

SIMILAR HISTORIES, DIFFERENT OUTCOMES: COMPARATIVE ANALYSIS OF THE ROOTS OF THE INSTITUTIONAL TRANSFORMATION IN IRAN AND TURKEY

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Abstract:

This study is a comparative analysis of the roots of institutional evolution and its power-relational and distributional dynamics in Turkey and Iran that, by 1980, led to approval of openness and economic integration in one country and a totally different economic transformation which resulted in a rather isolation from the world economic order in the other.

Iran and Turkey had many similar features regarding their ‘politoeconomic’ structures and encountered many similar events which affected their institutional organisations (both political and economic) on the eve of the new world economic reformation of the nineteenth century. What is attention-grabbing, that today these two states though had a similar history in many respects, are on totally different points in terms of political structure and accordingly of economic policies practiced. Similarities in historical developments are apparent, but emergence of different institutional outcomes is difficult to elucidate.

The subject matter of the study is how these developments can be analysed on the grounds of the institutional economics framework. Among the approaches in the Institutional Economics framework to the formation of diverse economic institutions across countries, *the Utilitarian Perspective*, *the Structuralist Stance*, *the Beliefs and Ideologies Approach* and *the Political Institutionalism* are found inadequate in providing completely the necessary tools for a comprehensive analysis of the current cases. Thus, the current work, taking into consideration of the merits of the aforementioned approaches, proposes a new framework which can be called as the *Clash of Paths*.

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Similar Histories, Different Outcomes: Comparative Analysis of the Roots of the Institutional Transformation in Iran and Turkey

1 Introduction

The political and economic developments such as significant increases in production and output due to technological improvements occurred in the West during the last four centuries, all resulted in a new social, political, and economic transformation in these countries. Such a revolutionary change, in turn, had profound effects on non-western less developed countries of the time. Technology was the predominant factor in shaping institutions, both political and economic. This is because, configuration of social and institutional structures went hand in hand with technological evolution¹, however always accompanied by conflicts arising from change in distribution of resources.

Turkey and Iran, in this respect, got their shares. Although they did not become colonized, both states were left far behind the advances of the West, subject to their first defeats to developed countries' technologically superior armies and consequently turned their faces towards the West in order to adopt the reforms that had taken place there. More interestingly, both countries changed their political systems from monarchy to constitutionalism in exactly the same period; Iran's Mesrutah of 1906 and Turkey's Mesrutiyet of 1908. However, today these two states though had a similar history in many respects, are on totally different points in terms of political structure and accordingly of economic policies practiced.

Historically, Turkey and Iran, as stated by Issawi (1981), originated two of the major ancient civilisations; greatly contributed to the formation of Islamic society and culture; had roughly same size of population and degree of development and per capita incomes equal; were integrated in the world economy at much the same time; and experienced the stagnation and decline that characterised the Middle East in the modern period. In addition, they had many similar features regarding their politoconomic structures and experienced many strictly similar events in terms of their economic and institutional organisations on the eve of the new world economic reformation. However, the outcomes of these reorganisations were different in many times in the twentieth century. Thus it appears that there must be some important dynamics that provided the basis for implementation of economic liberalization policies of 1980 in one country and a completely different economic transformation in the other.

One possible account suggested for the divergent paths is the differences in religion and sect in these countries. Indeed, the role of ideology in determining diverse institutional structurings among different countries is underlined in the institutional economics literature (i.e. North, 1990; Kuran, 2008). Ideological differences, particularly

¹ Here we do not assume that technology is exogenous. Rather it is tried to stress upon the fundamental effects of technological change during the era of Industrial Revolution on technologically backward countries' institutional evolution. These countries, for example, felt the first impact on territorial issues when they were defeated by countries with technologically more advanced armies.

the different sects of Shiism and Sunni Islam, seem to play a role in different institutional settings also in Turkey and Iran. However, limiting the causes of completely different transformation experiences of these countries to belief differences would not provide us with complete explanation of institutional divergence.

Resource endowments, in the current case *oil*, appears to play an important role particularly on formation of attitudes, or say shaping *mental models*, towards global economic integration in Iran during the 1970s, when oil windfalls were at an unprecedented levels. Yet, this does not mean that oil is the sole reason underlying the totally different institutional outcomes that Iran and Turkey experienced in 1979 and 1980 respectively. This is because, institutional structures, their moulding effect on individual actors and the interaction of both the former and the latter are shaped and reshaped in a long period of time. Besides in the case of Iran this development was partly independent from its oil endowments. Moreover, historiography agrees that the modern rentier state of Iran has established in 1963, that is significant revenue-based differences in the two countries' resource endowments in fact root in as late as 1960s.

When the issue is related to institutional features, dealing with the sources of the problem rather than with the current symptoms is more effective. In view of that, for an appropriate evaluation of radically different social, political and economic transformation of Iran and Turkey, there seems to be a need for exploration of the roots of diverse structuring of both political and economic institutions across the two countries, about which the Institutional Economics literature provides the means to reach some insights. In this context, for the specific cases at hand the analysis will be made on the grounds of complex web of power relations among different groups with economic interests as well as between the state and those groups. However, then the question of 'where does power originates from?' has to be thoroughly addressed.

Accordingly, the core question that the current analysis will deploy around is:

What were the roots of institutional evolution and its power-relational, class-relational and distributional dynamics during the course of capital accumulation in Turkey and Iran that, by 1980, led to approval of openness and economic integration in one country and a totally different economic transformation that resulted in a relative isolation from the world economic order in the other?

This is somewhat a comprehensive question, and requires not only an analysis of the economic structures of the two countries, but also consideration of their social formation. Political economy of institutions, in particular, has to be taken into consideration in order to reach the origins of power balances both within different classes and between those classes and the state.

Such a question has not yet been asked. Apart from Charles Issawi (1981)'s comparative work on Iran, Turkey and Egypt's economic performances for the period of 1800-1970, the literature is rich in country-specific studies on social and economic

history rather than comparative studies. The current study, on the other hand, aims to dig deep in order to find the roots of the two divergent transformations in a comparative manner. There are a few other comparative analyses on the two countries but none of them tries to answer such a question. Their standpoint is either differences in religion and sect in the two countries (e.g. Akyol, 2006) or modernization movements during the reigns of Ataturk and Riza Shah (e.g. Atabaki and Zurcher, 2004 and Atabaki, 2007).

The reason why such a question has not been asked so far is possibly that, Iran experienced a proper revolution whereas in Turkey, though the second half of the 1970s witnessed many upheavals, there was no such event. It is also likely that a kind of perception has been formed among many that comparing a rentier and Islamic country and a non-rentier laic country is not the best meaningful option. Such a view, however, clearly neglects the pre-1980 structures and developments that will be explored in this paper. That is to say, the major institutional developments of the nineteenth century in particular should be carefully elucidated because, many of the structural changes in the twentieth century in fact had their origins in the transformations of the nineteenth century and the interactions between domestic structures and external forces occurred in this era.

In short, this study aims to provide an analysis of the diverse formation of economic institutions in Turkey and Iran on the eve of 1980s. It is generally assumed in the paper that institutions are not typically chosen for the general benefit of the society as a whole, but rather imposed by groups with political power for their economic consequences. For that reason, understanding institutions, in turn, requires understanding the dynamics of political power balances. However, apparently political power balances specific to every different country do not develop from scratch: Rather “exogenous variations” such as historical events, seem to play important roles during the process of creation of alternative institutional pathways, whereas the belief structures, in North’s definition ‘mental models’ determine which alternative pathway will be selected or suppressed. In view of that, the origins of the power balances will be demonstrated in light of the new approach proposed: *The Clash of Paths*. Consequently, since the distribution of power (economic or political) is determined by pre-existing political institutions and corresponding distribution of resources, the evaluation of their roots will provide important insights on the totally divergent institutional restructurings of the 1980s in these countries.

Accordingly, in the following section a theoretical framework on institutional economics and political economy of institutions is drawn. In the third section, different approaches towards institutional change and persistence and the extent of their explanatory power will be elucidated. In the fourth section, a new dimension to institutional formation and reformation, namely the *clash of paths*, will be proposed and elaborated. The fifth section deals with the roots of institutional formation in Turkey and Iran in terms of the founding factors of the institutional paths of the two countries. In the sixth section, important critical junctures at which choices among alternatives were made that determined the course and the direction of institutional evolution will be analysed in terms of complex web of power balances. The seventh section applies the proposed theoretical outline to the case countries and demonstrates how initial political power

balances stemming from early political institutions though affect the establishment, change and persistence of the subsequent economic institutions, it is not a deterministic effect due to clash with other national paths and inter/trans –national developments in a continuously changing environment. Finally, the last section concludes.

2 Theoretical Framework: Institutional Economics and Political Economy of Institutions

As economic actors, every step we take and every decision we make, are affected by institutions and the institutional environment that we are in. The structure of society which is composed of various forms of institutions and other hegemonic thought and attitudes limit and even shape our decisions and behaviours. Institutions affect the economic life through a variety of channels such as various forms of political systems and economic organizations, diverse attitudes towards different modes of production and exchange, nature of the entrepreneur class, and a variety of consumption habits, that is indeed societies' general outlook for life.

The importance of institutions as one of the main determinants of the pace and the structure of economic growth, which originates back to Polanyi (1957) and Commons (1936) and more systematically to North (1973, 1981 and 1990), has now become a generally certified premise in the economics literature. North and Thomas (1973), for instance, state that factors such as innovation, education or capital accumulation are not causes of growth but they are the very embodiment of growth. In North and Thomas's view, the fundamental explanation of comparative growth is differences in institutional structures.

In this context, institutional change or persistence is key to understanding historical change, whether in social, political or economic arrangements. As North (1990 p.118) points out, institutions “*connect the past with the present and the future so that history is a largely incremental story of institutional evolution in which the historical performance of economies can only be understood as a part of a sequential story.*” Starting from this precise point, then, a major task in analysing the different socio-economic transformation experiences of Iran and Turkey appears to be a profound study of institutions and institutional change. The theoretical framework provided by institutional economics, in this respect, outlines a theory of institutional conservation, innovation and change with an emphasis upon the mutual interaction and interlinkage between institutions and individuals thus the importance of belief structures (Veblen, 1899; Commons, 1934; Hodgson, 1994b; Hodgson 2000, North, 1990; North, 1994; Adams, 1994).

The political economy of institutions in which the notion of power is given a particular importance in shaping and reorganizing institutional structures, are also firmly stressed in the institutional economics literature (North, 1981; North, 1994; Olson, 1982; Morris and Adelman, 1989; Robinson, 1998, Acemoglu, Johnson and Robinson, 2004). Almost all studies searching for the roots of diverse institutional structuring among different countries, give particular importance to the concept of power in shaping and

reorganizing institutional structures, and bring up the very existence of social conflict on political and economic rents with a special reference to dissimilar power structures and power balances within societies.

In North (1981) for instance, North focuses on the development of property rights, which he explains in terms of the economic interests of rulers. However, the rulers' need to take account of powerful interest groups and the existence of transactions costs typically result in inefficient property rights.

Olson (1982) also puts a particular emphasis on the concept of power and the very existence of social conflict and dissent underneath the outcomes derived from economic practices and relations. According to him, the rise of impersonal rules and contracts means the rise of the state and with it unequal distribution of power. This provides, in turn, opportunity for powerful groups to formulate the rules to their advantage, with little or no account on their efficiency implications. That is, rules will be devised and implemented along with the interests of the politically powerful factions of the society, but they will not necessarily have a lowering effect on total transaction costs and thus may well be socially detrimental.

Furthermore, Morris and Adelman (1989), in their aforementioned review of comparative quantitative study of the nineteenth century development, found that the market institutions, which were the determinants of the speed of growth, differed depending on whose assets were increased, who held political power, whose political power and property rights were strengthened, and in what manner factor mobility was promoted.

Nonetheless as a beginning, let us first start with the main meta-theories put forward in the institutional economics literature in order to provide well-grounded answers to the central question of 'why do institutions differ across countries?' Analysing the extent of their explanatory power will offer some insights on the evolution of the institutional paths of the two case countries, Iran and Turkey.

3 Why do Institutions Differ across Countries? Different Approaches to Institutional Change and Persistence and their Explanatory Power

Why do economic institutions in different countries not follow a common pattern which proved to be more growth- and distribution-enhancing? There are different approaches in the Institutional Economics framework to the formation of diverse economic institutions across countries. They range between the efficiency considerations from a utilitarian point of view and path dependency arguments from a structuralist stance and can be classified² as:

² Acemoglu, Johnson and Robinson (2004) classify these approaches as 1) Efficient Institutions View 2) Ideology View 3) Incidental Institutions View and 4) The Social Conflict View which the authors themselves propose

- Utilitarian Perspective
- Sociological Institutionalism (Ideologies and Beliefs View)
- The Structuralist Stance and Path Dependency
- and Political Institutionalism

In the following four sections, we analyse these four core frameworks on the causes of institutional diversity and search if they are appropriate to be employed as the analytical framework to explain the *roots* of diverse institutional structuring in Turkey and Iran.

