SECTORAL CREDIT AND INVESTMENT PATTERNS IN TURKEY: 1963-70

by

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Note

13 Turkish Lira (TL.) = 1 U.S. Dollar ($)

I. INTRODUCTION

The primary objective of this paper is to identify those factors responsible for the changes in the pattern of credit allocation in Turkey during the 1963-70 period. The role of financial systems in economic development and the weaknesses of Turkey's financial system are discussed in this section. Turkey's industrialization policy during the 1963-70 period is reviewed in Section II. The growth performance of sectors and sectorial investment and credit flows are analyzed in Section III. Conclusions and policy suggestions are presented in Section IV.

A. The Role of Financial Systems in Economic Development

The mobilization of savings is required for capital accumulation which is considered to be the basis of economic growth. Savings have to be collected from a wide range of sources and made available to investors. This involves a division of labor between savers, investors and intermediaries. This division of labor leads to the issue of primary securities by borrowers (investors) and the acquisition of financial assets by lenders (savers) [5]. Financial intermediaries attract savings by paying a deposit rate and allocate savings by charging a lending rate. The creation of a "finance economy" where people hold financial assets such as money, bonds, and shares facilitates the accumulation of savings and their allocation to the most productive investments [14].

The growth of output, increased commercialization, and the monetization of subsistence sectors influence the demand for the services of the financial sector. Patrick [8] argues that the faster the rate of growth of real output, the greater the demand for the services of intermediaries because the demand for borrowed funds is greater. He also states that the greater the variance in the growth rates of sectors, the greater the need for intermediaries to transfer savings to leading sectors. Therefore, the financial sector can support and sustain growth, and if it malfunctions, growth will be hindered.

There are a number of alternative techniques for eliciting savings and transferring them to investors. Some of these techniques such as self-finance and taxation involve more centralized decision-making and less specialization between savers and investors [5]. The debt-asset system, the financial technique, encourages division of labor, involves more decentralized decision-making, and depends on relative prices to guide economic behavior. In this sytem the market rate of interest plays an important role in mobilizing savings and allocating them to investment.

An alternative technique which is often used by less developed countries (LDC's) is inflation. As a technique of self-finance, inflation is used when other techniques of mobilizing resources have not been fully developed and when "relative prices tend to move perversely for the purposes of growth" [8]. In contrast to the debt-asset system, inflation is a more centralized technique and less conducive to specialization. It indirectly imposes a tax on financial assets such as money balances. This technique is less effective in those LDC's where only a small part of the economy is monetized and, therefore, the base of "inflationary tax" is small [6]. Furthermore, inflation can have negative effects on growth in LDC's.

Some industries and groups in LDC's are "protected" from inflation. Such "protection" usually consists of controls on prices of agricultural commodities, transportation fares, etc. Low agricultural prices inhibit the growth of the agricultural sector and other controls involve the state in subsidies and deficits. Under these circumstances the funds collected through the "inflationary tax" are spent on supporting consumption of certain sections of population rather than on investment. Secondly, as the rate of inflation fluctuates, businesses divert their resources to forecasting, speculating, and hedging. Finally, when LDC's maintain fixed exchange rates, inflation leads to the overvaluation of their currencies. The result frequently is protectionism with resources diverted to high cost import substitution and away from export industries [6].

Many LDC's suffer from deficiencies in their financial structure and are attempting to establish financial structures more conducive to their growth. The result has been a wide variety of financial structures at given levels of income and wealth as various combinations of taxation, inflation and other techniques have been used as substitutes for the debt-asset system.

The course of future growth is determined by the allocation of investment today. The goal is to allocate investment resources in order to provide the most rapid growth. But too often governments plan investment levels and allocations without ensuring the existence of necessary funds. With a debt-asset system investment decisions are affected by many factors including the interest rate and capital rationing. The interest rate affects the level as well as the distribution of investment among sectors. When the development of sectors is determined by government policy, it becomes necessary to provide sufficient funds to sectors that are to be encouraged. This frequently is accomplished by establishing special banks at the initiative of the government. These banks transfer resources to selected sectors and promote and stimulate entrepreneurial response in these sectors. Patrick [8] refers to these as "supply-leading" institutions.

In summary, there is a two-way relationship between economic growth and the financial structure. The financial structure influences growth because it affects the accumulation of savings and their allocation to investment while, on the other hand, growth stimulates the development of the financial sector by creating a demand for its services.

B. The Problems

The ratio of deposits to national income or the share of loans and advances to the private sector in national income are some of the criteria used to determine the development of the financial structure. In Turkey, the share of loans and advances to the private sector has increased from 20.6% in 1963 to 34.5% of national income in 1970.[1] This indicates that

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[1] Loans to the private sector by the banking system including the Central Bank were 11.3 billion Turkish lira (TL.) in 1963. National income stood at TL. 54.7 billion. In 1970, the volume of loans increased to TL. 40.7 billion while national income reached TL. 117.8 billion.

the financial structure is developing. Nevertheless, Development Plans and other studies have noted that the financial system is still relatively weak because most of the deposits are sight deposits held for their "moneyness."

The Development Plans mention the financial system as a factor in the failure of domestic savings to reach target levels. In both of the Five-Year Development Plan periods of 1963-67 and 1968-72, domestic savings were below planned levels. This creates serious problems for the private sector in particular. Most of the funds such as social insurance collections, Central Bank credits, and foreign loans are allocated by law or decree to public institutions [14]. As a result, only limited funds are available to the private sector. Securing loans from these funds is very difficult. The Second Five-Year Development Plan states that real estate worth about 200% of the credit extended is usually required as guarantee. Consequently, few enterprises can use the resources of the banks and have to rely on their own resources for finance. Burk [1] states that "in Turkey loans are based on collateral not profitability and the market favors the acquisition of inventories and real estate over working capital for the services of labor." A survey of 285 private enterprises shows that most funds for operating capital have to be obtained from sources other than banks.

One of the major difficulties of the private sector during the First Five-Year Planning period was to find medium-term loans. Banks made short-term low risk loans, but the Central Bank would not discount industrialists' medium-term bills. The Central Bank Law of 1970 aims at correcting this situation by allowing discounting of medium-term bills by the Central Bank and requiring that 10% of loans above a limit be medium-term credits. Fry [4] argues the failure to realize planned investment and achieve the desired allocation of private investment during 1962-67 was due to lack of financial planning.

Another problem of the Turkish financial structure is that interest rates are controlled. Deposit rates are very low whereas lending rates of banks can reach as high as 30% when service charges, taxes, and stamps are added [4]. On the other hand, loans to the public sector are made at symbolic rates. Yenal [14] states that most funds transferred to the public sector at less than market prices are once-and-for-all operations which do not add to financial assets but become signed documents.

The effects of these problems and the government's approaches to solving them will be discussed in the following section.

II. INDUSTRIALIZATION AND THE FINANCIAL STRUCTURE

A. Industrialization Policy in Turkey

Rapid industrialization has been the major objective of the Turkish government since the 1930's. Until 1960, industrialization policy was formulated in terms of industrial projects with no comprehensive plan coordinating them. After 1960, Five-Year Plans, the first one starting in 1962, were drawn. A target rate of growth of 7% a year was set for GNP and the Plans emphasized the need to change the structure of the Turkish economy from its heavy reliance on agriculture to industry. The change in the structure was to be achieved by registering the highest growth rate in the industrial sector.[2]

During the two Five-Year Planning periods of 1962-67 and 1968-72, significant changes took place in the Turkish economy. The share of the industrial sector in GNP increased while that of agriculture declined. However, the growth rate of the industrial sector has been below whereas that of services and housing has been above target rates. Consequently, the Turkish economy is now dominated by agriculture and services with agriculture accounting for 26% and services 39% of GNP in 1971.

