Chapter 14

Turkish Corporate Governance Regime: Antecedents and Outcomes

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ABSTRACT

This chapter focuses on the characteristics of Turkish corporate governance regime with an emphasis on the dominant characteristics of emerging economies. In Turkey, corporate governance practices were introduced as a precondition of the International Monetary Fund (IMF) rescue package in and around the 2001 financial crisis. Governance practices were enforced by World Bank (WB) and were supported by the TUSİAD (Turkish Industry and Business Association). While OECD-based governance principles were drafted by the Capital Market Board (CMB) their implementation has gone through modifications that are characterized by the institutional environment, the culture and legal system in which they were embedded and accordingly, today corporate governance practices, especially the board structuring and transparency routines reflect this local milieu.

INTRODUCTION

The liberalization of markets since 1970 began to affect Turkey by the mid-1980s. The emergence of corporate governance issues and problems are in a way punctuated with the neo-liberal policies and deregulation followed by then. Furthermore, the Asian crises in the late 1990s facilitated a milieu where corporate governance issues were given a prime importance and reconsideration. Thus, the last decade witnessed a remarkable increase in governance practices both in developed and emerging markets. Corporate governance reforms which included legal and structural adjustments have been the major focus of international and local organizations. Although there is a divergence among corporate governance regimes at the national level, a widespread agreement on the fundamental governance issues like ownership rights, transparency, risk, and accountability prevails.

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Prior to the 1980s, the Turkish economy was characterized with insufficient private capital, and heavy import substitution policies that prevented competition and inadequate financial markets which altogether contributed to insufficient corporate governance practices. However, these economic imbalances were accommodated by the 2001 financial crisis which was characterized by a 10 percent decrease in Gross National Product (GNP), bankruptcies, and takeovers by state. Failure in both the public and private sectors, especially in banking, was considered to be the result of mismanagement practices and corruption. Consequently, good governance practices were recommended as a precondition to the stand-by agreement to be signed with International Monetary Fund (IMF) (Erturk, 2003) and with the support of the Turkish Businessmen and Industrialists Association (TUSIAD) a code of corporate governance in line with OECD (Organisation for Economic Co-operation and Development) governance principles as prepared by the Capital Market Boards (CMB).

Although the 2001 financial crisis, one of the most severe in history, had adverse effects on the macroeconomic indicators, the proposed reforms led to the creation of an optimistic economic environment which was helpful in attracting foreign investors which, in turn, encouraged the acceptance and implementation of “good governance” practices. The code which has a self-regulating tone and is based on “comply or explain” principles was soon gained support from a wide range of economic and political actors; state agencies, international organizations like the World Bank (WB), voluntary associations such as the Turkish Corporate Governance Association (TKYD), international rating agencies, consulting firms, universities and listed companies all supported the corporate governance reform. In 2007, the Corporate Governance Index started to be calculated by Borsa Istanbul (formerly the Istanbul Stock Exchange) and with this initiative listed firms are rated according to their corporate governance performance.

The Turkish governance regime which can be described as an “insider model” without any strict regulations that enforce their implementation (Okutan-Nilsson, 2007) has been widely influenced in practice by the Turkish institutional context, legal system, and management culture and thus diverges from other governance regimes that implement a similar model. The purpose of this chapter is to provide a deeper understanding for the emergence of this regime by focusing on its antecedents and then analyze the outcomes which dominate the practices of companies in Turkey. Accordingly, the chapter is organized as follows: In the first section, the institutional environment (the dominant actors and formal/informal arrangements), the legal system and the management culture that shape corporate governance regime in Turkey will be explained. In the second section, outcomes of this specific governance regime in terms of board structure, risk management, and transparency will be discussed with reference to the existing research in the field. The last section includes a discussion on the current state of governance practices in Turkey.

BACKGROUND: AN OLD PROBLEM, A NEW SOLUTION

The core idea behind corporate governance practices is mainly related to the alignment of interests between managers (agents) and owners (principles) in corporations. The issue was stated by Alfred Marshal in the early 1920s: