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**Institutions, Corporate Political Strategies and Economic Development: The Cases of
Turkey and South Korea**

C. Emre Dogru

PhD Candidate, Political Science and International Relations, Koc University - Turkey

Abstract

While the causal link between institutions and economic development is well established in the literature, the role of firms in economic performance as determined by informal institutions remains to be explored. This paper argues that informal institutions in firms' political environment can be a mediating variable to explain how institutions cause economic differences among countries. The informal institutional environment influence firm behavior, which is a significant driver of economic development. This paper suggests three attributes of informal political institutions, namely perceived policy and regulatory commitment, the complementarity of formal and informal institutions, and a shared sense of purpose between public and private sector. The cases of Turkey and South Korea - two countries with similar formal institutional arrangements but different economic development paths - demonstrate the significant role played by informal institutions in firms' political environment.

Introduction

Significant differences exist across countries in terms economic development. The reasons that some countries get rich while others remain in the league of the underdeveloped or emerging market category is a fundamental debate in the literature. The explanations that are based on trade, geography and institutions attempt to clarify the causes that make a country

prosper. While the institutional theory has a more advanced research agenda, the exact causal links between institutions and economic development are still subject to debate. The literature indicates that there is a gap between firms as significant drivers of economic growth and their relation to institutional structures within the context of macroeconomic performance. This study aims to contribute to the literature by bridging this gap.

Recent years have witnessed a significant interest in the research on the interactions between firms and nonmarket actors. The corporate political activity and nonmarket strategy literature have covered the interactions between firms and governments in particular. Those studies asserted various findings on the impact on firm performance, the value of corporate political ties, firms' market value, as well as corporate resources ((Brockman, Rui, & Zou, 2013; Brown, 2016; Guo, Xu, & Jacobs, 2014; Peng, 2000; Sun, Mellahi, & Wright, 2012). Previous research demonstrates that firms are economic and political actors, whose actions have implications on other actors and on the ecosystem in which they operate. Firms' actions are determined by their institutional environment and their capabilities. But they also have the ability to influence the market and nonmarket dynamics.

According to North, "institutions are humanly devised constraints that structure political, economic and social interactions (North, 1991, p. 97)." Interactions among market actors are thus influenced by the institutional arrangements that those actors have developed as a result of certain historical contingencies (Acemoglu & Robinson, 2012). Following this rationale, I assert that firms' actions in response to their institutional environment have determining effects on macroeconomic performance. The market actions that drive economic growth can be categorized as investment, productivity, and innovation. Furthermore, the theoretical analysis of this study demonstrates that there are clear links between institutions and the growth-inducing actions.

Once the causal relationship between institutions and investment, productivity and innovation has been established, the question of which institutions have the most influence on those drivers becomes more critical. The literature on institutional theory provides insight into the importance of formal and informal institutions. Informal institutions are the fundamental rules of the game that affect the actions of players, and they put constraints on

firms in their market behavior (Chiu, 2015; Guo et al., 2014; Weymouth, 2012). In cases where there are changes in formal institutions, the influence of informal institutions becomes even more important due to their long-lasting impact. The incompatibility of evolution between formal and informal institutions is a critical factor that determines macroeconomic performance in transition countries. In most cases, formal institution building in the political environment does not lead to expected economic outcomes due to the constraints imposed by informal institutions.

The selection of Turkey and South Korea as the two comparative cases proves this point. Both countries have similarities regarding the political environment and institutional arrangements. However, their development paths have diverged significantly since the early 1960s. While the two countries had similar GDP per capita levels back then, today South Korea is among the most developed technology-driven economies, while Turkey has remained in the middle-income trap since 2008. The quality and governance of institutions had a significant impact on the conditions that have created the economic imbalance between the two countries ((Acemoglu & Ucer, 2015; Erdogdu, 2000). However, the research shows that the real difference is in informal institutions rather than formal ones.