The public sector has played an important role in Turkey's industrialization. Since the 1930's, the provision of infrastructure and the establishment of new industries fell on the government. Public investment accounted for 53% of total investment in these areas during the 1968-72 period. The government has been and still is very actively involved in all the sectors of the economy through State Economic Enterprises (SEE's). The

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[2]The industrial sector, as defined in the Plans, consists of mining, manufacturing, and the energy sectors.

basic problem of the public sector in carrying out its task in the industrialization of Turkey has been the lack of funds to finance target levels of expenditures. Target levels of tax collection could not be achieved and the government had to resort to deficit financing. In an economy where there is no capital market, this required borrowing from the Central Bank and resulted in an increase in the money supply.

The SEE's occupy an important role in Turkey's growth process. During the period 1968-72, 43% of total public investment was made through the SEE's. In particular, their contribution to the manufacturing sector has increased. At the end of the Second Five-Year Planning period, 38% of the investment made by the SEE's went to the manufacturing sector.

While most of government investment goes into infrastructure and heavy industries, most of private investment concentrates in small-scale family type enterprises engaged in simple processing or services such as transportation. After 1960, the share of private investment declined and its composition changed. The share of private investment going into housing has fluctuated around 30%. The share of investment in machinery and equipment declined between 1963 and 1970.

The Turkish development strategy has stressed growth through industrialization. Resources have been channelled to the industrial sector to stimulate its growth. However, the industrial sector in Turkey is still rather weak in that consumer goods industries dominate the sector.

B. The Financial Structure

"The financial structure of an economy is characterized by the composition of financial assets and the pattern of financial organization" [14]. Financial assets are all the intangible assets in an economy. These include currency, deposits, life insurance and pension claims. In Turkey, the bulk of financial assets consists of currency and deposits. In 1962, Yenal [14] estimates the share of currency and deposits to be 74% of total financial assets held by the non-bank public. As a result, he concludes that the banking system plays an important role in the financial structure of Turkey.[3]

Financial assets of the banking system, coins, notes, and deposits, play a dual role. They serve as the money supply and provide the source of finance for the economy. In Turkey, the Central Bank issues notes and the Treasury coins. Deposits fall into four classes:

1) official (deposits of government departments and state organizations)
2) interbank
3) commercial (deposits of legal entities: firms, corporations, etc.)
4) savings (deposits of individuals).

Deposits in each category can be either sight or time deposits.

The major institution in the banking system of Turkey is the Central Bank. It is a joint stock company with private and government-owned capital and subject to special law. The bank was established in 1931 and began operations in 1933. The functions of the Central Bank are to issue notes, establish the discount rate, regulate the money market and the circulating currency, take measures to stabilize the Turkish lira, carry out Treasury transactions, and help the economic development of Turkey jointly with the government [3]. The Central Bank can issue notes against gold, foreign exchange, government bills, and commercial paper. There are rules as to the amount of notes that can be issued against each of these assets, but the major determinant of the money supply in Turkey is government borrowing [14]. The Central Bank's obligations to the Treasury and to agricultural price support programs have reduced its effectiveness in controlling the money supply. The Central Bank Law of 1970 was designed to correct this situation.

The Central Bank provides credit to the SEE's, to agriculture, to industry, and to the Treasury. Most of the loans to the public sector are long-term loans and often become non-redeemable [14]. The Treasury can borrow freely and the SEE's can get credit on their Treasury guar-

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[3]Branch banking is practiced in Turkey.

anteed bonds. Loans to preferred industries by the Central Bank through rediscounting carry interest rates of 11-12% compared to market rates of 15-18% [7].

Some of the most important banks in Turkey in terms of their share in total credits are called Special Law Banks or State Banks. These are holding companies whose resources are either thei own capital or credits obtained from the Central Bank. Their assets are fixed assets or long-term credits [14]. The transactions of a few of these banks will be discussed below and reference will be made to them later.