3.1 Efficiency Considerations are Inherent in Institutional Formation: The Utilitarian Perspective

The Efficient Institutions View maintains that growth- and efficiency-enhancing policies are more likely to triumph over the efficiency- and growth-retarding ones since societies, though may be not in the very short-run, choose the economic institutions that are socially efficient. The efficient economic institutions view, in a variety of forms, has been proposed in different analytical approaches. North and Thomas (1973), in which the general framework is an efficiency explanation, argued that feudal economic institutions, through which the lords provided a public good and protection whereas the serfs provided their labouring in exchange, were the most efficient ones available given the lack of a modern fiscal system. The concept of timing then appears to be important in such forms of evaluation of institutional efficiency. Liebowitz and Margolis (1995), for example, stress that the selected institutions may be proved to be inefficient ex-post, but this does not mean that they were inefficient at the very exact point of time when they were established. The authors further state that if one of two options is superior in the long run but not in the short run, then market arrangements will generally assure the adoption of the superior path. This point of view is to a large extent related to Liebowitz and Margolis' private actor-centric way of analysis, that is individual economic actors, who calculate in the shadow of the future, have the ability to capture the returns from long term investments, and this is what prevents them from making bad choices.

Similar to Liebowitz and Margolis (1995), Becker (1983) in his analysis of competition among pressure groups for redistribution and the resulting economic policies and institutions, puts forward that policies that raise efficiency are likely to win out in the competition for influence because they create gains and individuals and groups who benefit from these gains will put pressure for their maintenance.

Efficiency arguments reserved a significant area particularly in theoretical and empirical works on *property rights*. Indeed, the underlying reasoning behind the Efficient Institutions View comes from the well known Coase (1960) theorem, in which Coase identified the importance of transaction costs in determining the conditions that would lead to efficient outcomes. Demsetz (1967), following Coase (1960), argued that creation of property rights is related to an economic motivation rather than having any political dimension. The motive for internalization of externalities, in effect, provided one of the

most significant bases for formation of property rights. That is, property rights emerged to maximize efficiency. Such an analysis which explains the formation of property rights in terms of efficiency then leads to one important question about the contemporary world: How are we then going to explain the absence of some specific institutional, political and policing structures which are required for lower transaction costs but are often missing in many developing countries?

The subject matter of a possible answer to above question should be about the central role of distributional concerns in emergence of different institutional structures among countries. That is, Coase's framework for looking at efficiency is distributionally blind, in that it says that economic efficiency can be achieved through different allocations of rights and liabilities which can each be efficient despite having very different implications for the distribution of net social welfare. Yet, historically, private property rights emerged through processes which involved distributive conflicts and state intervention as well as calculations of superior efficiency. That is, behind the evolution of any structure of property rights is likely to be an underlying power distribution and this background of social power is important if we try to explain why some institutions do not sometimes emerge at all or emerge at very high cost (Khan, 2003).

The emergence of different property right systems through processes of conflict and struggle is indeed one of the essential characteristics of Karl Marx's analysis. Marx explicitly argues that whatever the subsequent efficiency or otherwise of a property right system, in practice it is often political factors, such as class struggles over distributive shares, which bring about changes in property rights that may have little to do with a consideration of the social costs and benefits of the system as a whole (Macpherson, 1978). This is hardly surprising since those who stand to lose from system change are hardly likely to be comforted by the fact that society in aggregate will be better off. The view was also supported by Douglass North in his later works. North (1994, p.360-61) explicitly states that:

Institutions are not necessarily or even usually created to be socially efficient; rather they, or at least the formal rules, are created to serve the interests of those with the bargaining power to create new rules. In a world of zero transaction costs, bargaining strength does not affect the efficiency of outcomes; but in a world of positive transaction costs it does.

Thus, the profound point that must be once again highlighted is that efficiency-based approach to the formation of various types of institutional structures is a limited, if not misleading, one. This issue is particularly important when we consider the vast literature in institutional economics that is concerned with the persistence of *inefficient* institutions in many countries. Why do then many societies end up with some certain economic institutions that are not in their best interest? The answer to this question should not be a magic. As long as certain economic institutions lead some part of the society to be better off, then efficiency considerations cannot be separated from distributional conflicts. Furthermore, given that political power is crucial in overcoming distributional conflicts, then inefficient institutions may well be created and preserved if they happen to benefit some politically powerful groups.

Having discussed the limitations of the Coase Theorem, let us now return to the other abovementioned efficiency-based arguments and analyse them in more depth. Becker (1983), for instance, himself also states that in the analysis governments correct market failures, that is greater efficiency, with the view that they favour the politically powerful. However, he simply assumes away the cases where the governments deliberately create market failures in order to favour the politically powerful.

Liebowitz and Margolis (1995)'s argument as well, though has a considerable merit, first does not fully take the possibility of free-riding and apparently cannot measure the strength of the pre-described mechanisms in overcoming this problem. More importantly, institutional evolution cannot be comprehended in Liebowitz – Margolis-type explanation, in which institutions are efficiently constructed in accordance with the needs of the specific period considered. This is because the environment described in Liebowitz-Margolis, such as the presence of market mechanisms that lead to more efficient outcomes, is not the cause of institutional progress but as North and Thomas (1973) stressed, it is the very product of institutional environment.

From a different critical approach, Acemoglu (2003) argues that an extension of Coasian reasoning to the political sphere implies that there exists a strong tendency towards efficient policies and institutional structures parallel to varying needs and requirements of societies, generated via political and economic transactions, though, irrespective of who or which social group has political power. However, Acemoglu asserts that Coasian-type compensation does not exist in the real world, due to the prevalence of *contract enforcement problems*. That is, contract enforcement requires a third party, typically the state, which possesses the monopoly of legitimate coercion in society. Yet, when the state is one of the contractors, this type of outside enforcement becomes impossible. Similarly when social groups with high political influence and power of pressure on state policies are one of the contracting parties, say alongside the rest of the society, then these contracts will also be non-enforceable because politically influential groups “cannot commit to not using their power to renege on their promises or to not changing the terms of the contract.” Thus, contrary to the arguments proposed by the Efficient Institutions View, all above underscored limitations and Acemoglu (2003)'s critical assignments of Coasian-type reasoning, highlight one of the main arguments of this thesis that *efficiency* and *distribution* are inexorably inseparable. Because, economic might is usually associated with political power and hence initial distribution of income and subsequent allocation of political power have a strong potential to create an inherent commitment problem that undermines the likelihood of reaching efficient outcomes.

Since the concept of commitment is related to political power or influence, but political power in turn is partly associated with economic might, then growth- and distribution- enhancing institutional arrangements are also strongly interrelated with possible changes in political power. For example Robinson (1998) argues that the reason that inseparabilities of efficiency and distribution are so prevalent is not for conventional reasons, but because of the effect that efficient policies have on the distribution of political power. He also argues that whether or not commitment is a problem in practice

hinges on how quickly development affects political power. In Robinson's (1998, p. 29-30) words:

A perhaps the central theme of existing ideas about bad policy is that bad policies occur because they happen to benefit some politically powerful groups and that the Second Welfare Theorem fails to hold. If growth is not Pareto improving, and if market participants have political power to oppose changes which adversely affect them, development may not occur. Without political institutions to generate compensation, coalitions with a vested interest in old technologies, types of capital, or institutions, will attempt to block change... [S]ince gainers cannot commit to compensate losers ex post a particular policy is not chosen, even though it is known to be efficient.

Accordingly, in order for the Coasian logic be applicable in any evaluation of institutional structurings, “incentive-compatible” or “self-reinforcing” arrangements are required (Acemoglu, 2003). Such cases can exist in repeated games where future punishment strategies play a role. In such cases commitment can be supported, but then there are further requirements among which time horizon of the ruler is one of the most important factors because, the possibility of replacement weakens the incentives from the threat of future punishments and thus reduces the value of future cooperation for the ruler. Consequently, the most efficient outcome becomes difficult to be reached. Alternatively, Acemoglu and Robinson (2000b, 2002) propose that rulers who fear replacement are more likely to resist the introduction of superior technologies or institutions when these changes may erode their incumbency advantage and their potential future political power.

Efficient Institutions View to diverse institutional structuring across countries is thus inappropriate for the cases of Iran and Turkey. Apart from the general limitations given above, our country cases have special features particularly associated with the high extent of the state intervention in the economy. For example, in monarchic Iran, despite the existence of a constitution, time horizon of the extremely interventionist shah was naturally very long and the fear of replacement effect was very low. In the republican Turkey, on the other hand, time horizons of succeeding political parties often remained very short, repeatedly interrupted by military coups. Therefore, when the formation and restructuring of economic institutions in the two countries are evaluated in detail, the political power balances appear as much, if not more, influential as efficiency considerations in those processes. These processes and mechanisms will be elaborated in depth in the following sections.

Yet to put it briefly, utilitarian approach to institutional dissimilarity across countries, in which the original needs of societies determine the emergence, change and stability of institutions, cannot take us very far in understanding the reason behind the persistence of some specific institutional structures, despite them historically being proven to be inefficient. This micro-level perspective examines the issue in terms of ‘collective action problem’, in which, when there is not enough actors who see sufficient personal utility in establishment of a particular institutional arrangement and thus not

willing to contribute to its creation, the pre-existing institutional structure remains intact. However, all complex interactions explained above point towards a need for identifying the causes of collective action problem. That is to say, what is the reason behind the inexistence of collectively acting actors to contribute to institutional change despite the change being socially more efficient? Hence, there is a need for a framework which captures the effect of power relations, which the Efficient Institutions View largely neglects.

3.2 Transaction Costs, Imperfect Information and the Role of Belief Structures in Institutional Formation: Beliefs and Ideologies View

This second approach to elucidating institutional diversity among countries, asserts that the underlying reason behind the formation of dissimilar institutional structures in various countries, is different *ideologies* that societies and/or their leaders internalize. The reason why ideologies are considered as playing such an essential role in institutional structuring is put forward by North and Denzau (1994): the very existence of *uncertainty* stemming from diverse situations characterizes the choice-making, at both individual and institutional levels. The relationship between uncertainty and ideologies, on the other hand, are explained in terms of *mental models* (i.e. belief systems such as myths, dogmas, and taboos in ‘primitive’ societies and religions and ideologies in ‘civilized’ societies) that are constructed by individuals in order to interpret the world around them and make decisions in the face of uncertainty. Ideologies, in effect, evolve from such constructions. As North (1996, p. 4) puts forward, “the pervasive human attempt to reduce uncertainty is the key to understanding the way belief systems evolve.” That is, agents do not always have a precise idea about the changing character of diverse circumstances within which they have to make decisions. However, this does not stop the process of decision making. Rather, in the face of uncertainty, *belief systems* serve as a basis for decision making, though the consequences are not always what individuals predicts.

In the development of ideologies, beliefs or generally ‘mental models,’ the key factor is ‘*shared mental models*’, which is related to *learning*, but has a deeper effect than one usually assumes. That is to say, an uncertain chooser learns directly from the external environment to improve his mental models. This process is slow, and can be made more rapid by having some indirect learning in the form of artifactual models already created by others, that is ‘*shared mental models*’. A set of prior beliefs about ‘action-outcome mappings’ is then learned as part of the shared mental model, in the form of traditional culture or ideology. Shared mental models become more significant particularly when acting in accordance with an established belief system is convenient – or less costly, economically speaking – especially when “one cannot ascertain the probability of an event and therefore cannot arrive at a way of insuring against such an occurrence” (North 1990, p. 126). Consequences that are not anticipated by the actors in advance might sometimes dominate the situation in such a way that actors facing increasing complexity of the situation may prefer to stick to the same set of beliefs instead of measuring their performance and adopting new tools if necessary. Consequently, growth-retarding economic policies or more broadly institutions may well endure.

In view of that, according to Ideology View, which states that there is uncertainty about the right economic institutions, the political-economic systems and institutional structures of different societies are, in effect, shaped by ideologies which can be viewed as shared mental models of a society. Thus, this view asserts that problems in political economy or economic development, for example, all require an understanding of the mental models and ideologies that have guided choices upon institutional constructions. This is because, ideologies, in a way, have a deterministic effect on our interpretation of various institutional structures. Acemoglu, Johnson and Robinson (2004), for instance, remind us that ideological differences between the leaders of North and South Korea, on whether communist or capitalist economic institutions are more conducive to economic growth and development or on which one provides greater social benefit for the society, may well led to formation of radically different institutional environments in these countries.

Indeed, the central reasoning behind this view is the cognitive dimensions of institutionalization, that is individuals' internalization of some particular institutional environments, which leads to inertia. More specifically, as Zucker (1977) points out, dominant behavioural norms in societies are internalized as cognitive schemata and are socialized as taken for granted routines that are no longer questioned. Thus, a new institutional mix, particularly the ones that significantly differs from the old patterns, may not easily spread among the society, if it is not attractive to the majority of the population even if the estimated benefits exceeds the sunk costs related to establishing it. As also Veblen (1898) puts it: circumstances in an economy might not be conducive to the best material interest of the system in force if a community's past habits of thought are at cross-purpose with the conditions of life afforded by the new state of industrial arts. The problem basically is a matter of belief structures accumulated in different stages of the life history of any society, that is shared mental models. Thus, ideologies or belief systems may well become entrenched due to positive feedback effect. Romer (2003) for instance presents a model where misconceptions of voters with different beliefs correlate and lead to socially inefficient outcomes.