This study, therefore, focuses on uncovering the difference in informal institutions between Turkey and South Korea with the aim of providing an alternative explanation for the divergence in their economic development. In other words, the significance of informal institutions is suggested as the mediating variable in the causal mechanism between institutions and economic development. Since informal institutions are difficult to clarify and measure, this study adopts a deductive research strategy. By reviewing the existing theoretical framework, I deduct three propositions on informal institutions that can allow us to understand the causes of economic difference between these two cases that have similar formal institutional arrangements. Those propositions are “perceived policy and regulatory predictability,” “complementarity between formal and informal institutions” and “a shared sense of commitment by public and private sectors to national development goals.”

This paper is structured as follows. In the first chapter, I discuss various theories on the causes of economic development, with a particular focus on institutional explanations. Next, I

attempt to clarify how institutions precisely determine business by exploring the new institutional economics literature. In the last section of the first chapter, I discuss how the firm can be incorporated into the institutional development debate and examine the contributions of varieties of capitalism literature in this regard. The conclusion of the first chapter clarifies the theoretical gap this study aims to fill. In the second chapter, I discuss the conceptual framework that will allow me to explore the question. I first review how institutions determine firm behavior in the market and nonmarket areas. Next section discusses advances our theoretical understanding of how institutions affect economic development by influencing firms' actions. The third section of the second chapter goes on discussing the importance of informal institutions. Finally, I suggest an alternative explanation to the impact of informal institutions with firms' growth-inducing actions. The third chapter explains why Turkey and South Korea are the appropriate cases to study the question. As briefly discussed above, the two countries are similar regarding formal institutional arrangements but different regarding economic development since the 1960s. The idiosyncrasy of these two comparative cases allows me to discuss the explanation on informal institutions in the next chapter. The fourth chapter is thus dedicated to exploring the historical empirical evidence. The purpose of the empirical discussion is not to provide the complete story of development in two countries (which are already existent in the literature), but to study the three propositions suggested in the theory chapter. The final chapter draws general conclusions and provides suggestions for further research.

1. Literature Review

1.1. What causes economic development?

The causes of economic development and differences across countries is a well-established research area in the literature. This section compares different theories and explores institutional theory with regards to some questions in the field.

There are three main theories that attempt to explain why some countries are rich and others are poor: trade, geography, and institutions (Rodrik & Subramanian, 2003). Trade, also known as integration, the literature suggests that globalization and trade drive economic convergence. Geography-driven explanation asserts that some factors such as climate, natural resources, transportation costs, agricultural productivity and diffusion of technological

advancement are the main causes of economic growth. Sachs (2003) finds that malaria disease, in particular, has a strong effect on per capita income. According to the geography hypothesis, geographic factors shape incentives of individuals (Acemoglu, 2003; Diamond, 1997). The institutional theory seems to have a more advanced research agenda. Previous studies demonstrate that institutions override other explanations regarding causing economic development ((Acemoglu & Robinson, 2012; Rodrik, 2004; Rodrik & Subramanian, 2003). Most evidently, when institutions are controlled for, “integration theory has no direct effect on incomes, while geography has at best weak direct effects (Rodrik, Subramanian, & Trebbi, 2002, p. 4)” In other words, the fact that institutions matter for economic growth has become an unequivocal statement (Klein, 1998; Rodrik, 2000; Shirley, 2008). This, however, does not mean that there is no interaction of institutions with other factors, especially with geography (Sachs, 2003). It’s often presumed that geography could have made the introduction of certain institutions possible, establishing an indirect link with economic development (Acemoglu, 2003)

Despite the robust and positive effect of institutional quality on economic growth, the questions of causality and endogeneity still beg a definitive answer. The literature suggests that the link can be established in both directions, meaning that institutions are both causes and results of economic growth, as they are also shaped by the actors’ behavior in the economy ((Nye, 2008; Rodrik, 2004). Thus, institutional theory presumes a mutual reinforcement mechanism that takes place between institutions and economic growth. Bruinshoofd (2016) asserts that it is primarily the institutions that lead this virtuous circle. By creating a growth-inducing environment, institutions provide the conditions where economic actors engage in activities that result in development.