The State Bank that specializes in agricultural credit with some help from the Central Bank is Ziraat Bankasi (Agricultural Bank). The agricultural sector receives almost all the credits it requires from this bank which also provides funds to agricultural cooperatives. Credit is provided by the Agricultural Bank for seed and fertilizer projects, agricultural export goods, and projects to reduce the influence of natural forces on agriculture. The most interesting feature of the Agricultural Bank is that although a State Bank, its resources are mainly deposits and its assets short-term commercial credits. In this sense it is more a commercial bank than a State Bank.

The only bank in Turkey specializing in loans to the housing sector is the Emlak Kredi Bankasi (Housing and Credit Bank). A small percentage of the credits of this bank are made at low interest rates. A depositor of TL. 10,000 who does not claim interest for two years is eligible for a TL. 30,000 loan at 6%.

Another Special Law Bank, Halk Bankasi (People's Bank), provides credits to small business and artisans. This bank gives credit to a large variety of enterprises whose need for loans differ a great deal.

In addition to State Banks, there are commercial banks and investment banks. Commercial banks come under the general banking act. Their resources are mainly deposits and their assets are short-term commercial loans [14]. Investment banks do not accept deposits and their resources are their own capital and loans from the Central Bank. There are three investment banks in Turkey: Sinai Kalkinma Bankasi (Industrial Development Bank), Sinai Yatirim ve Kredi Bankasi (Industrial Investment and Credit Bank), and Devlet Yatirim Bankasi (State Investment Bank). The first two lend to the private sector and the third to the public sector.

The Industrial Development Bank was established in 1950. Its resources, mainly foreign funds and domestic non-deposit sources, are used to make long-term credits to private industry. Loans made from domestic resources carry an interest rate of 8-9% while the market rate on bonds of similar maturity is 13-15% [7]. Similar purposes are served by the Industrial Investment and Credit Bank established in 1964.

The State Investment Bank established in 1964 provides credit to the SEE's. The interest rates charged vary between 5% and 7%. This bank is not bound by the credit law.

Insurance companies are part of Turkey's financial system. Although the number of Turkish and foreign insurance companies has increased, this has had little effect in increasing insurance assets. The Second Development Plan suggests that growth rate of life insurance companies declined during the 1960's. This is explained in terms of high premiums charged for life insurance and the uncertainty regarding the value of the insurance in the long run.

The First Development Plan stressed the need for a capital market. However, at the end of the Second Plan's implementation period (1972), there was still no true capital market in Turkey. There is a movables and stock exchange in Istanbul, and on a small scale, banks handle such services as selling and buying stocks. Yenal [14] estimated the volume of bonds and stocks in the Istanbul Bourse to be 10% of financial assets held by the non-bank public in 1962. According to the Second Plan, there has not been any considerable increase in the activities of the Bourse.

Of the institutions discussed so far, the Central Bank and other banks in conjunction with organizations lending under the provisions of Law 2279 make up the organized credit market in Turkey. In addition, there is an unorganized credit market that operates extensively [9]. In 1963, the net volume of credits by the unorganized credit market stood at TL. 3.7 billion. The very existence of this market indicates that the funds in the organized market are quite insufficient. In the next section, the sectorial credit flows are analyzed in detail.

III. SECTORAL INVESTMENT AND CREDIT: 1963-70

During the First and Second Planning periods, some sectors have grown at rates higher than target rates whereas others failed to perform as expected. The average growth rates of sectors over the period 1963-70 are given in Table 3.1. Agriculture and industry were the major sectors that did not perform well. On the other hand, the housing and services sectors grew faster than planned.[4]

Table 3.1. Annual average growth rates of sectoral GNP at constant prices: 1963-70.[a]

	Growth rates in percentages	
Sector	Target	Realized
Agriculture	4.2	3.3
Industry	12.0	9.1
Services	6.5	7.7
Construction	8.5	7.3
Transportation	8.5	7.5
Housing	5.9	7.9
Other	6.0	7.8

[a]Source: Turkiye Cumhuriyeti Basbakanlik Devlet Planlama Teskilati [13].