The role of belief differences in shaping policies and institutions is also expressed in a number of comparative economic history studies. Timur Kuran (2003), for instance, in his work on institutional causes of economic underdevelopment in the Middle East, stresses upon the role of institutional structures associated with traditional Islam. The author explicitly states that a number of critical institutions, which were evidently the products of Islamic ideology, though egalitarian in a way, blocked the region from adapting the conditions brought by the Industrial revolution. The *Islamic contract law*³

³ “The Islamic Law of Contract enabled the pooling of labour and capital through partnerships. Under the system...investors who could not or did not want to exert physical effort financed merchants and producers lacking the capital...What is striking about the consequent partnerships is their small scale and short duration. Although it was legal for fifty people to pool labour and capital for a trading mission expected to last three years, typical partnerships with usually only two partners, was established to pursue a mission with an expected duration of at most a few months” (Kuran, 2003 p.66).

and the *Islamic inheritance system*⁴, by creating incentives to keep commercial enterprises small and short-lived, prevented the emergence of modern commercial institutions from within Islamic law. The consequence was a weak entrepreneur class, strong state intervention in economic life and relatedly, a large bureaucracy. Small traditional enterprises meant a *limited division of labour*⁵ which in turn implies stagnant commercial relations. Furthermore, the aim of securing private property consistent with the Islamic ideology, brought about the *Waqf* system as an antidote to predatory states and arbitrary use of power, because regardless of the service it provided, a *waqf* was considered *sacred*, making the *waqf* assets more secure. However, as Kuran (2003) notes, in the eighteenth and nineteenth centuries, major *waqfs* in the Middle East, with perpetual functions, became conspicuously dysfunctional when around the world new technologies of production were being exploited via reallocation of existing resources.

Therefore, mental models such as belief systems or ideologies appear to play a significant role in creation and maintenance of various institutional arrangements. In fact, for our cases of Turkey and Iran, one cannot deny the importance of ideological differences, particularly the different sects of Shiism and Sunni Islam, in creating different viewpoints towards certain economic as well as political institutions. Nevertheless, as it is misleading to point toward to ideologies as the sole *raison d'être* behind diverse institutional developments and resulting economic performances of North and South Korea, particularly when the whole actions and outcomes of more than a half a century are available for comparison, limiting the causes of completely different transformation experiences of Turkey and Iran to belief differences would not provide us with complete explanation of institutional divergence.

That is to say, Turkey and Iran both originated two of the major ancient civilizations and greatly contributed to the formation of Islamic society and culture. Religion and state administrative system were inextricably intertwined in both countries. However, in the nineteenth century, the *ulama*, as a leading class in both countries, went on a totally different reformation as a response to the rising international power of the West. Accordingly, their role in the two societies developed in a totally different manner. That is, the late nineteenth and early twentieth centuries witnessed the replacement of the *Ulama* in the Ottoman-Turkey with the bureaucratic intelligentsia, whereas the same international conditions led to Iranian *Ulama* to strengthen its position in political and economic institutional restructurings. These restructurings, in turn, had profound effects

⁴ Islamic inheritance system was a remarkably egalitarian system in which the male and the female relatives were getting half and half. However, according to Kuran (2003) it made it difficult to keep the property intact from one generation to the next. Consequently, successful businesses were doomed to fragment following their founders' death. What is more, in a society where relatives, thus heirs, were very high in numbers, reconstitution and dissolution becomes excessively costly, leading the investors to keep the risks at minimum by keeping the partnerships small and limiting their duration. In many of the Western countries on the other hand, because the Bible does not explicitly specify an inheritance system, it was much more on experimentation and the common practice was primogeniture, where the oldest son gets the larger share. In this way, long term business partnerships and possibly successive large enterprises became possible.

⁵ Kuran (2003) demonstrates that the number of commercial occupations between the 8th-11th and 12th-15th centuries was statistically constant, whereas the number of occupations in the state bureaucracy and the military tripled and the number in education, law and religion more than quadrupled.

on formation and change of political institutions, distribution of resources, power balances and thus economic institutions.

3.3 An Application of the Strong Version of Path Dependence Theory to Institutional Formation: The Incidental Institutions View

Incidental Institutions View approach to institutional divergence across countries is principally a critical response to the Efficient Institutions View, which perceives institutions as choices and thus attributes the cause of this institutional variation to different cost-benefit calculations of individuals. The Incidental Institutions View alternatively puts forward that the evolution of institutions, organizations or practices does not necessarily follow a pure logic of efficiency. Accordingly, it argues that *unforeseen small events*, also called ‘historical small events’ following the writings of Brian Arthur on complexity, increasing returns, and path dependence, grow big and lead to substantial consequences in future. From a negative point of view, that is to say, small errors related to particular consequences of historical accidents or other social interactions, last long grow big and thus interrupts institutional progress.

The arguments of the Incidental Institutions View, in fact have their origins from *path dependency* tradition in economics, economic history and political science. The strong variant of the path dependency argument, to which the Incidental Institutions View is particularly related, focuses more on mechanisms that lead to *persistence*. Steps are considered to be to some extent contingent at the early stages, but after a point in time they are argued to produce a near-deterministic path. That is, institutional persistence comes out due to *increasing returns* that follow from an initial choice or a step in one particular institutional direction, similar to the notion of ‘first mover advantage’ in microeconomics. The significance of the influence of increasing returns here stems from ‘learning and coordination effects’ and ‘adaptive expectations’ (Mahoney, 2000; Pierson, 2000).

Indeed, what made the theory of path dependence such a popular research area among many economists, such as Brian Arthur, Douglass North and Paul Krugman, was the first of the sequel of articles on the issue of path dependence in economics, namely, ‘Clio and the Economics of QWERTY’, published by Paul David in 1985. Paul David’s work on the economics of QWERTY keyboards is in fact an example of Incidental Institutions View. David argues that in the late nineteenth century, the QWERTY type keyboard was developed due to clashing and jamming problems with mechanical parts of typewriters. Besides, it was also a marketing strategy, in that all characters that a salesman needed to write the brand name “typewriter” to impress his customers, was put on the first row of the keyboard. David stresses on the fact that although the new digital technology does not any longer allow clashing and jamming and there are faster keyboard options that would let us write 20-40% faster, the institutions – that is the QWERTY keyboard itself – has persisted. Thus, ‘QWERTY-nomics’, in general, points at a critical issue in the historical evolution of social and economic institutions. To be precise, evolution of institutions may be blocked in to specific paths in history because some

unforeseen *small events* (i.e. choice of QWERTY as a marketing strategy) grow big and lead to substantial consequences in future. This is because; feedback mechanisms working in certain ways disallow individuals to switch between different behavioural strategies (therefore other paths of evolution) via exposing costs to their decisions of changing strategy. It then becomes imprudent to get rid of old habits and develop new behavioural patterns as alternatives due to the very existence of uncertainty.

Following Paul David (1985), Brian Arthur (1989, p.1), in his prominent article ‘Competing Technologies, Increasing Returns and Lock-in by Historical Events,’ argued that “when two or more increasing-return technologies compete, then, for a market of potential adopters, insignificant events may *by chance* give one of them an initial advantage in adoptions.” This privileged position that is gained by chance, however, endures for a long time due to the positive feedback effect, making path dependent factors vital for market share. An extension of this reasoning to the chain of events in the ‘*markets for institutions*’, then, we come across with a three-stage path dependent process in institutional formation. In the first stage, an event is ‘*naturally*’ selected and enters the intermediary stage as a result of a *stochastic procedure*. In the intermediary stage, feedback mechanisms operate but without a determinate destination. The intermediary stage is also where the ‘mental models’, explained in the previous section, also play a role via feeding back upon ideologies and thus magnifying the significance of particular consequences of *naturally* selected events. The final stage is characterized by *lock-in*, because in this stage switching from one institutional organization to another becomes extremely costly. Hence, similar to Arthur’s case, in this third stage one particular institutional arrangement dominates and almost forcefully makes even the new actors to adopt to it.

Having generally explained the roots and various characteristics of the Incidental Institutions View, now let us underline some of its specific features which makes the former inadequate in analysing the particular cases of Iranian and Turkish institutional transformation experiences, that the current research deals with.

First of all, the Incidental Institutions View, strongly linked to the theory of path dependence, tends to have a rather *deterministic* and *inflexible* approach towards institutional development. The arguments predominantly have a tendency to focus on mechanisms that anchor the chain of possible events to a particular route, which is itself determined by the initial conditions, some of which created by chance factors to some extent. The commonly used terms in explaining institutional evolution such as ‘self reinforcing processes’, ‘lock-in’ or ‘irreversibility’, within which early chance events tip the random walk towards one path that may well be a suboptimal path, rule out even gradual adjustments to an institution that may be necessary for its long-term survival. Accordingly, we can say that such a view though acknowledges the possibility of change, generally pays less attention to the sources and ways of achieving change. It is mainly because, particularly in the strongest versions of path dependency, the image or model of change is one of *punctuated equilibrium*. Path transformation is presumed to be highly unlikely except through rare radical ruptures or reorientations, which are often associated with violent *external shocks* (Djelic and Quack, 2007).

Second, this type of approach, in turn, excludes the individual actors and their strategies as well as the social contexts in which these processes take place. This does not however, mean that a narrow actor-centered perspective – as if the evolution of a path were solely related to the rational decisions of independent actors – is the best appropriate analysis of institutional evolution. Instead, as Crouch and Farrel (2004) points out, path dependence appears as the evolutionary outcome of multi-actor collective interaction, due to which, an inefficient macro-level outcome can well be the unintended consequence of the interaction of rational micro-level decisions made by individuals.

To sum up, the Incidental Institutions View has significant merits in that once an institutional structure comes into existence and entrenches; interdependent and complementary institutions tend to persist via embedding into the overall institutional landscape (Granovetter, 1985). Nonetheless, collision of strategic actions of individuals, some of which seek to change whereas some intend for maintaining the prevailing institutions, and the specific institutional context which to an extent mould their ability to mobilize their resources tells much about the course of the institutional evolution. Hence, the possibility of and factors leading to any erosion of those self-reinforcing processes, at least in the medium or the long run, should also be explored, for a better understanding of institutional change or inertia. Consequently, we should analyse the details of the decision processes of individual actors and groups, amalgamation of various decision points and naturally multidirectional conflicts; then we have *power balances*.

3.4 Institutional Formation and Political Economy of Institutions: Political Institutionalism

We have so far seen that the concept of *power* has a particular importance in shaping and reorganizing institutional structures. Accordingly, the Social Conflict View, which is first systematically developed in the economics literature by Douglass North (1981), puts forward that institutions, both economic and political, are not always chosen by the whole society or for the benefit of the whole society, but by the groups that control the political power at the time. These groups will choose the economic institutions that maximize their own rents, and the economic institutions that result may not coincide with those that maximize total surplus, wealth or income. North argues that a set of property rights that the “self-interested state agents,” as North models, would choose for society would be those that maximized their payoff and because of ‘transaction costs’, these would not necessarily be the set that maximized the social welfare, or say would be unfavourable for some other groups.

Accordingly, Acemoglu, Johnson and Robinson (2004), state that *commitment problems* are at the root of ‘transaction costs’ creating such a divergence between the interests of the state and the citizens. As they put: “because commitment problems seem so endemic in collective choice and politics, it seems natural to believe that institutional change has significant distributional consequences and as a result there will be conflict over the set of institutions in society” (Acemoglu et.al. 2004: 48). Hence, in order for

guaranteeing the outcomes of the new economic institutions, change or re-structuring in existing political institutions appears as necessary in the eyes of the hegemonic classes.

In such a non-utilitarian mechanism, power is understood as *institutionally embedded power* given that different institutional settings, in both political and economic spheres, provide societal actors a variety of access to different types of power resources (Djelic and Quack, 2007). This institutionally embedded power in turn plays a role in entrenchment and reproduction of institutional frameworks.

Thus, the framework develops as follows: Given that economic institutions determine the incentives of and the constraints on economic actors, shape economic outcomes and hence different groups and individuals typically benefit from different economic institutions, there is generally a conflict over these social choices, ultimately resolved in favour of groups with greater political power. The distribution of political power in society is in turn determined by *political institutions* and the *distribution of resources*. Political institutions allocate *de jure* political power, while groups with greater economic might typically possess greater *de facto* political power. Thus, Acemoglu et.al (2004)'s theoretical framework becomes a dynamic one with political institutions and distribution of resources become the state variables. These variables, however, are not static: they may also change over time due to prevailing economic institutions affecting the distribution of resources, and groups with de facto political power today strive to change political institutions in order to increase their de jure political power in the future.

Therefore, information about the two state variables, which are political institutions and the distribution of resources, at a point in time is necessary to discover the facts about all the other variables in the system. In view of that, de jure and de facto political powers that are determined by political institutions and the distribution of resources respectively, in turn, shape the economic institutions' formation and affect the future evolution of political institutions. What is important here; although the economic institutions have substantial effect on economic performance as underlined by the overwhelming literature on institutional economics, they are endogenous to prevailed political institutions and distribution of resources in society.

The Social Conflict View, which particularly searches for the causes of persistence of inefficient institutions, provides valuable tools for a comprehensive analysis of institutional variety among different countries. However, this view, though points towards central issues essential for the current analysis, does not fully grasp the vital aspects required for a full-scale exploration of the two country cases that the current study deals with.