Nevertheless, institutions are not seen as preconditions or indispensable triggers of economic growth (Engerman & Sokoloff, 2008; Rodrik, 2004). While institutional transformation does not necessarily initiate an economic spurt, it plays a significant role for sustaining it (Acemoglu & Robinson, 2012). Therefore, emergence and evolution of institutions are central to understanding their determining effects on the economy. The scholars of institutional theory contend that there is no predetermined path to a certain institutional arrangement (Acemoglu & Robinson, 2012; Rodrik, 2000). Rather, institutions seem to emerge as a result of historical

contingencies, which both create and are created by certain political, social and economic drivers. While discussing these specific drivers are beyond the scope of this paper, some degree of equal opportunity, political competition, and constraints on the rulers are suggested as the main causes of growth-inducing institutions (Shirley, 2008). A similar ambiguity persists regarding institutional evolution. The literature provides neither a definitive recipe for how institutions change, nor a tendency that they will evolve toward better arrangements (Acemoglu, 2003). Moreover, institutional change becomes problematic given that those who have the power to establish a certain institutional setting, including abusive ones, would also have an interest in maintaining them, especially given the lack of collective interest and information by those who are abused (Nye, 2008).

Having asserted that institutions are the primary drivers of economic development and discussed questions on causality, endogeneity, emergence and evolution of institutions, we can now explore what institutions are and how they exactly determine economic activity.

1.2. Why institutions matter and how exactly they determine economic activity

Institutions are created by social actors to meet certain needs. Borrowing North's (1991) definition, "institutions are humanly devised constraints that structure political, economic and social interaction." Exploring this definition provides some insight into why institutions exist. North's definition tells us that the institutional mechanisms, which are designed by humans, aim to intervene in humanly interactions to establish a certain environment (Nye, 2008). Therefore, understanding why interactions require self-imposed constraints is key to establishing the exact link between institutions and economic activity.

Institutions set the rules of the game, where constantly actors interact with each other (North, 1990b). Such institutions can be formal such as laws, regulations, constitutions, or informal such as beliefs, culture, and codes of conduct (Menard & Shirley, 2008; O. E. Williamson, 2008a). Past research shows that the focus on rules and enforcement mechanisms derive from the past failures in economic development programs that lacked institutional component, especially in the aftermath of World War II (Nye, 2008; Peter Murrell, 2008). As a result, the modern market economy rediscovered the "embeddedness" of markets in political and social relations, which meant that markets were far from being self-regulated and required

intervention to avoid failure (Polanyi, 1944). Accounting for the centrality of human interactions makes it possible to forcefully integrate institutions within the neo-classical economics and development literature (Zimbauer, 2001). Thus, understanding the role of institutions and their implications on economy necessitate interdisciplinary research that involves contributions from various disciplines (Joskow, 2004).

The New Institutional Economics (NIE) literature aspires to meet this scholarly need by exploring the determinants of institutions and their impact on economic performance (L J Alston, 2008; Nye, 2008). It provides an institutional response to transaction problems caused by human interactions while they engage in economic activity. In general terms, institutions create an environment by providing incentives and placing restrictions on economic actors, which determine their behavior based on expected utility (Acemoglu, 2003; Bruinshoofd, 2016; North, 1991; Soysa, 2007). It is, therefore, necessary to get a better understanding of how and which transaction costs should be reduced to create a growth-inducing economic environment (L J Alston, 2008).

Economic growth is closely linked with how actors behave. Actors make decisions and make market exchanges under uncertainty and complexity (Klein, 1998). Contrary to the assumptions of neo-classical economics, they have incomplete information and limited cognitive capacity (Menard & Shirley, 2008). It, therefore, follows that growth occurs to the extent that a stable institutional environment reduces costs of uncertainty and complexity (North, 1990a, 1991). Coase's (1937) seminal article provides the philosophical background that formal and informal institutions are primarily devised to reduce "the cost of doing business (Soysa, 2007, p. 7)." Institutions support the market economy and incentivize actors to engage in economic activity by decreasing transaction costs and protecting property rights (Nye, 2008; Platteau, 2008; Shirley, 2008). The degree of transaction costs, whether caused by information asymmetry or risk of expropriation, determine market competition and the conditions that are conducive to economic growth (Acemoglu & Robinson, 2012; Dumludag, 2007). The central role of nonmarket institutions is, therefore, to provide trust and predictability in the market environment (L J Alston, 2008; Joskow, 2004). Economic growth and investment take place where contract enforceability is assured, and property rights are enforced (Knack & Keefer, 1995; Oppen, 2008; Shirley, 2008).