The allocation of public and private investment for 1963 and 1970 as well as the target allocation for both years are shown in Table 3.2. The most interesting observations regarding investment allocations are that, in both 1963 and 1970, agriculture failed to receive its target share while manufacturing and housing received much more than their planned allocations. It should also be noted that in accordance with the industrialization

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[4]Throughout this section, the analysis will be concentrated on agriculture, industry, housing, and services.

Table 3.2. Sectoral allocation of investment in percentages: 1963-70.[a]

Sector	1963 Target	1963 Public	1963 Private	1963 Total	1970 Target	1970 Public	1970 Private	1970 Total
Agriculture	17.7	16.1	11.8	13.8	15.2	13.6	8.9	11.4
Mining	5.4	6.6	1.7	4.1	3.7	5.0	1.4	3.3
Manufacturing	16.9	10.2	37.1	23.6	22.4	19.8	30.2	24.7
Energy	8.6	8.9	0.1	4.4	8.0	17.2	1.2	9.6
Transportation	13.7	28.1	4.0	15.7	16.1	21.2	11.3	16.5
Tourism	1.4	0.5	0.8	0.7	2.3	1.3	3.0	2.1
Housing	20.3	3.3	44.0	23.8	17.9	4.5	39.7	21.2
Education	7.1	12.9	0.2	6.3	6.7	8.1	0.3	4.4
Health	2.3	2.3	0.1	1.2	1.8	2.5	0.3	1.5
Other Services	6.6	11.1	0.2	6.4	5.9	6.8	3.7	5.3
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

[a]Source: Turkiye Cumhuriyeti Basbakanlik Devlet Planlama Teskilati [13].

policy, the target allocation for agriculture was reduced while that of manufacturing increased. A reduction in the share of housing was planned for 1970, but, as in 1963, realized allocation in this sector exceeded the target.

The information in Table 3.2 explains partially the growth performance of various sectors. The private sector dominates housing and the bulk of private investment goes into the housing sector. The influence of natural forces on agriculture and the failure of this sector to get its planned share in investment help explain its poor performance.

The failure of the industrial sector to reach its target growth rate is more difficult to explain. Manufacturing accounts for almost 90% of industrial value added. Manufacturing is dominated by import substituting industries which depend on imports of raw materials and intermediate goods. Table 3.2 shows that about 30% of private investment goes into manufacturing. In both 1963 and 1970, the investment target share of this sector is exceeded. The Third Five-Year Development Plan indicates that during the period 1965-70, there was considerable unused capacity in manufacturing.

In 1965, capacity use was 81%. The ratio fluctuated in the next two years and then declined to 69% in the first half of 1970. Excess capacity increased because sufficient raw material and intermediate goods could not be imported [13]. This prevented industry from reaching its target rate of growth in output.

The next step is to determine how the allocation of credit changed during 1963-70. Only bank credits, excluding the Central Bank, will be considered. The volume of credits and their composition for 1963 and 1970 are shown in Table 3.3.

Table 3.3. Credits by the banking system excluding the Central Bank: 1963-70 (billion TL.)[a]

Sector	1963	%	1970	%
Public Sector	1.725	14.5	3.209	8.7
SEE	.504	4.2	1.361	3.7
Other	1.221	10.3	1.848	5.0
Private Sector	10.161	85.5	33.796	91.3
Agriculture	2.408	20.3	9.030	24.4
Investment Banks[1]	.385	3.2	2.132	5.8
Housing	1.294	10.9	2.342	6.3
Small Business	.202	1.7	1.108	3.0
Others	5.872	49.4	19.184	51.8

[a]Source: Devlet Istatistik Enstitusu [3].