To begin with, the *state variables* – political institutions and distribution of resources – which are considered as sources of institutional diversity across countries, are analysed on the grounds of colonial origins by the authors. Specifically, Acemoglu, Johnson and Robinson (2001; 2004) propose that in countries where the colonial powers settled, political institutions established in a different manner than those where colonial powers' aim was only extracting these countries' resources. However, what is distinctive

about Iran and Turkey, neither state were colonized partly due to the environment of rivalry of powers in these countries – between Great Britain and Russia in Iran and Great Britain, France and Germany in the Ottoman Empire (Pamuk, 2008). It is an important feature that underlines the complex nature of pace and structure of institutional evolution in the two countries, because institutional change was not as easy as it was in the official colonies. Rather, such a characteristic draws the attention to the role of interdependence among both the external developments (impact of outsiders) and the internal structures (path – *not past* – dependent factors) in formation and reformation of political institutions and hence distribution of resources.

In addition, the framework though acknowledges the importance of ideologies in directing decisions on the possible institutional compositions in the short-run, does not put much emphasis on this factor in shaping institutional structures in the long-run. This standpoint is certainly appropriately constructed, since it would be a rather naïve approach to attribute the vast diversity between, say North and South Korean or pre- and post- Revolutionary Iranian economic policies and institutions, to their leaders' ideologies on what is most socially beneficial for their society. However, what Acemoglu et.al (2004) overlook, is the importance of the highly complex interdependence and interaction among external factors and internal structures, that is shared mental models (belief structures), their feeding back upon ideologies on a widespread base within society, making leaders misrepresent policy makings to be perceived as legitimate and resulting intricacies regarding possible path switches.

Furthermore, Acemoglu et.al. (2004) implicitly point towards the importance of interest group formation. That is, on one hand, government decisions affect transaction and information costs of different economic interest groups, on the other hand different economic factions can organise themselves in such a way as to influence government policies in accordance with their interests. Given that any institutional arrangement together with its distributional implications are products of specific state policies, an appraisal of interest group formations (what type of groups are formed) and sources of their power along with various rent-seeking processes, whose inputs and outcomes depend on institutional rule and inter- and intra- class power balances should also be included into the analysis. Because, both Iranian and Turkish states were involved not only in redistributing incomes but also in creating new property rights and even entirely new economic classes.

To put it briefly, for the specific cases of Iran and Turkey we should first elucidate the *roots* of the formation of initial political institutions and associated distribution of resources in order to verify the power balances. Later, we can assess the mechanisms leading to institutional change or persistence on the grounds of complex web of power relations in the two countries.

4 A New Dimension Proposed: Broader Conceptualization of Institutional Evolution and the *Clash of Paths*

So far, the key mechanisms identified in the literature on the causes of institutional diversity, include the concepts of *efficiency* from a utilitarian perspective; *belief differences* from the viewpoint of sociological institutionalism; *increasing returns*, *self-reinforcing processes*, *institutional complementarities* and *lock-in* from structuralists' and functionalists' stance; and finally *political institutions* and *power balances* from the political institutionalists' point of view.

Since, in the previous sections, *efficiency* and *distribution* are demonstrated to be inexorably inseparable (so underlining the limitations of the Efficient Institutions View), ideologies and path dependent factors to some extent, but roots of altered power balances among different hegemonic classes to a larger extent, appear to be vital in understanding various institutional formations with totally different implications across countries. However, if there is an interrelationship between economic institutions and political institutions via determining political power balances and hence distribution of resources, then the question to be addressed for our particular cases is: where does the political power come from? Hence, a profound deliberation of *when* and *how* institutions evolve and *why* they change or persist requires a broader conceptualization of institutional evolution particularly for our specific country cases at hand. Doing this, in turn, involve avoidance of putting the ideological differences at the centre; trying to scrutinize the formation of political institutions and consequent distribution of resources that are put forward as the state variables determining institutional diversity in the Social Conflict View; but while doing this also eschewing from structural determinism of Incidental Institutions View.

Moreover, institutional development should be analysed via putting emphasis on *timing* and *sequencing* of events (Pierson, 2004), as interdependent sequence of events structure the alternatives for future institutional changes (North, 1990). Accordingly, we first focus on the historical origins of particularly political institutions, which indeed emerge from strategic and many times collective actions of more or less conscious actors under the restraint of particular domestic structural factors and external effects, contrary to Incidental Institutions View that attribute creation of various institutions to some chance elements. However, it is important to note that the outcomes at times do not materialize as intended, because institutional outcomes depend on the *intermediary mechanisms* between the initial conditions and the outcome. The next stage is in which the established institutions enter into a process of entrenchment. Then, institutional complementarities impede possible improvements in some organizations. Not only institutional complementarities, but also politically powerful hegemonic classes and groups with vested interests contribute to persistence of some specific institutional arrangements that are to their particular advantage. Ultimately, these deep-rooted institutions, in a way, internalize individuals' behavioural patterns and mould their attitudes towards the role of some specific institutions.

Yet, such a procession does not mean that change, either gradual or radical, is impossible. Indeed, more recent contributions to institutional evolution move away from institutional persistence and stress more on possible mechanisms that allow for more openness to change (see e.g. Ebbinghaus, 2005; Djelic and Quack, 2007; Crouch and Farrel, 2004; Thelen, 2003; Morgan and Kubo, 2005). Ebbinghaus (2005), for instance, examines whether the processes of institutional change can be explained via turning upside down the mechanism specified as leading to institutional persistence. In view of that, it is proposed that a logic of entrenchment that has to do with increasing returns will be sensitive to decreased efficiencies and transformation of the purpose of an existing network. Moreover, a power-induced stability can be questioned by shifting power relations which may arise due to the formation of new interest groupings or inability of pre-existing powerful classes to mobilize their power resources. Furthermore, institutional complementarities can work towards stability, but a tight interdependence between institutional subsets could also mean that when a particular subsystem evolves, the entire system is under pressure. Finally, mental models may well change, particularly in systems which can be considered as *open*⁶. In such a case, when the meaning of ‘legitimate’ changes, then pressures towards institutionalization become less and less appropriate and peter out.

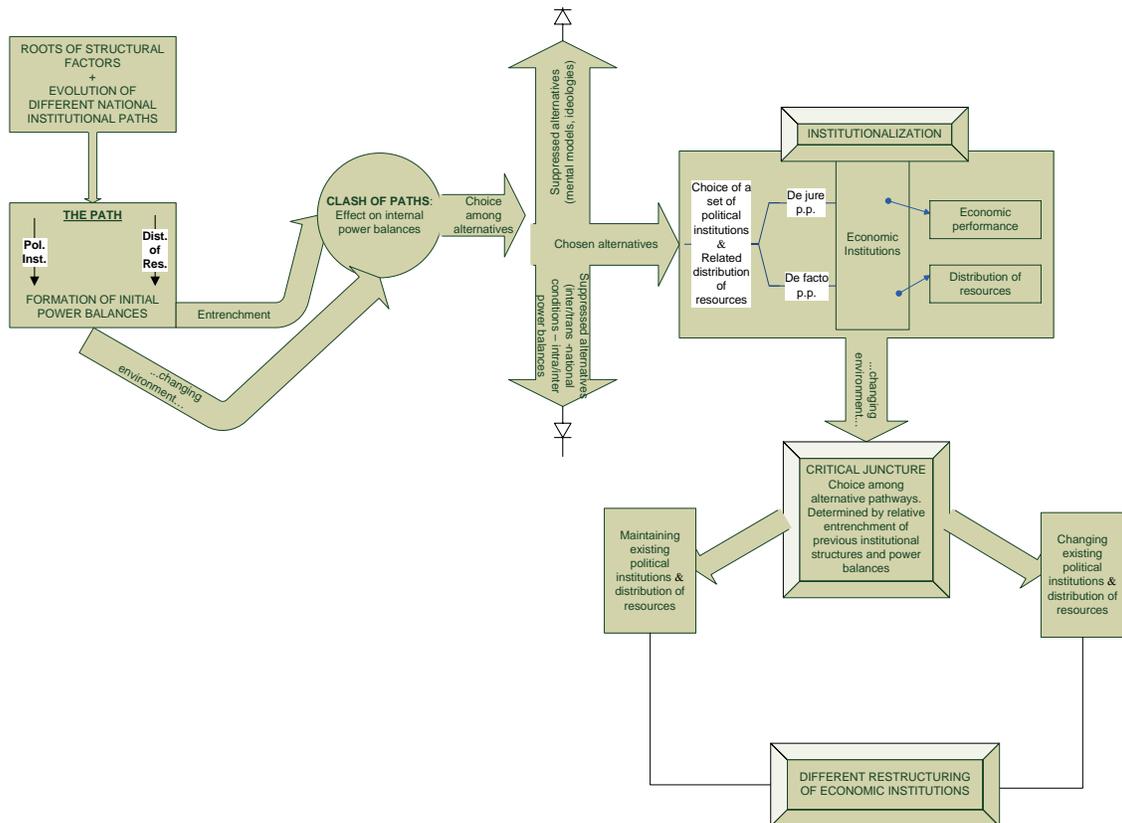
Indeed, ‘open system’ approach, though make the analysis relatively more complex, produce several advantages for a well-established analysis of institutional development. In open systems, however, possible *co-evolutionary interactions* (Djelic and Quack, 2007) among different nation’s institutional constructions should be carefully evaluated. Because such a co-evolutionary interaction will provide societal leaders, interest groups and other powerful classes with more than one road with several branching pathways, leading to long periods of conflict among countervailing forces.

Accordingly, the current work, taking into consideration of the merits of the different approaches explicated in the previous sections, proposes a new dimension which can be called as the *Clash of Paths*. In this framework, structural factors affect the establishment, reformation and persistence of institutions through a path dependent process, but the path of a country can well be affected by the outsider’s paths (usually the superior paths). The attempt of the widely accepted superior path to change the inferior one is, in effect, determined by its own path dependent restructuring. That is, the transformed would push the untransformed towards a change similar to his experience, due to psychological, philosophical and political reasons. Consequently, the so-called inferior path can *maintain*, *shift* or completely *switch*, but this time to the extent that its own path-dependent structures, ideologies and power balances permit it.

⁶ Both countries at stake can be defined as open systems. For the nineteenth century for instance, Ottoman-Turkey due to external debt burden and the non-rentier Iran, due to technological backwardness in oil extraction and resulting foreign dominance in the oil sector can be considered as open systems. Similarly in the twentieth century as well both countries were open to the effects of international developments: the Republican Turkey, during the post WWII period particularly in the 1970-80 interval due to severe foreign exchange shortages and Iran during the whole period before the Revolution (e.g during the oil-shock period due to world demand in oil.).

Subsequently, an institution emerges at a *critical juncture* at which collective actors establish new rules. The selection of a pathway is the result of political conflicts and power relations (Knight, 1992). Then a process of entrenchment starts due to positive feedback effects similar to those illustrated in David (1985) and Arthur (1989). As a result, the choice sets of societies enters in a process of restructuring, through which frontiers of these option sets are drawn, either in the form of limitation or widening as explained in North (1990). In addition to this internal formation, however, external environment also have a profound impact on this restructuring. What follows is deciding among alternatives, but depending on the above explained interaction of internal and external factors vis-à-vis inter- and intra-class power balances. The one which overcomes the other, happen to be more influential in the new restructuring. As should be clear, more fundamental changes comes apparently with higher costs, when the pre-existing institutions are severely entrenched due to the transaction costs associated with replacing them.

Schema 1: Schematic Representation of the Clash of Paths



So therefore, let us dig deep into Iran’s and Turkey’s bases of structural factors forming the initial political institutional structure and resource allocation in order to find the sources of de jure and de facto political powers in the two countries.

5 The Roots of Institutional Formation in Iran and Turkey: Similarities and Differences between the Founding Factors of the National Paths of the two Countries

5.1 Appearing Similarities

Although there are not comparative works on the socio-economic and politiconomic conditions in the two countries, reading through the country-specific studies reveals corresponding features of the roots of Iranian and Turkish politiconomic institutional paths.

To begin with, reasonably similar to some other less developed countries at the beginning of the 20th century, both economies were heavily agricultural based and open to trade and foreign investment. The administrative structure to control the land was fief system and was called as *timar* in Ottoman (Inalcik, 2000) and *tuyul* in Iran (Issawi, 1970), which could not be managed effectively in both countries, subjected to corruption and led to resurgence of local administrative powers, which in turn gave rise to problems in collecting taxes and in decrease in central treasury's income.

However, there were some certain characteristics that made Iran and Ottoman-Turkey similar to each other and distinguished them from other less developed countries, that is *strong central authority*, *political sovereignty*, and *small-scale production* (Pamuk, 2008). That is, in both countries there was the system of a central authority, though the Iranian state was not as powerful as the Ottoman state was. Furthermore, European-type feudalism did not exist in none of the countries. Specifically, socio-economic powers did not pass to feudal type of living following a fast transformation. Class-based stratification did not exist either. Such countries are defined as semi-feudal or patrimonial states in the literature (Katuzian, 1981).

Moreover, regarding the power of influence of Europe's efforts for opening less developed countries to world markets vis-à-vis their comparative advantage, Gallagher and Robinson (1953, cited in Pamuk 2008) categorize the peripheral countries as 1) official colonies and 2) countries that became a part of an unofficial empire of an imperial power. Pamuk (2008) proposes a third categorization, that is: 3) countries that were neither colonised nor became a member of an unofficial empire due to continuous rivalry between imperial powers on its resources. Such a categorization is important because this political sovereignty, in turn, meant that imperial powers that were interested in these countries had always had to negotiate with the central authority. Moreover, the central authority had a larger room for manoeuvre. This feature in turn has an effect on for example economic policies regarding openness and foreign trade in particular, and economic integration in general.