The next section will review the role of the central actor in the market: the firm.

1.3. Bringing the firm back in

The institutional analysis of economic development makes it necessary to explore the role of the firm as the main actor that engages in economic activity. As we have discussed, the determining effects of the institutions on the economy are mainly based on their ability to lower the transaction costs. In addition to the institutional arrangements that influence the development at the macro level, the theory also takes a deeper look into the specific actors and how they govern their relations. One such actor is the firm. Coase (1937) has developed the transaction cost approach to the theory of the firm. The NIE considers the firm as an organization, and Coase asserts that not only productive capabilities but also costs of transacting business creates a boundary (Klein, 1998). Such costs include search and negotiation, monitoring labor effort, coordination of production, monitoring the use of physical and financial capital and enforcing the terms of the contract (L J Alston, 2008). Critical to this view is its implication that contrary to neoclassical tradition, firms cannot be considered as black boxes that merely arrange the production functions, but rather governance structures that assume the tasks of information and enforcement (Joskow, 2004; North, 1990; O. E. Williamson, 2008b). Therefore, how firms manage their strategic interactions (both inside and outside the firm) is a central topic of institutional theory.

The literature on Varieties of Capitalism (VoC) “brings the firm back into the center of the analysis of comparative capitalism (P. A. Hall & Soskice, 2001, p. 4).” The literature posits a direct link between the aggregate behavior of firms and macroeconomic performance. Firms are relational organizations, and their ability to manage their internal (employees) and external (customers, suppliers, governments) relations is the main determinant of its competitive capability. The interactions between institutional arrangements and relational behavior of firms is a differentiating factor across national economies (Dore, Lazonick, & Sullivan, 1999). Firms as organizations and their managers engage in an activity and also become the agents of institutional change.

The central role of the firm notwithstanding, five spheres where firms face coordination problems with other actors are limited to (1) industrial relations (2) vocational training and education (3) corporate governance (4) Inter-firm relations (5) Employees (P. A. Hall & Soskice, 2001). Lacking in this analysis is how firms manage their relations with the institutions in their political environment, which is presumably a strategic interaction that both influences the economic activity of the firm and economic performance of countries. The next section will discuss why firm's political environment matters.

1.4. The missing institutional link: firms' political environment

The literature review above demonstrates that institutional arrangements have determining effects on economic development, which occurs as a result of its influence on the behavior of economic actors, mainly firms. Macroeconomic performance tends to be robust in market environments where the firm is provided with incentives as result of the existence of institutional constraints that lower transaction costs and protect property rights. A major driver of institutional arrangements that shape the economic environment, namely the political dynamics with regards to business activity, are thus worthy of exploration (Engerman & Sokoloff, 2008).

Despite the increasing interest in the field, the institutional aspect of firms' political environment and its impact on economic growth remains to be studied in detail. The corporate political activity and nonmarket strategy literatures have an extensive body of knowledge. Most research have focused on the impact of firms' political behavior on its performance (Busch, 2016; Hillman, Keim, & Schuler, 2004; T. Lawton, McGuire, & Rajwani, 2013; Peng, 2000; Rajwani & Liedong, 2015; Saner, Yiu, & Sondergaard, 2000; Shaffer, Quasney, & Grimm, 2000), how firms develop and implement political capabilities (Brown, 2016; Doh, Lawton, Rajwani, & Paroutis, 2014; Griffin & Dunn, 2004; Hadani, Dahan, & Doh, 2015; T. Lawton, Rajwani, & Doh, 2013; Mellahi, Frynas, Sun, & Siegel, 2016; Vining, Daniel, & Bernhard, 2005), and as well as the interaction between market and nonmarket activities (Baron, 1995, 1997, 2001; Funk & Hirschman, 2017; Kingsley, Vanden Bergh, & Bonardi, 2012; T. C. Lawton, Doh, & Rajwani, 2014).