[1]After 1964 includes credits by the Industrial Investment and Credit Bank. Credits by the State Investment Bank are not included in this category.

The volume of credits by banks has increased considerably relative to 1963 and there have been some changes in the composition of credits. The share of agricultural and industrial credits has increased while that of housing has declined. However, in both years, the bulk of bank credits went to the trade and services sectors. These sectors require a large volume of short-term credits. In the two years under consideration, they have made utmost use of the resources of the banks. The allocation of the major portion of bank credits to short-term loans indicates that only limited resources are available for medium and long-term credits. There is little change in this situation between 1963 and 1970.

Table 3.4 shows the ratio of private sector credits to total investment in three sectors for 1963 and 1970. This ratio increases for agriculture and industry and declines for housing.

Table 3.4. The ratio of private sector credits to total investment: 1963-70.[a]

Sector	1963	1970
Agriculture	4.32	7.85
Manufacturing	0.21	0.54
Housing	0.59	0.45

[a]Sources: Devlet Istatistik Enstitusu [3].
Turkiye Cumhuriyeti Basbakanlik Devlet Planlama Teskilati [13].

Deposits are the main source of credit by banks.[5] In 1963, the volume of commercial and savings deposits in the banking system excluding the Central Bank was TL. 2.0 billion and TL. 6.6 billion, respectively.[6] In 1970, commercial deposits reached TL. 7.3 billion and savings deposits TL. 25.0 billion.

Of particular interest is the change in the volume of deposits at the State Banks specializing in credits to agriculture, housing, and small business and artisans. Investment banks that lend to industry do not accept deposits. The volume of deposits in the Agricultural, Housing and Credit, and People's Banks is shown in Table 3.5. Savings deposits at the Agricultural Bank increased by 281% during 1963-70. Commercial and savings deposits at the People's Bank show spectacular increases over the same period. Relative to these two banks, the Housing and Credit Bank has not been very successful in increasing its resources. Changes in the resources of these banks have clearly influenced the types of changes noted in Table 3.3. Namely, agricultural and professional credits have increased because

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[5]Interbank deposits and official deposits are not considered.

[6]Savings deposits in Turkey are deposits by individuals. They have sight and time components.

of large increases in the resources of banks making these types of loans. The decline in the share of housing credits can be associated with the relatively small increases in the deposits at the Housing and Credit Bank.

Table 3.5. Deposits at three selected banks: 1963-70 (in billion TL.)[a]

Bank	1963 Commercial	1963 Saving	1970 Commercial	1970 Saving
Agricultural Bank	0.434	1.661	1.200	6.100
Housing & Credit Bank	0.024	0.238	0.071	0.845
People's Bank	0.005	0.018	0.140	0.572

[a]Sources: Turkiye Bankalar Birligi [11].
Turkiye Bankalar Birligi [12].

The share of sight and time components of deposits is an important factor influencing the type of loans banks make. Table 3.6 shows the shares for the Special Law Banks only. Deposits in these banks account for almost 50% of total deposits. It seems likely that other banks show a similar breakdown of sight and time deposits. The sight component of commercial deposits is quite large and shows a small increase in 1970. The four-month component of commercial deposits increases while the two remaining categories almost preserve their share. The sight component of savings deposits shows a decline while the one-year and more-than-one-year components increase considerably.

Table 3.6. Composition of deposits at Special Law Banks: 1963-70 (in billion TL.)[a]

Duration	1963 Commercial	%	Saving	%	1970 Commercial	%	Saving	%
Sight	.451	77.0	1.900	79.0	1.500	78.0	6.200	67.0
4 Months	.005	0.8	.101	4.0	.063	3.0	.578	6.0
1 Year	.026	4.4	.228	9.0	.076	4.0	1.200	13.0
More Than 1 Year	.105	17.8	.184	8.0	.293	15.0	1.300	14.0

[a]Sources: Turkiye Bankalar Birligi [11].
Turkiye Bankalar Birligi [12].