In terms of the above mentioned international environment, both countries became a free-trade zone after the treaties they signed with several developed capitalist states of the time. Iran signed the Turkmenchai treaty with Russia in 1828 and Anglo-Persian Commercial Treaty with Britain in 1841 whereas Turkey signed 1838 Baltalimani

Treaty with Britain and 1861 Trade Agreement with France. Due to these commercial agreements and concessions together with deficiencies in infrastructure, industrialization movements in open-economy conditions remained weak in both countries. Likewise both countries could find opportunity to pursue protectionist policies only in the second quarter of the 20th century. But here again, the extent of protective measures were different. The invention of oil in Iran had profound effects on policy-making (Katuzian, 1981). For example, although state intervention was widespread in Iran, due to its underdevelopment in oil extracting and processing technologies and lack of skilled labour, Iran could not put forward protectionist policies in its most important sector.

Regarding integration with the world markets and accordingly the volume of foreign trade in the 19th and the early 20th centuries, both Iran and Ottoman-Turkey were below the Middle East average. The performances of Turkey and Iran compared to Egypt during the period, for instance were essentially poor (Issawi, 1981). Pamuk (2008) provides three explanations for this difference: First, neither Turkey nor Iran gave priority to economic integration and foreign trade. Exports were supported only to the extent of financial political and military impositions. Second, neither states were colonized, that is powerful countries could not make every reforms that they desired. Third, the environment of rivalry of powers in these countries created resistance against European penetration in both countries. This in effect retarded the integration process.

A further common characteristic of the two countries was a mosaic type social structure that is both of them were divided according to ethnic and religious differences such as a Muslim majority versus a non-Muslim minority. However, there are significant nuances between these two types of structures that should be considered with caution. First, a large segment of relatively more prosperous non-Muslim communities who had had contacts with Europe for long time, had Western style education and knew Western type trade methods was one of the Ottoman Empire's social characteristics. In Iran, on the other hand, though there were non-Muslim minority groups, they were much less in number; culturally more isolated thus had limited influence on determining economic or social processes. Moreover, the social structure in Iran was characterized by an exceptional group-dependence originated from tribal roots and communal conflicts that according to Abrahamian (1982) could best be described as "communal diversity" with its intense tribal and communal conflicts.

Thus ethnic conflict was not the most important issue in Iran whereas in the Ottoman Empire ethnicity came increasingly to the fore particularly after the French Revolution. This had considerable outcomes in many respects such as persistent independence movements and related wars on the territories of the Empire in contrast to Iran which did not have any noteworthy wars after the Russo-Persian war. This is important when it is considered that the Ottoman Empire got its first foreign debt after the Crimean War. More interestingly, it was the Galata Bankers who belonged to these non-Muslim communities and had extensive communications with the European financial institutions (in contrast to 'Sarrafis' of Iran), that played the major role in the Empire's first foreign borrowing experiences. Such developments, in turn, engendered relatively different public reactions to fairly similar economic policies in the twentieth century, as

foundation of modern banking facilities was subject to different responses from the public in these countries: abolition of Galata Bankers meant something positive to Turkish people whereas in Iran Sarrafs had long had a very good reputation among Iranian people.

5.2 An Important Difference behind the Appearing Similarities: The State Tradition

Although this study does not perceive state as a unified subject acting in one way or another, this view applies to modern capitalist states rather than patrimonial type state structures. Accordingly, we can argue that one important aspect that distinguishes the pre-twentieth century Ottoman Empire political system from the Iranian political structure is that a continuous state tradition was one of the Ottoman's main qualities whereas Iran had long been governed by "changing and kaleidoscopic array of dynasties that appeared and disappeared with amazing rapidity." (James Bill, 1972:5) The country was thus suffering from the lack of deep rooted and robust state administrative institutions.

Differences in pre-capitalist period state organizations are vital in understanding relationships – collaborations or contradictions – among social and economic groups and classes in the modern period since as Mann (1993: 52, cited in Akca, 2006) argues: "states institutionalize present social conflicts, but institutionalized historic conflicts then exert considerable power over new conflicts." Thus, when state policies are considered as the result of class and group conflicts and cooperations which indeed themselves inscribed in the very structure of the state as put forward by Poulantzas (2000), then continuous state tradition becomes important because as mentioned above 1) previous political institutions and related distribution of resources determine political power balances and 2) economic institutions are endogenous to those prevailed political institutions.

For instance, in the Ottoman Empire the continuity of the strong state was the sole condition for classes' existence and the spread of Islam. Thus secular imperial politics was legitimized. The Qajar shahs who "in theory...were omnipotent; in practice...were politically impotent," on the other hand, ruled through, "and so with the kind permission of...tribal chiefs, local notables, and religious leaders." (Abrahamian, 1982:41) Such patterns in turn led to dissimilar political institutional settings and diverse formation of political power balances in the two countries. Accordingly, assuming that institutions are choices made in line with the demands of hegemonic classes; institutional restructuring, in relation, means converting from one hegemonic project to another; and developments in state organizations are those that lies behind the origins of the power balances, in the following section, we analyse the formation of various politically active groups with economic interests regarding their relationship with the state. Among them

the *ulama* and the *traditional bourgeoisie* in Iran and the *military* and the *modern bourgeoisie* in Turkey appear as the particularly important ones.⁷

Thus, differences among the characteristics of these groups with either de jure or de facto political power (or both) and their existence and relational patterns within the institutional materiality of the state in terms of complex web of power balances will shed light on the different institutional restructuring, in both political and economic spheres, on the eve of 1980s.

5.2.1 State-Religion Relationship in Turkey and Iran

A detailed historical assessment of the 16th to 20th century Iranian institutional structuring, demonstrates that some of the organizational arrangements were indeed, to some extent, the consequences of a clash with the path of Ottoman institutional development. To be more precise, one distinctive feature of Iran is a politically active and economically powerful clergy. Such a characteristic however, was not formed by any chance factor occurred in a stochastic process as proposed by the Incidental Institutions View. Conversely, the establishment of the Safavid State was a critical juncture in that religious mysticism was one of the most important founding factors of the state and the related institutions that were established were choices rather than “accidents”. This was mostly because the Ottoman Empire, which was enlarging towards the West, was under a thorough institutional development process that included the centralization movement, in which the nomadic heterodoxy Turkmens, the original founding factors of the state, gradually alienated due to nomadic traditions being incompetent with an expanding society and its organizational and policy-related needs.

Those heterodox Turkmens of East Anatolia who were left alone due to the Ottoman’s new social structuring thus turned their faces towards Shah Ismail (Akyol, 2006). However, after a period of victories, defeat in the Caldiran War raised the recognition of a need for modern army and for it to be realized and maintained, a modern administration system in the form of say, an effective taxation system. Hence, the Ottoman-type centralization and institutionalism, according to which Turkmen-Qizilbash traditions were obstacles to modernisation, was seen as a must. The inclination of the Safavid state towards Persian bureaucracy and the Shia Theocracy started in this conjuncture. What is interesting that Shah Ismail was actually of Sunni origin. Yet, he had to espouse Shiism due to political reasons, that is the ambition of a strong Shiite Safavid state in the East against the Sunni Ottoman Empire in the West. Accordingly, the Shiite *ulama* (clergy), who were indeed transferred from particular countries in the Middle East such as Iraq, were equipped with a high religious authority and a great economic power via religious foundations.

⁷ This does not, however, mean that these four groups and classes were the sole ones with political power. Landowners had long been and the working class were becoming also important politically powerful classes in both countries. Yet, given the scope of the paper and for the sake of a concrete analytical analysis, one group with de jure and another with de facto political power are chosen from both countries.

In fact, the rise of the Safavids was one of the critical junctures in the formation of such a social group, which later would gain power to influence the state policies. With the declaration of Shiism by the Safavids as the official sect of the country, new organizations such as *sadaret* were created and the ulama integrated in the state apparatus, to which its de jure political power was founded on. However, it is important to note that none of these organizations were acting independent from the state. The Shiite Ulama, although was an effective organ in social life, had not directly intervene in the political arena before the nineteenth century. The collapse of the comparatively young Safavid State left behind not deeply-rooted, weak and intermittent state institutions, which together with the interregnum of fifty-eight years with tribal and dynastic conflicts and rise and fall of three dynasties; provided the time and the means for the Ulama to institutionalize.

What is more, the ulama as a social category with economic and political interests, set up systematic connections between some particular economic classes such as the landowners and the merchants (the Bazaar). However, as Moaddel (1986) argues, the alliance between these classes and the ulama was only an *instrumental* relationship that was based on mutually beneficial conditions. In the early periods, for instance, the clergy, particularly for consolidating relations especially with the tradesmen, gave more importance to ritualistic features of the religion. These rituals meant a growing trade for local merchants who in turn donated directly to the ulama whose considerable portion of income was based on religious taxes, donations from merchants and petty bourgeoisie, and payments made in relation to particular commercial affairs such as legitimizing the illegal income (Algar, 1969 and Uyar, 2004). In sum, such a win-win position got the two closer to each other and from then on, particularly after the collapse of the Safavid State, in several occasions where the large landowners' or merchants' interests were deteriorated due to the state policies (e.g. the planned concession a foreign company for the Tobacco Regie or the Land Reform under the White Revolution), the ulama were allied with them in their direct confrontation with the state.

When the Qajar period started, the Ulama with their established and partly institutionalized networks finally achieved an independent position from state domination. Via internalization of the ritual elements of the societal belief structure into the Shiite ideology, the Ulama's power, political and economic, increased substantially. What supported this process was that Qajar Dynasties agreed upon such a win-win situation because the Qajars "...were of nomadic descent, and for them the administration of a country was far more complex than that of a tribe...The growth of the ulama was thus reinforced by their ability to perform educational, judicial, and legitimating functions of the Qajar state" (Moaddel, 1986: 522-523). In addition, the Qajar ruler needed the cooperation of the ulama in order to legitimate their power, because the Shiite sect had been apparently severely entrenched in the society after three centuries of hard workings of the clergy (Uyar, 2004).

Thus, the era of Qajars is marked by a development in religious hierarchy, that is networks of governance, and the expansion of the financial resources in parallel with this development. As a result, some clerics became economically very powerful that even the

state could not disregard. For instance, although the increase in the ulama landownership was partly a Safavids legacy (Moaddel, 1986), it is pronounced by Akhavi (1980, cited in Moaddel) that in Isfahan, for example, the ulama comprised a very important land-owning element, via forming the forty-seven percent of the large landowners in this city. Similarly, Tenkabuni (1985) points out that Hucetü'l Şafti, a high cleric who lived in the first half of the nineteenth century, owned four hundred Caravanserai and two thousand shops only in Isfahan, and numerous villages in other cities. Waqfs, in addition, were vital sources of income for the Ulama in Iran and as well as in the Ottoman Empire. Akyol (2006) for instance underlines the enormous amount of waqf revenues during the Qajar period and states that they amounted to almost the half of the total government revenues.

Religion and state administrative system were also inextricably intertwined (Traditional Duality of *Din-ü-Devlet*) in the Ottoman Empire. However, the Safavids, coeval of the Empire, was collapsed due to a chronic legitimacy crisis, which obliged the former to make a relatively more sophisticated synthesis. Accordingly, the most liberal branch of the Sunni Islam, Hanafi School of Law, was adopted because of being more pragmatic and therefore more worldly in nature. Flexible and dynamic character of the Hanafi tradition in the Ottoman Empire played an important role in maintaining the long term survival of the empire. An example of factors leading to dynamism in the Hanafi School of Law is '*hiyel*' (tricks in religious law). *Hiyel*, are remedies applied via adapting practice to jurisprudence to avoid *haram* in situations when jurisprudence and practice are contradictory.

Moreover, the Hanafi School of Law, because developed by way of considering political conditions and public affair in a political center namely Baghdad, is more prone to a system in which the ulama join the ranks of governmental bodies (*hikmet-i hukümet*). Such an integration of the ulama to the state administrative body in the Empire then provided continuity of political legitimacy. That is to say, decisions taken by the government in a pragmatic way had to be a posteriori legitimized by the ulama through wangling. Accordingly the Ottoman ulama served as in Antonio Gramsci's term: the "experts in legitimation".

Thus, the characteristics of the Ottoman approach to interpretation of Islam (including e.g. formalism, legitimism) was rather different from the view of dynasties that governed Iran. The geographical expansion towards the West, additionally, required to ensure the socio-political order and not to discriminate against the imperial subjects that belonged to different religions which in turn meant ensuring civil union. The Sunni political doctrine was then obedience to '*Ulul-Emr*' which were understood as rulers, governments and administrators (Gencer, 2008).

Consequently, the *ulama* class and its relation with the state in the two countries then were developed into completely different structures. In contrast to Keddie (1972)'s finding of *inversely* proportional power balances of the state and the ulama in Iran, it was *directly* proportional in the Ottoman Empire. That is, in case of an external threat to state's power, ulama used to further attack to the state in Iran; whereas the ulama even in

“the sick man of Europe” were legitimizing all decisions of the state even they are not statutory in religious law. This was largely because of the belief that Islam could maintain and be spread if and only if the state was strong which further strengthened the above explained strong state tradition.

Hence, it must be clear that the Beliefs and Ideologies View to institutional formation is necessary but not sufficient to provide a comprehensive explanation on institutional divergence in Iran and Turkey even the analysis is attributed to the development in the role of clergy class in state administrative organs. Because institutions, as said before, were rather ‘choices’ made in accordance with the demands of the hegemonic classes of these countries. In view of that, after assessing the origins and the extent of political power of the ulama in the two countries, we will now try to reach the sources of the political power of bourgeoisie (traditional mercantile bourgeoisie in Iran vs. modern industrial bourgeoisie in Turkey).