Those studies provide a comprehensive perspective from resource-based view. However, they do not explain the role of firms' coordination problems with political institutions in relation to economic performance. This is key consideration given the fact that formal and informal political institutions have a significant influence on how firms perceive transaction costs of engaging in economic activity. Therefore, the theoretical gap that needs to be filled is how the institutional arrangements - particularly informal institutions - in firm's political environment determine macroeconomic growth by determining firm's economic activity.

2. The Theoretical Framework

By deducing relevant concepts from the existing literature, this chapter builds a theoretical proposition that would help explain the research question. The sections below demonstrate that institutions in firms' political environment structure their market strategies in mainly three areas - investment, productivity, and innovation -, and thereby influence the macroeconomic development of countries. The study further reveals that informal institutions, in particular, have strong determining effects on firm performance. Therefore, in the last section, I suggest three propositions on informal political institutions that will be empirically discussed and analyzed in the fourth chapter.

2.1. An institutional view of firms' political environment

The scholarship on firms' political environment has an increasing focus on the institutional perspectives, especially with the growing importance of business - government relations in emerging countries (Doh, Lawton, & Rajwani, 2012). Institutional arrangements influence the political behavior of firms (Zhilong Tian, Hafsi, & Wei Wu, 2009). They try to shape either their institutional environment or their organizations according to the constraints and opportunities in the nonmarket area. Institutions are also considered as the main drivers that determine firms' capabilities to leverage resources for competing in the market area, by setting the rules of the competition via regulations and policies. As with many other actors, firms respond to institutional incentives and constraints. They make strategic choices regarding how to manage their political environment, based on the specifications of the institutional arrangements and internal capabilities (Peng, 2003).

Firms' strategic choices are explored through the lenses of resource dependency and institutional theory perspectives (Griffin & Dunn, 2004; Oliver, 1991). Resource dependency studies the way that firms allocate and exploit their organizational capabilities. The institutional theory provides insight on whether and how firms conform with their institutional environment. The effectiveness of firms' strategies in response to institutional arrangements in the political environment is thus determined by the combination of internal and external constraints (Oliver, 1991). Firms are organizations that are in constant interaction with their environment to exploit the opportunities provided by the institutions (Eising, 2007; Stopford, Strange, & Henley, 1991; Taylor, 2012). But their interactions also influence how those institutions will evolve (North 1990). Since policymakers also have incentives to respond to corporate interests by making institutional changes, institutional arrangements are also endogenous factors of the "political market" (Hillman & Hitt, 1999; Keim, 1981; Lord, 2000).

Since firms are both demanders and suppliers of institutional arrangements in the political environment, the way they interact with their environment is central to our study. Weymouth (2012) argues that firm heterogeneity, including size and market power, as well as regime type, determine the motivations and degree of influence they have on the formal and informal institutions. Firms allocate internal and external capabilities, such as boundary-spanning responsibilities for the public affairs department and building alliances with other stakeholders shape "the rules of the game" to improve their competitive advantage (LJ Alston, 2008; Doh et al., 2012; North, 2008; Peng, Wang, & Jiang, 2008; Spiller & Liao, 2008). A core capability is firms' managerial ties, especially during critical times such as institutional transition and crisis situations (Acemoglu, Johnson, Kermani, Kwak, & Mitton, 2013; Guo et al., 2014; Peng, 2003). While there appears to be a causal link between managerial ties and firm performance, past studies also suggest that such a link is highly contingent on internal resources, such as ownership, business sector, firm size and industry growth, as well as external arrangements such as environmental uncertainty, market conditions, international regulations and institutional quality (Brockman et al., 2013; T. Lawton, Lindeque, & McGuire, 2009; Peng, 2000; Sun et al., 2012).

Institutional environment structures how firms decide on their corporate strategy. For this reason, there are systematic differences in how firms' governance structures are organized,

managerial decisions are made and whose interests are prioritized (P. A. Hall & Soskice, 2001; Yoshimori, 1995)). Institutions also determine whether firms will recur to market relations or strategic interactions to overcome coordination problems and transaction costs (P. A. Hall & Gingerich, 2009). Such nonmarket institutions have direct impact on firms' business decisions that not only determine their own performance, but also that of market economy (Bakir, 2014; Brockman et al., 2013; Chiu, 2015; Rodrik, 2000).

The next section will explore in detail how formal and informal institutional arrangements determine firms' strategic choices that possibly explain economic differences across countries.