The major portion of bank credits is short-term commercial loans. Banks apparently are reluctant to make medium and long-term loans when sight deposits constitute the bulk of their deposits. The increase in the time component of savings deposits in 1970 can be explained by the change in the structure of deposit rates. The maximum deposit rates prior to and after 1970 are shown in Table 3.7.

Table 3.7. Maximum deposit rates in percentages.[a]

Type of Deposit	Prior to 1970	1970
Sight and 4 Months		
a) Commercial	2.0	1.0
b) Saving	3.0	3.0
4-6 Months	4.0	4.0
6 Months - 1 Year	5.0	6.0
1 Year - 18 Months	6.0	9.0
More Than 18 Months	6.5	9.0

[a]Source: T. Iş Bankasi A. S. [10].

Interest rates in Turkey are set by law and tend to remain unchanged for long periods of time. Sight deposits also earn interest, but when these interest rates are compared to inflation rates, it can be seen that such accounts earn negative real interest rates. In 1963, the Istanbul cost of living index rose 4.7% and the Ankara index increased by 5.0%. Thus, all deposit accounts of less than six months were earning negative interest rates. The real rate of interest corresponding to the highest deposit rate was 1.5% to 1.8%. Such deposit rates would not have induced many people to hold money for any reason other than their "moneyness."

In 1970, a new deposit rate structure was established. The interest rate on commercial sight and four-month deposits was lowered and the rates for deposits starting with six months and over categories were increased. These high rates could have induced the increase in the time component of savings deposits in 1970. However, in terms of real interest rates, the new rates do not show much improvement. In 1970, the Istanbul and Ankara cost of living indices showed 8% and 10% increases, respectively. Using the Istanbul index only, deposit accounts of one year and over would earn positive real rates.

In Turkey, all banks pay the same rates on deposits. Therefore, other considerations must guide the decisions to hold accounts with particular banks. Yenal [14] has called attention to non-price competition which he says leads to the waste of resources in a system of controlled interest rates.

The final step of the analysis is to examine the lending rate structure. Lending rates determine the volume and allocation of credits. Table 3.8 shows the maximum lending rates prior to and after 1970. It must be remembered that these rates are set by law and do not change frequently. The rediscount rates at the Central Bank remained constant over the period 1961-69.

Table 3.8. Maximum lending rates in percentages.[a]

Types of Credits	Prior to 1970	1970
Central Bank Rediscounts		
General Rediscount	7.50	9.00
Agricultural Bills	5.25	7.50
Export Bills	5.25	7.50
Bills of Priority Industries	5.25	7.50
Artisans and Small Business Bills	5.25	7.50
Advances Against Bonds	10.00	11.00
Advances Against Gold	6.00	7.00
Medium-term Credits	--	9.00
Bank Loans		
General	10.50	11.50
Agricultural Credits		
General	9.00	10.50
Medium and Long-term	7.00	10.50
Export Credits		
From Bank's Resources	9.00	10.50
From Central Bank	8.00	9.00
Priority Industries	9.00	10.50
Small Business and Artisans	9.00	10.50
Medium-term Credits		
From Bank's Resources	--	12.00
From Central Bank	--	10.50

[a]Source: T. Iş Bankasi A. S. [10].

The Central Bank's rediscount rates were increased in 1970. This was part of numerous measures taken following the devaluation of the Turkish lira in the summer of 1970. Despite the increase in the rediscount rates, there has not been any change in the priority status of various credits. The most important change is the introduction of rediscounting for medium-term bills. Prior to 1970, medium-term bills of industrialists could not be rediscounted at the Central Bank. There were very limited resources availble for medium-term credits because banks preferred to make low risk short-term loans. Note that in 1970, lending rates on medium-term loans by banks were also introduced.

