesia to mount a serious challenge for dominance over the higher reaches of state power and the economy: none can compare with the stature and credibility of PAS in Malaysian politics.

VII. Conclusion

This essay made historically informed connections between Islamic politics and political economy to explain how trajectories of the former have reached quite different positions in Indonesia and Malaysia. The result is a complex picture that defies easy assumptions about how political Islam has developed in either country, or may develop in any other.

Early political Islam in Indonesia had strong organization and substantial aims. Yet, overshadowed by state secularism and demobilized by brutal authoritarianism, no Islamic force emerged as a credible challenger for state power, even when a crisis of capitalism resulted in a dramatic widening of the parameters of political contestation. The beginnings of political Islam in Malaysia were marked by weaker organization and milder political tones. Yet, its principal bearer, PAS, although disadvantaged vis-à-vis a 'Malay-Muslim state' that launched socio-economic reform and imposed official Islamization, surged by seizing chances created at two moments of the ruling party's near-implosion. These divergences in trajectories may be traced to processes of state and capitalist transformation that reshaped the social bases of political contestation. Only when such processes and factors – external to Islam as religion – are taken into account does the rise of Islamic politics that combines populist mobilization with religious idioms and goals become comprehensible.

To explain political Islam in these Southeast Asian countries in such terms is not fundamentally different from treating political Islam elsewhere. As in Egypt, Tunisia, Algeria, Iran, or Pakistan, the political appeal of Islam and the power of Islamic populism cannot be separated from issues of post-colonial state transformation, pathways of capitalist development, and

the destruction of ideological alternatives. The contexts are comparable, even if historical peculiarities and local specificities add to the complexities of particular situations, as in Southern Philippines or Southern Thailand today. There, one must add the unresolved problems of severe regional inequalities, antagonistic state–Muslim minority relations, and subordinate social identities to see how ‘jihadism’ is such a terrible misnomer for political struggles rooted in unfulfilled socio-political aspirations.

Where new forms of Islamic populism threaten ‘secularism’, in Indonesia, Malaysia or elsewhere, it is not the foreignness of the idea of secular government or its ‘alleged unintelligibility to the “Islamic masses”’ that matters, but typically a regime’s economic mismanagement, social failures and political implosions (Azmy Bishara 1995). Nothing in this reasoning vulgarizes Islamic politics as an epiphenomenon of economics: it is accepted that the devout and pious may view social problems in religious terms and seek religious solutions to them. But, precisely because Islam, ‘like all great religions, [has] a reserve of values, symbols and ideas from which it is possible to derive a contemporary politics and social code’ (Halliday 2000: 133), Islamic politics cannot be divorced from the contemporary and secular needs of those who articulate variants of that politics. To do so is to commit the common error of representing Islamic politics as a phenomenon that flows, as it were, from Islam itself. Here, hostile portrayal would depict Islamic politics as a defective outgrowth of a flawed religion. Conversely, idealized rendering would praise Islamic politics as an activity enjoined by a perfect one. Avoiding those two sides of the same coin, it is necessary to see, as Armstrong (2000: 133) has succinctly expressed it, that the special character of Islamic resurgence lies in its political exertion, not so much its doctrinal reassertion.

Notes

- 1 Interview with Abdullah Fanani, Hiszbut Tahrir Indonesia, Jakarta, 26 January 2009.
- 2 At the general election of 10 May, the ruling Alliance coalition suffered considerable defeats. Amidst heightened pre-election ethnic tensions, groups of Malays attacked Chinese in Kuala Lumpur, sparking Malaysia’s most serious incidence of ethnic violence. The regime later gave poverty and Malay economic disaffection as the causes of ‘May 13’.
- 3 Tun Abdul Razak, the NEP’s architect, was proud to call state intervention a form of ‘nationalist socialism’ (Khoo 2003: 196).
- 4 Darul Arqam was suppressed for being ‘deviationist’ in 1994. Some of its leaders were detained without trial.
- 5 ICMI primarily incorporated the Muslim intelligentsia and members of the new urban Muslim middle class.
- 6 However, PPP parliamentarians did challenge a 1970s marriage bill thought to contravene Islamic precepts.
- 7 Pancasila consists of belief in God, humanism, national unity, deliberative democracy, and social justice.

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