2.2. How institutions influence firms' impact on economic development

Firms make business decisions to grasp the market opportunities, based on the analysis of their institutional environment and organizational resources. Such decisions have an aggregate effect on the economic growth. The literature suggests that three spheres of firm activity, namely investment, innovation, and productivity. This section explores the causal link between institutions, and macroeconomic performance determined by firm behavior in these spheres. The assessment below demonstrates that growth-inducing activities of firms are driven mainly by the quality of informal institutions.

Investment is arguably the most significant business activity that influences long-term macroeconomic performance, and also requires institutional stability and predictability to create an enabling environment (Bruinshoofd, 2016). Previous studies show that institutional variables have direct determining effects on inward and outward FDI (Dumludag, 2007; Stoian, 2013). Since investment usually involves sunk costs and the expectation of incremental returns, firms try to gauge the institutional quality in a wider time-span. Innovation is another business area that significantly determines economic growth, but it also includes a significant degree of uncertainty regarding the business return (Teece, Peteraf, & Leih, 2016). Thus, the quality of formal and informal institutions become even more influential in the face of innovative uncertainty (Bruinshoofd, 2016; Lee & Law, 2016). The structure of the market economy determined by the institutions is also a critical factor in innovation capacity. Based on the dichotomy between liberal market economy and coordinated market economy of the

Varieties of Capitalism literature, Hall and Soskice (2001) claim that coordinated market economy supports incremental innovation, while Witt and Jackson (Witt & Jackson, 2016) assert that radical innovation occurs where institutions combine specific liberal and coordinated elements. A core argument of their study is that radical innovation provides countries with higher comparative advantage. Productivity is also a major driver of economic development through larger output per worker (Heilbroner & Milberg, 2011, p. 112). The economic differences across countries mainly stem from differences in labor productivity caused by “local social environment (Clark, 2009, p. 322; R. E. Hall & Jones, 1998).” (Previous studies show that firms perform better in certain kind of activities and increase efficiency in productive processes depending on the institutional environment, which allows them to accumulate capital and social skills (Doh et al., 2012; P. A. Hall & Soskice, 2001).

It is critical to understand what kind of institutions have such fundamental effects on firms’ investment, innovation, and productivity. The literature suggests various variables that determine firm behavior are mostly related to informal institutions. The first and most impactful institution is the political commitment, which directly affects investment and trust in public reforms (Rodrik, 1991). Past research found that political risk has a negative relationship with FDI (Khan & Akbar, 2013), though Busse and Hefeker (2005) argue that only a few indicators such as stability, law and order, and quality of the bureaucracy are statistically significant. The credible commitment by the political institutions, such as regulatory predictability and lowering transaction costs are important for investment decisions (Cetin, n.d.; Cicen, 2016). Bakir (2014) asserts that state capacity is a key factor in investment bargaining between multinational firms and state. His findings show that stronger state capacity leads to higher probability of investment. Productive entrepreneurship and innovation are also highly correlated with informal institutions that create social capital and trust, as well as information sharing (Rauf, 2009; Salimath & Cullen, 2010). Lee (2016) claims that in addition to the existence of formal institutions, social capital is critical to “promotion of knowledge sharing and creation of ideas” to increase innovation capacity of firms and countries.

This section examined the relation between institutions and growth-inducing firm activity and underlined that informal institutions are key determining factors that explain differences across countries. The next section will explore the informal institutions in detail.

2.3. The Impact of Informal Institutions

Informal rules are significant drivers of human interactions. According to North (1990), informal institutions structure business activities by defining “codes of conduct, norms of behavior and conventions.” Formal institutions might be considered more stable and predictable. However, interactions that take place between organizations are embedded in the social context and require informal institutions (Fafchamps, 2017). Even though people’s behaviors are motivated by both formal and informal institutions, the importance of informal institutions are often neglected due to the difficulty to identify and measure them (Soysa, 2007). Despite the fact that informal institutions are not as discernible as formal institutions, their impact on cross-country differences can also be measured (Knowles & Weatherston, 2006).