In 1970, lending rates for banks were increased. The rates shown in Table 3.8 are, however, not the effective rates. Agricultural, professional, and export credits are exempt from tax and stamp charges. All other loans are subject to these charges which at times increase the effective rate by up to 30%. There is also a subsidy system, but it does not cover the Industrial Development Bank and the Industrial Investment and Credit Bank where lending rates are already below market rates. Under the subsidy system, no subsidy is given if the bank uses Central Bank rediscounts for the specific loan.

Inflation lowers the real rate of interest below the nominal rate. The real rates on agricultural, professional, and export credits were very low in 1970 considering that inflation was 8-10%. This might have been an important factor in the large volumes of credit going into agriculture, trade, and services. A definite conclusion cannot be reached regarding other credits because effective rates on such credits are affected by the subsidy system, taxes, and stamp charges. Finally, inflation seems to have helped create a bias toward fixed investment by lowering the nominal rates on industrial loans supplied by the investment banks. Ongüt [7] reports that lending rates at these institutions are around 8-9%.

IV. CONCLUSIONS AND POLICY SUGGESTIONS

Over the period 1963-70, some significant changes have taken place in the patterns of sectoral credit and investment in Turkey. This study has been concerned mainly with four sectors: agriculture, industry, housing, and services.

During the period under consideration, agriculture failed to grow at the target rate and did not receive its planned share in investment. However, the share of this sector in total credits has increased due to increases in the resources of the Agricultural Bank. This sector has also benefited from tax and stamp charge exemptions on credits received. It appears, therefore, that the availability of credit has been a major factor that prevented this sector from achieving its planned share in investment. In other words, the volume of credits available was not sufficient relative to planned investment.

Industry was another sector that performed poorly in terms of growth. The share of this sector in total investment was greater than planned. This can be associated with the increase in the share of industrial credits. The industrial sector has also been helped by the establishment in 1964 of a second investment bank lending to private industries. In accordance with the industrialization policy, lending rates in investment banks have been lower than market rates.

The housing sector grew faster than planned and this sector received more than its planned share in total investment. However, the share of housing credits has declined. This could be due to the relatively slower increase in the resources of the Housing and Credit Bank. The importance of housing in private investment reflects the fact that real estate and small businesses are the major outlets for savings by individuals.

The growth rate of the services sector has been higher than planned. In general, this sector has received its planned share in investment. In certain sub-sectors such as transportation, realized shares exceeded planned allocations. The services sector benefited from the large increases in the resources of the People's Bank. Tax and stamp charge exemptions on professional loans have also been an important factor determining the volume of credit to this sector.

It can be concluded that the volume of credit and relative interest rates play an important role in investment decisions. Other factors such as the availability and cost of primary inputs, the supply of inputs from other sectors, and the availability of projects also influence investment, but credit availability, which, in turn, depends on the interest rate structure and the resources of the banks, appears to be the major determinant of investment.

The deposit rate determines the volume of resources and the composition of deposits in terms of sight and time components. In Turkey, the deposit rate affects the composition of deposits more than it does their volume. Over the period 1963-70, deposit rates remained constant yet deposits in the banking system increased. The time component of savings deposits increased in 1970 in response to the new rates.

In Turkey, the volume of funds in the banks and their composition play a more important role in credit extension than the price of credit does. Easy lending terms are available for agricultural sector. However, resources that are available are less than the amounts required for planned investment. Limited resources are available for medium-term credits since banks prefer short-term loans. This is influenced by the fact that the major portion of bank resources is sight deposits. The existence of an unorganized credit market also indicates the insufficiency of funds.

Policies in Turkey should aim at increasing bank resources. This can be accomplished by abandoning interest rate controls and letting the market mechanism determine the rates. If high interest rates emerge and their negative effects on investment are feared, fiscal measures can be adopted to stimulate investment.

Loans should be based on profitability of the project and not on the type of guarantee used. Lending rates should be determined by risk and duration. Tax and stamp charges on loans should be eliminated.

Finally, Development Plans should include consistency checks to ensure the availability of funds for planned investment.

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