5.2.2 Entrepreneurial Independence From the State

Comparing the entrepreneurial classes of Iran and Turkey requires consideration of the nature of the state-business relationship; state administrative structure; a possible threat from other classes (e.g. working class) and timing of industrialization during the course of capital accumulation.

Among the classes with power of pressure on state economic policies in Iran comes the Bazaar as another most influential. In the Ottoman Empire where all classes were tried to be kept in the place with a platonic conception of the world in which *order* rather than *change* was more accepted, on the other hand, all economic activity was heavily controlled by the state and thus the establishment of an independent local bourgeoisie class was impeded (See Keyder, 1987 and Heper 1992).

One specific feature of the Iranian local entrepreneur class was that they were forming a rather homogenous structure in a heterogeneous country like Iran. That is to say, these merchants forming the part of the traditional bourgeoisie did not consist of non-Muslim minorities as was the case in the Ottoman Empire. The importance of the merchants and craftsmen for the economy in general was also highlighted by some nineteenth century foreign officials residing in Iran. Arthur de Gobineau (1859, cited in Issawi, 1971), for example describes traditional merchants, who hold vast amounts of capital, as playing the same part as European credit institutions and providing credit even for the government. Given their importance in the eyes of the government, they appear to not to pay a penny in taxes.

Sir John Malcolm (1829, cited in Bill, 1972) as well underlines the meaning of the traditional middle class via as follows:

“The merchants are a numerous and wealthy class; and no part of the community has enjoyed through all the distractions that kingdom has been afflicted with, and under the worst princes, more security, both in their persons and property. The reason is obvious;

their traffic is essential to revenue; oppression cannot be partially exercised upon them, for the plunder of one would alarm all; confidence would be banished, and trade cease.”

which also demonstrates that the traditional bourgeoisie had long been enjoying a de facto political power.

In Ottoman-Turkey, on the other hand, the heterogeneous social structure explained in the previous sections, manifested itself in an economic transformation in accordance with Turkish Nationalistic movement pioneered by the Union and Progress Party. The aim was establishing a Muslim-Turk entrepreneur class and had momentous consequences that shaped the twentieth century state-business relationship, structure of industrialization and the nature of capital accumulation process. In view of that, the entrepreneur class in Ottoman-Turkey, contrary to Iranian local entrepreneurs, is analysed either as a weak and dominated class or as a dependent collaborator of the state in the broad literature on the state-society relations in Turkey (see Keyder, 1987 and Bugra, 1994)⁸.

Thus, with no local traditional bourgeoisie trying to impede change forced by the nineteenth century developments (on the contrary, existence of non-Muslim minorities who were rather seeking for the Western hegemony) reformation period in accordance with the nineteenth century demands of the international system were relatively much easier in Ottoman-Turkey compared to Iran, where the traditional bourgeoisie were continuously opposing against the concessions given to the European states and companies and the custom duty policies.

Given the central importance of inter and intra power balances both among the groups and the classes and between them and the state, such a different structural feature between the two countries' bourgeoisie classes had a major impact on the institutional choices made at the critical junctures.

One such important, if not the most important, critical juncture was the “coming of the West” in the nineteenth century. The institutional paths of the two countries clashed with the economically advanced and politically and socially different West's path. Subsequently, Iran and Turkey were left with a few options to select, some of which were suppressed due to ideologies and mental models and some that were shaped by exogenous variations but at the end selected in accordance with complex web of power relations.

6 Nineteenth Century: Impact of the West and Responses

Similar to many traditional systems belonged to the Islamic World, Iran and the Ottoman Empire were lacking innovative approaches towards the world system, which could be best explained by North (1990)'s “mental models.” That is the curiosity to learn about future in the West versus the view that piety rather than to seek for information

⁸ According to this literature, state was perceived as ‘above’ society which subjectified in the state elites, military and civil bureaucracy. In Akca (2007)'s words state is “deemed to be an entity and a subject which exists outside the society and whose source of legitimacy lies in the state per se.”

about what would be the end of humanity was necessary in the Islamic societies (Gencer, 2008). In the Ottoman Empire, additionally there was some sort of dynamism that was dependent upon the conquest politics. Motive for the conquests thus military technology superiority was the engine in other fields of innovation and dynamism. Yet, there was a limit to the conquests and approaching towards to this limit in the sixteenth century was the harbinger of the gradual loss of this social dynamism.

Being belonged to the last dominated religion, Islam, instilled a sense of absolute superiority, in Gencer (2008)'s words, which might gave to an outside observer the impression that the time was frozen. However, the time was passing in full speed and both the Qajar-Iran and the Ottoman Empire had gradually left behind the West which was experiencing a major transformation that would change the destiny not only of its own but also of the whole world.

6.1 Impact: Social Political and Economic Penetration of the West

Throughout the history the struggle with the West had been perceived by many Islamic societies as a struggle of faith. In the technical era, on the other hand, as opposed to the absolute superiority of one group against another, *comparative advantage* that exceeds the boundaries of beliefs and ideologies were at the stage (Hodgson, 1974, 201-5; 1996, 123-4). As a result, the nineteenth century experience of both Iran and Turkey were relatively similar marked by the social, political and economic penetration of the West (Issawi, 1982). In Abrahamian (1982, 52)'s words: “[m]ilitary defeats led to diplomatic concessions; diplomatic concessions produced commercial capitulations; commercial capitulations paved the way for economic penetration; and economic penetration, by undermining traditional handicrafts, was to cause drastic social dislocations.”

That is, as mentioned above, both countries signed commercial treaties with several developed capitalist states of the time and incorporated into the Western network international commerce. Although the “concession hunting era” (Abrahamian, 1982: 55) started relatively earlier in Iran, both countries gave important concessions to the Western countries in approximately similar areas that were ranging from the railroads (i.e. concession given to Reuters) to banking facilities (Imperial Bank of Persia and Ottoman Imperial Bank). The effects of these and the following related developments on the mercantile capital of the two non-industrialized countries would have then shape the economic institutional structures particularly during the next century vis-à-vis developments in de facto powers of these classes.

The modernization movements, which occurred during the big transformation in the West, greatly affected also the state-religion relationship and thus the status of the ulama in the two countries, yet in different ways. The initially established political institutions and associated distribution of resources that had determined initial power balances between the state and the ulama had gone through a process of a change during the nineteenth century. It was an era of transition from deduction to induction and the Iranian and the Ottoman Ulama developed different responses to these revolutionary

changes: The latter could not develop a dynamic Islamic political thought and hence could not provide an active guidance beyond either reluctantly supporting or giving a zealous response to reform initiatives whereas the former could develop a dynamic Islamic political thought and claimed that they had the ability to understand and manage the changing world (due to the Doctrine of Jurisprudence – *Ictihad*).

Consequently, the two countries when came across with new critical junctures in the twentieth century, stabilization, shift or switch of institutional paths were possible. However, then again some alternatives had to be suppressed due to belief structures (mental models), and intra/inter -power balances.

6.2 Response: Change in the Political Institutions: ‘Mesrutah’ of 1906 and ‘Mesrutiyet’ of 1908 with Different Implications for Power Balances

By the early nineteenth century it was explicit that considering the Western modernization solely as innovation in military technology would be overlooking the great transformation taking place in the background. It was firmly understood that the fate of the countries that missed the reformation era not depended on the divine will, but to concrete economic, psychological, cultural, social and demographic factors (Karpas, 2000: 155).

The Ottoman ulama for instance who had trained in accordance with Aristotelian deductive reasoning specific to the traditional world, was used to solve problems via applying universal principles to particular cases. Yet, “the world they were dealing was a fragmented world that could no longer be interpreted in accordance with universal principles.” (Gencer, 2008: 144) The inductive logic as in the Sociologism of Emile Durkheim had to be applied and that was something very unfamiliar to the Ulama. In such an environment, thus the bureaucrats of ‘Tanzimat’ (the administrative reform period) in the process of modernization, did not hesitate to exclude the ulama, whose connection with political reality had been weakened, for the sake of survival of the country whose existence, as mentioned earlier, was considered as the sole condition for the existence of all classes, including the ulama who had long been embedded in the state governmental bodies.

Iran also experienced similar developments in terms of the effect of the West and modernization. The rise of the intelligentsia which Bill (1981) for instance classify as up rooters, technocrats and manoeuvrers, was also a fact about Iran. However, due to significant key differences in de jure and de facto political power holders and the power balances among them, the two countries have chosen completely different institutional restructurings.

One very important example is again about the clergy class and how its de jure political power restructured. To be more precise, the year of 1826, was the turning point in the transition from military-oriented modernity to a more comprehensive politically-oriented modernization in which the status of the modern bureaucracy was becoming

elevated in internal political power relations in the Ottoman Empire. Modern-educated bureaucrats' perception on the country's development was that it was contingent upon the establishment of the rule of law, which would in turn provide the basis for legitimacy for modern administrative bureaucracy. Accordingly, the Ottoman Ulama was deprived of the authority of administration of the waqfs and in 1826 the Ministry of Foundations was established through which:

- management and supervision of waqf revenues were taken from the ulama
- funding was provided to be used for fiscal reforms
- the ulama's de facto political power was eroded

The year 1826 was also a milestone for the Iranian ulama, but in different terms. In this year the Iranian high ulama declared *jihad* on Russia, who had occupied Caucasian land and persecuted the Shiite community there and who had inserted its products into Iranian territory in advantageous conditions stemming from capitulations thus leading to bankruptcy of many Iranian merchants and craftsmen. With this declaration of war, the Iranian 'high' ulama was indeed proclaiming that they had the power even to shape the national politics (Momen, 1999 cited in Akyol, 2006). However, the above-explained lack of deep rooted institutional structure was an important factor shaping the general conditions for such a declaration: the collapse of the Safavid State left the country with communal conflicts and governance of two more dynasties in a period of approximately a half century. The Qajars were the third dynasty governing the country and thus the political authority was not deep-seated and was suffering from many weaknesses. William Cleveland (1993) demonstrates this weakness via highlighting the fact that the number of the government troops during this period was only three thousand and it was the tribal soldiers that were responsible in the provincial areas.

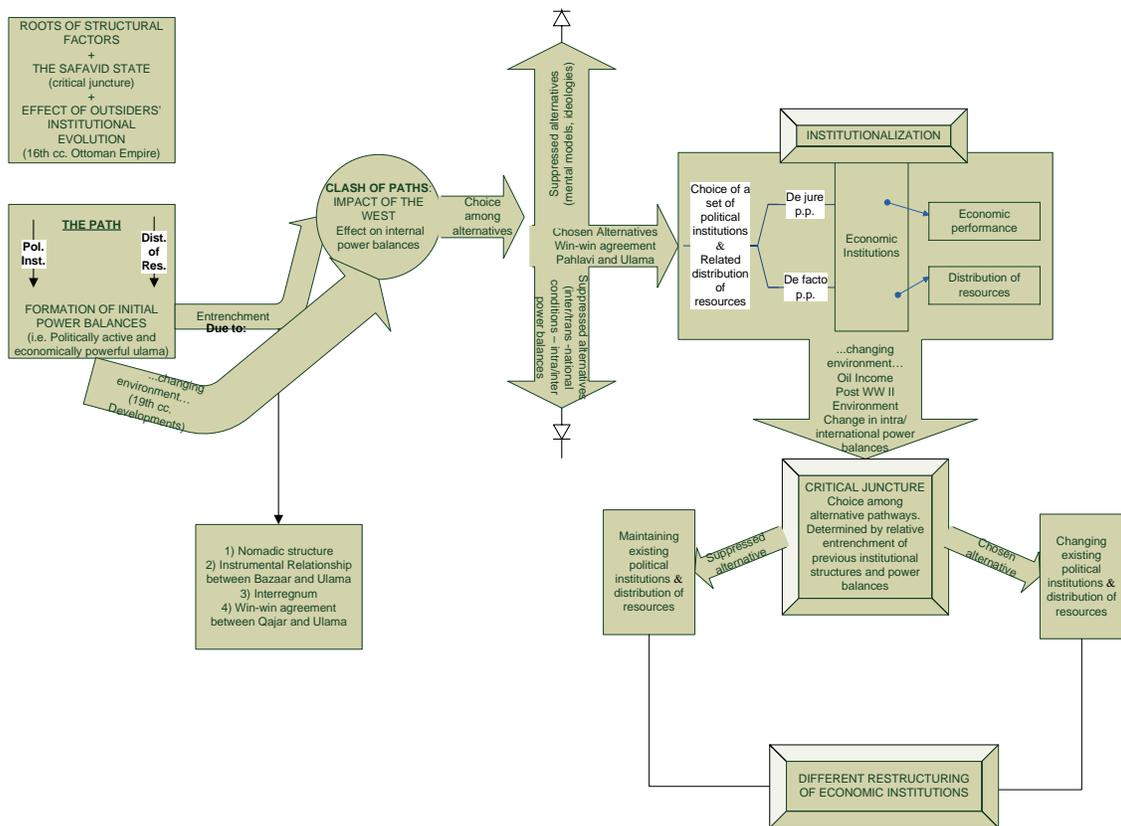
In line with these characteristics, we observe strong alliance between traditional power holders in opposing drastic changes in institutional structures and consecutive entrenchment of traditional networks and power balances in Iran as long as there was no conflict of politico-economic interests. It can be best seen in the famous Tobacco Protest (Keddie, 1966), in which when a tobacco regie was administered to England, tobacco producers, merchants and the ulama who was indirectly benefiting through taxes, formed a collective action and managed to cancel the regie. One factor that led to such a protest was related to one of the most important income sources of the ulama: the waqfs, most of which in that era were dependent on agricultural income leading the ulama to oppose large-scale commercialization. Interestingly, the Tobacco Regie was also applied in the Ottoman Empire, but the response was different: there was no protest but rather smuggling (Dogruel and Dogruel, 2000).

One of the reasons behind why the two countries responded differently to Western penetration, was that in an environment in which nationalism was on rise after the French Revolution and in the absence of a Turkish bourgeoisie, the Empire's subjects in money and trading business who belonged to non-Muslim minorities preferred to live

under the protection of one of the Great Powers, rather than to fight for a strong Ottoman state (Ahmad, 1993).

More importantly, both countries experienced a major event that was central in reformation of political institutions, associated distribution of resources, and thus political power balances: The 1906 Mesrutah of Iran and the 1908 Mesrutiyet of Turkey. However, the political power balances approach maintains that some formal institutional structuring may well function in a completely different way depending on who holds the de jure and de facto political power. This is what happened in our case countries: while the Constitutional Revolution occurred due to very similar reasons and almost at the same time in the two countries, it had completely different implications for the power balances, that is for instance, in favour of versus at the expense of the ulama. This, in turn, led to different formation and reformation of economic policies in these countries. The Mesrutah of 1906, for instance was supported by the Ulama in Iran, and from then on it has become impossible to cast out them from governmental institutions (Usur, 1992). In Turkey, on the other hand, Constitutional Revolution, which was supported by the Military and was the last point in the fall of the ulama and the rise of the intelligentsia, brought civil and soldier bureaucrats at the center stage. These restructurings, in turn, had profound effects on the choice of totally diverse institutional paths on the eve of 1980s.

Schema 2: The Clash of Paths – The Case of Iranian Institutional Transformation



7 An Application on Power Balances, Hegemonic Projects and Different Economic Institutional Restructurings: Ulama - Traditional Bourgeoisie versus Military – Modern Bourgeoisie Alliance

The twentieth century developments cannot naturally be elucidated in one section, but what is aimed to be done here is to demonstrate how diverse power relational dynamics in the two countries, that have their origins in prevailing political institutional restructurings explained in the previous section, in turn, determined the way the resources were distributed. Accordingly, on the eve of 1980s, depending on the relative power balances, how groups with de facto political power stemming from economic might and the ability to solve collective action problem, wanted to convert it to de jure political power which is considered to be more persistent compared to de facto power.

In view of that, being aware that the analysis seeks for the inclusion of some particular classes (e.g. the working class), it nonetheless, demonstrates an attention-grabbing finding on collective action formed between de jure and de facto power holders in the two countries during the course of capital accumulation period: That is to say, it appears that the high ulama – traditional bourgeoisies alliance in Iran and the high military – modern bourgeoisie alliance in Turkey were formed during the process of restructuring of economic institutions in line with the intra/inter power balances that stemmed from the effects of the changing world economic order.

To put it briefly, the twentieth century, following the World War I, was marked by the rise of the two leaders with soldier backgrounds, Riza Khan and Ghazi Mustafa Kemal and the establishment of Pahlavi Monarch and the Republic of Turkey. From then on both states would be characterized by military, modern state bureaucracy and state patronage. In the course of capital accumulation, furthermore, both Iranian and the Turkish states played an effective role in not only redistributing incomes but also in creating totally new economic classes. They both had a deep transformation program on their agendas. However both the state structures and the composition of the hegemonic groups and classes, which had had their roots in prevailing institutional structures, and hence their relationship with the state were thoroughly different in the two countries.

What is important in terms of power balances is that the Ulama in Iran gradually lost its de jure power within the New Order while the Military in Turkey, which had played a vital role during the last years of the Empire and in the process of the establishment of the Republic, with its growing de jure political power, increasingly intervened in the political processes during this period (see Table 1).

Table 1: Parliament Representation since the Constitutional Revolution in Iran and Turkey: Comparison of Occupations (in percentage)

| Occupation | IRAN | | | | TURKEY | | | |
|----------------------------|-----------|-----------|----------|----------|------------|-------------|-------------|--------------|
| | 1906-26 | 1926-41 | 1941-63 | 1963-79 | 1908-18* | 1920-60 | 1960-80 | Senate |
| Soldier | - | - | - | - | 5.6 | 9.56 | 5.21 | 14.63 |
| Cleric | 24 | 11 | 4 | 0 | 22 | 1.46 | 1.81 | 0 |
| Merchant | 15 | 16 | 13 | 10 | 2.4 (+) | 12.11 | 10.78 | 2.03 |
| Landowner | 39 | 57 | 57 | 35 | 21 | 10.65 | 9.12 | 3.29 |
| Government Employee | 44 | 39 | 46 | | 30 | 24.11 | 14.19 | 18.49 |
| Professional | 12 | 17 | 19 | | 19 (+) | 25 | 38.1 | 48** |
| Private Sect. | 3 | 2 | 2 | | | 9.35 | 3.91 | 6.30 |

Source: 1) *Cumhuriyet Donemi Turkiye Ansiklopedisi*
 2) *Bill, J.A. (1972)*
 3) *Ahmad, F and Dankwart A. Rustow (1976)*

* Data for the Turkey's 1908-18 period cover only the fifty percent of the parliament representatives due to lack of data on non-Muslim delegates. According to Ahmad and Dankward (1976) if this data could be obtained, the ratio of merchants would be much higher. This applies also to the ratios of professionals.
 ** 35 percent being lawyers and jurists.

Although occupational classification of parliament representation cannot provide us with clear-cut results due to different fragments of both societies generally used to be from more than one occupational category (e.g. the ulama in both countries in some instances belong to both the 'clerics' and the 'landowners' categories.), the table still has the ability to demonstrate some basic facts about transformation in power balances among certain classes and the state.

For instance, the drastic fall in the power of the Ulama with the establishment of the Turkish Republic is markedly demonstrated in the table. In Iran, on the other hand, there were negotiations that going on between the Ulama and the Shah during the establishment and the early period of the Pahlavi Dynasty, and thus although the table points towards a severe fall in parliament representation ratio of the ulama with the rise of the Pahlavi Dynasty, the case was not the eradication of the Ulama from domestic politics. More importantly, the ulama class in post-1920 Turkey is, indeed, classified under the categorization 'government employee' but for the sake of the comparative concerns their parliament representation ratios are demonstrated separately.

One may rightly ask why then the ratio of soldier representation in the parliament – apart from the fifteen percent in the Senate – was relatively low. In fact, the extent of the power of the Turkish Armed Forces is clearly defined in the Constitution of the Republic of Turkey along with its functions (e.g. influence in political affairs via the National Security Council) which indeed led more efficient ways of exercising and preserving power than representation in the Parliament.

Indeed, the Military in Turkey were perceived among the population as “the promoter and guardian of the Republic and democracy and it is an autonomous and neutral instance in the sense of being above-classes, above politics, above particularistic interests, so as to be able to represent the nation and the state as representative of the general interest.” (Akca, 2006) Interestingly, the Ulama in Iran, which is indeed one of the founding factors of the country and thus with de jure political power stemming from prevailing political institutions, was also regarded by a noteworthy portion of the population as defending the general interests of the country and the Iranian people.

More interestingly, however, both the high Ulama in Iran and the high Military officials in Turkey were indeed groups with also economic interests and thus deeply embedded in the process of capital accumulation through as a propertied class in the former and by means of a form of military complex OYAK (Armed Forces Pension Fund)⁹ in the latter. This process of being a part of the economic decision making was indeed strengthened via the alliance formed with the traditional bourgeoisie (the Bazaar), which emerged as a state-wide political force in the country as a response to the impact of the West in the nineteenth century, in Iran; and with the petit Muslim-Turk bourgeoisie that were created by the Union and Progress Party almost from scratch, but would rapidly become a powerful hegemonic class, in Turkey.

As we have already mentioned the roots, general characteristics and sources of income and thus de jure and de facto political power of the Iranian ulama, we will now shortly elucidate the main features of the Turkish military and analyse how it was embedded in the capital accumulation process in Turkey during the period studied.

The military, under different organisational structures in the case of Turkey through OYAK, became industrialist, merchant, financial investor and rentier. Although the phenomenon is not unique to Turkey, it forms one of the earliest and the most developed example of the occurrence of military capital.

OYAK is defined as a “financially and administratively autonomous legal person subject to the verdicts of private law.” On the other hand, article 37 reads that “all assets, earnings and accounts of the foundation are to be treated as state property, and any party causing damage to OYAK property will be treated as having damaged the state property.” OYAK also enjoys all kind of tax exemptions (corporation tax, turnover tax, income tax, stamp tax...) at the level of the Foundation (not at the level of affiliated companies) (‘OYAK Law’, Article 35)¹⁰. Indeed in Feroz Ahmad’s depiction OYAK can be classified as the “third” sector alongside the private and state sectors.

⁹ The phenomenon of ‘military capital’ is not unique to Turkey (some of the other examples are: China, Thailand, Egypt, Pakistan, Syria, Chile, Bolivia...). While in advanced industrial countries the military-industrial complex develops in the war industry, in several other countries it starts within the sectors of production and consumption goods. Through a military-industrial complex, the military acts as a collective capital group and becomes an economic actor at every moment of capital circulation (production, exchange, and finance).

¹⁰ ‘OYAK Law’ available at www.oyak.com.tr

The broad literature on OYAK agrees upon that OYAK functions as a collective capital group running productive, commercial and financial economic activities as much as or even more than being a social security organisation (Akca, 2004; Parla, 1998; Ahmad, 1993, Ozturk, 2010). Started with a very small capital around \$1000 in 1961, OYAK increased its investments to \$50 million in 1970 and by 1986 its capital was \$33 million following the other giants of Turkey such as KOC, SABANCI and CUKUROVA with capitals of \$52.3 million, \$47.8 million and \$38.8 million respectively (Ozturk, 2010). OYAK also increased its value of assets from \$4.871 in 1961 to \$20 million in 1972 (Ahmad, 1993). With regard to the profits, OYAK was the third biggest capital group in 1990 following KOC and SABANCI (Ercan, 1997).

The centrality of holding-like activities for OYAK may also be derived from the fact that the most important item among OYAK's revenues is its revenues from economic investment activities, which display both horizontal and vertical integration, and though concentrated in the automotive, cement and finance sectors, have been expanded to several sectors such as construction, food, transportation. In the period 1961-1974, 74 percent of the total budgetary profit of the Foundation originated from their profit-oriented investments (Akca, 2006).

Hence, OYAK's positioning within the big capitalist groups of Turkey, which are powerful in defining the course of accumulation strategies in a way that would most benefit themselves, is worth focussing in order to provide insights on different institutional reorganizations, from agriculture based development strategy to import substitution industrialization and further to export oriented industrialization and economic liberalization in Turkey. In order to do this, there is a need for considering the development of OYAK under different systems of accumulation so as to picture how the military through OYAK is deeply embedded into the class structure of Turkish capitalism and how it is embedded in accumulation strategies and the related social power balances.

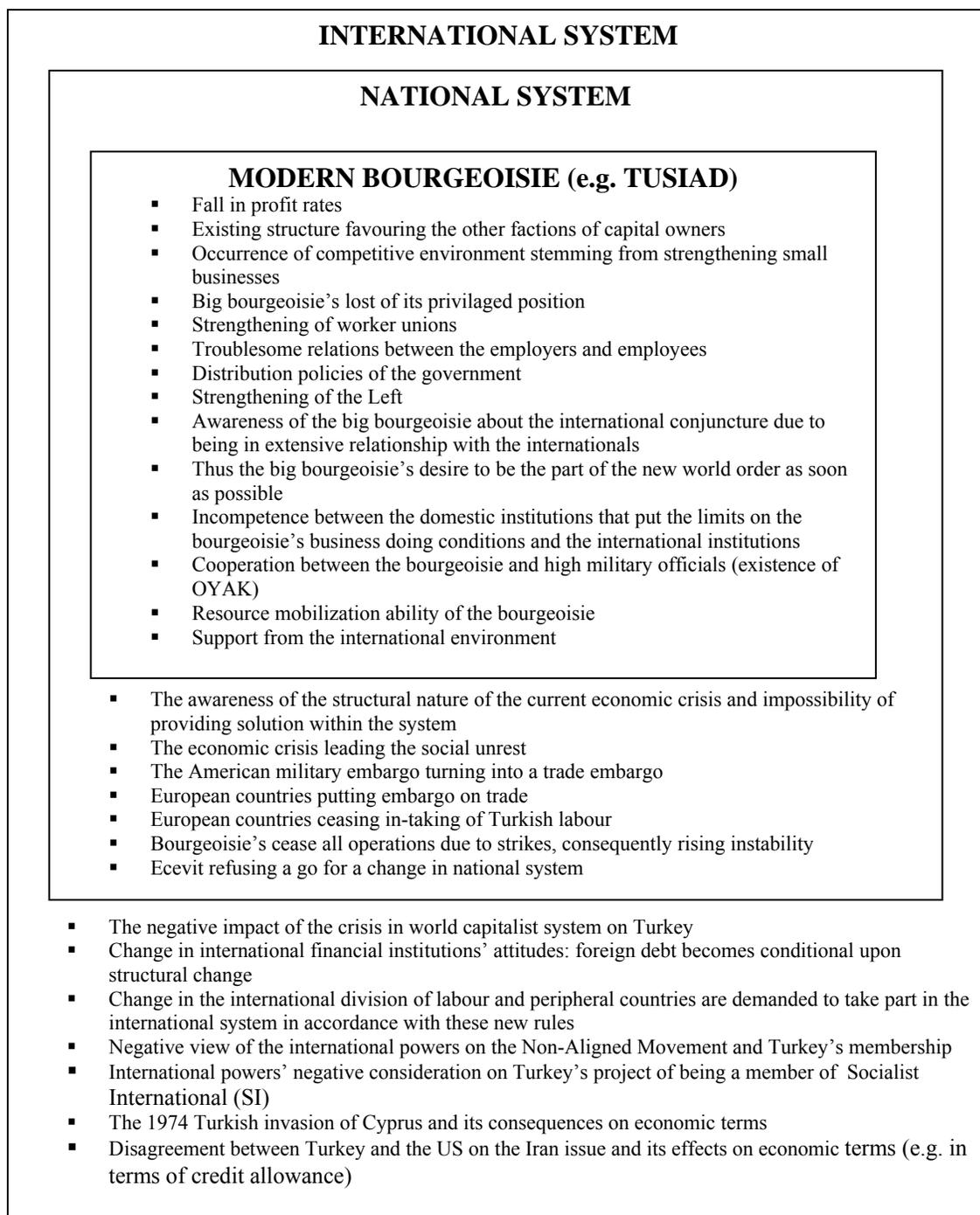
OYAK, during the period analysed, though was not a State Owned Enterprise, benefited from considerable state incentives. One example is the high protection that during the import substitution industrialization period OYAK enjoyed in the automotive sector, the entire of which OYAK was controlling together with KOC company. Quoting from Aksoy (1990): “[d]uring the ISI period, the industry of passenger-cars enjoyed the highest rate of protection (280.2%) within the overall manufacturing industry.”

However, the first crisis of the ISI led the Justice Party (AP) to implement an IMF Stabilization Program and a 66 percent devaluation. It in turn had a devastating impact on the automotive sector due to enormous increases in the prices of the imported intermediate goods. On top of it, a trading tax was enacted and as a result the sales drastically fell. Under these conditions, the Military's political-hegemonic as well as economic-corporate interests that had been gained via OYAK who was controlling the automotive sector together with KOC Company under the shelter of the import substitution policies were destroyed. What followed was the 1971 Memorandum. As Eder (1993: 291) states: “*The aftermath of the March 12, 1971...signalled the triumph of the import substitution industrialists and most importantly of the automotive firms.*”

Quoting also from Henry Barkey (1990: 115): “...[t]his industry’s long term stability and success was assured with the direct involvement of the armed forces.”

The Military-Big Bourgeoisie¹¹ alliance was also at stage on the eve of the Coup D’ Etat of 1980 and during the following period of the introduction of the economic liberalization policies. All associations were closed down or their activities were terminated during the period of Military rule apart from the Turkish Industrialists’ and Businessmen’s Association (TUSIAD), which on the contrary was awarded with the name “socially beneficial organization.”

Schema 3: Power Balances and Institutional Entrepreneurship (TUSIAD)

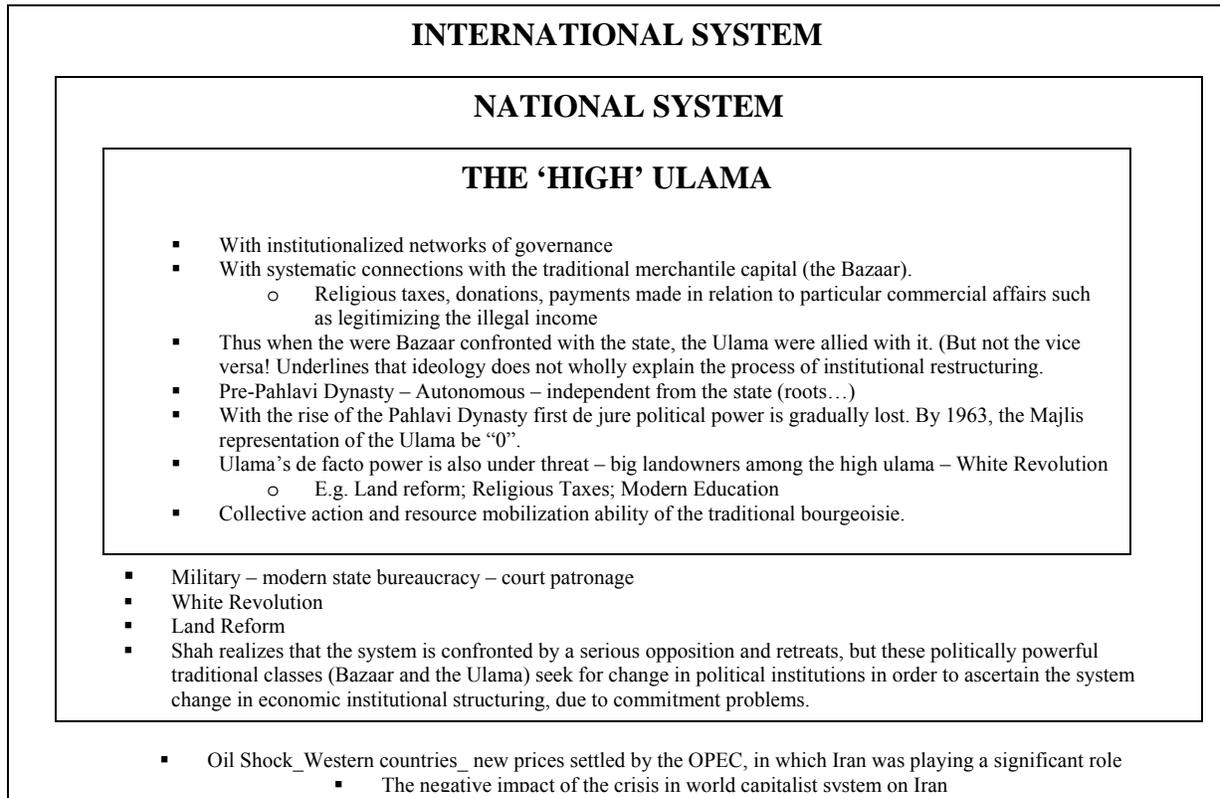


The 1960s, the years of import substitution industrialization also in Iran, were marked by impressive growth rates and a massive industrialization movement and were important for the traditional bourgeoisie of Iran, that is the Bazaar. Although the traditional mercantile capital was not under the state patronage, high growth rates and industrialization did not emerge at the expense of the Bazaar. This was mostly because Import Substitution Industrialisation was mainly financed by foreign debt and workers' remittances in Turkey (Boratav, 2003 and Pamuk, 2007) whereas in Iran the means of financing was the oil revenues (Issawi, 1970 and Katuzian, 1981). That is to say, the rising oil income, principally after the formation of the modern rentier state in Iran, radically altered the relation between the state and the economic actors. State's income generation procedure changed from customary methods to unusual means, which unsurprisingly had an effect on fiscal policies. At this precise point, because the process of state-directed formation of an industrial bourgeoisie was being financed by extraordinary oil revenues, the practice did not realize itself at the expense of traditional merchant trade. This is certainly a key point in that it provides the roots of one of the most influential economic groups in Iran, that is the Tehran Bazaar (Keshavarzian, 2007).

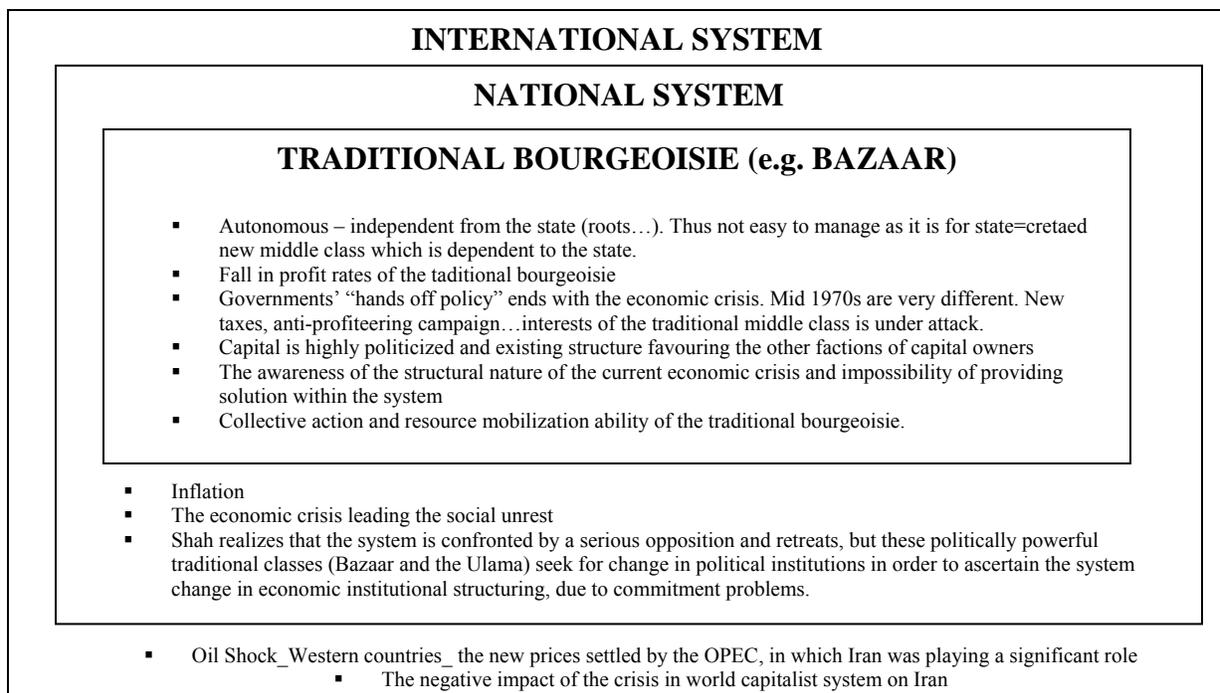
However, the de facto political power of the high ulama, whose de jure political power were eliminated as early as in the beginning of the Pahlavi Monarch, also came under threat due to White Revolution, which was devastating all income sources of the ulama due to particularly modern education movement and land reform attempt. Nonetheless, because the interests of the *both* groups were not deteriorated, a form of collective action could not be formed to change the economic institutional structuring, again highlighting the fact that the widely known ulama-bazaar alliance was not formed on the grounds of religious terms, underlining the insufficiency of the explanatory power of the ideology view once more time.

The post-Oil Shock period, however, marked a turning point in which the economic interests of the traditional bourgeoisie was also threatened by the state policies. This meant a formation of collective action in selecting among alternative pathways at this particular critical juncture (See Schemata).

Schema 4: Power Balances and Institutional Entrepreneurship (The Ulama)



Schema 5: Power Balances and Institutional Entrepreneurship (The Bazaar)



8 Conclusion

This study, starting from the proposition that institutions are all *choices* endogenous to natural experiments of history, analyses the roots of completely different institutional restructurings in Turkey and Iran on the eve of 1980s.

After an introduction of the four core approaches to institutional diversity across countries, it is gone through two interesting country cases, within which it is tried to be demonstrated that:

1. Although efficiency considerations are important for institutional formation, we cannot answer the question ‘why then some societies prefer growth-retarding institutions’ via the Efficient Institutions View.
2. institutions are not chosen solely because of their implications in terms of belief structures or ideologies
3. Nor institutions result from historical accidents as proposed by Incidental Institutions View, because although there is evidence that institutional choices persist, they are still choices, not simply dictated by history.
4. Institutions are not simply choices, but choices of politically powerful collective actors for their economic, generally distributional consequences.

In this context, institutional structures which can generally be described as relatively more socially beneficial are demonstrated to exist if:

- politically powerful also benefit from it
- there are relatively few resources to be exploited, thus reducing the tension of distributional conflicts
- constraints on political power prevent expropriation

However, it is also shown that in order to make sound interpretations on institutional evolution, the origins of political power should be thoroughly analysed. For the specific case countries of the current study, we dig deep in order to reach the sources of political power balances for Turkey and Iran. It is evidently observed for both countries that existing power balances indeed have their roots in the preceding political institutions and initial distribution of resources. Moreover, it also surveyed that although there are many factors effective in institutional evolution of the two countries (e.g. international environment since both countries are considered as open systems; the interaction between the national and the international system; and mental models), it is comprehensively revealed that if hegemonic classes solve the problem of Collective Action, they usually shape and reshape economic institutions in accordance with their interests.

Finally, we applied these theoretical findings on the institutional evolution cases of Iran and Turkey and discovered further attention-grabbing findings that are:

- a) The ulama in Iran has centuries old roots of de jure political power, in which the establishment of the Safavid State was the critical juncture

- b) The military in Turkey also as a founding factor of the country has roots of de jure political power
- c) The traditional bourgeoisie's and the modern bourgeoisie's de facto powers stem from specific features of these classes and their relations with the state
- d) State structures which are noticeably different from each other stand as the major reason behind different power relations and resulting institutional evolution.
- e) Co-evolutionary interactions among different national paths are also effective in reshaping institutional structures.

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