We have discussed in the previous section that institutions have a direct and significant impact on firm behavior, as well as on macroeconomic performance. The literature on informal institutions shows the critical role of informal institutions regarding this matter (Marosevic & Jurkovic, 2013). The existence and strength of informal institutions can lead to higher levels of factor productivity and increase the income per capita, by encouraging cooperation and reducing transaction costs (Knowles & Weatherston, 2006). The use of informal institutions, such as trust-based networks and relational assets, can replace the role of formal institutions and drive firms towards more risk-appetite activities (Salimath & Cullen, 2010). Same dynamics also affect firms’ nonmarket strategies, especially in the area of corporate social responsibility, which is closely tied with local informal institutions such as cultural attributes (Keig, 2013). Peng (2000) argues that informal institutions facilitate economic exchange and improve firm performance despite weaknesses in formal constraints, such as laws and regulations. According to Williams and Vorley (2015), formal institutions will not have any significant impact on fostering entrepreneurial activity, unless informal institutions are also taken into consideration by policy-makers. Thus, previous studies demonstrate that informal institutions are key drivers of economic performance (P. A. Hall & Soskice, 2001).

The interaction and evolution of both formal and informal institutions are central to understanding their effectiveness on the economy. According to North, formal institutions are the crystallization of informal ones and they co-evolve according to activities of organizations, such as firms (Casson, Giusta, & Kambhampati, 2010). Previous studies show that even though formal institutions can be transplanted in other countries with the goal of imitating development of advanced countries, the results would be significantly different unless they are grounded in established informal constraints (Pejovich, 1999; C. R. Williamson, 2009). Even though the rules might be the same, informal institutions such as enforcement mechanisms, actor behaviors, and cultural differences can lead to different outcomes (North, 1990). Informal institutions are not complementary, but rather important determinants on their own. Moreover, change in formal institutions can be altered, even reversed due to the “stickiness of established beliefs and norms” (Shirley, 2008, p. 629). This is because informal institutions are “much more impervious to deliberative policies” (Steer & Sen, 2010, p. 1603). Therefore, reforms in formal institutions should be compatible with informal institutions to be effective on development. Even if there is no unique institutional mapping to foster economic performance, it becomes clear that finding the right institutional mix is a critical factor.

4.4. An alternative explanation

As I have discussed in the first chapter, institutions are primary drivers of economic development, especially to maintain their sustainability. They do so by reducing transaction costs and uncertainty to facilitate exchanges between market actors. The way that institutions interact with those actors, most prominently with firms, structure fundamental arrangements of the economy. Institutions are also structured as a result of their interactions with organizations that operate in given institutional context. Interactions between political institutions and firms have determining effects on their growth-inducing market strategies. The existing theoretical approaches show that informal institutions, in particular, are significant drivers of firm behavior. The informal institutions in the nonmarket environment influence how firms act in the market environment, either directly or by affecting the structures of formal institutions. Thus, I suggest that the quality of informal political institutions is the mediating variable that explains the causal link between institutions and

economic development, by influencing firms' market activities, such as investment, innovation, and productivity.

This section attempts to clarify which attributes of informal political institutions can explain economic differences across countries. I suggest three attributes regarding their impact on firms' impact on economic development: firms' perception on policy and regulatory commitment, alignment between formal and informal political institutions, and a sense of common purpose between public institutions and firms. I suggest that these three attributes of informal political institutions are central to determine the market activities of firms.

Firms make predictions about their current and planned activities based on the perceived policy and regulatory commitment by the government. Such commitments can manifest themselves in various areas, such as policy outcomes, administrative decisions, and regulatory reforms. Cetin argues that firms tend to avoid long-term market strategies and sunk-cost investments unless they are confident about the reliability of public commitments. Establishment of certain formal institutions, such as independent regulatory agencies usually aims to provide such commitments (Cetin, Sobaci, & Nargelecekenler, 2016). However, perceived independence of those agencies from political discretion is at least as significant as the institution's existence. Another indicator is government's commitment to a certain industrial strategy (Bugra, 1991). While governments and related institutions develop and disclose certain economic programs, industrial strategies and incentive mechanisms as formal institutions, market actors monitor the capacity of enforceability to decide on their impact (OECD, 2002; Rodrik, 1991). The first proposition is therefore as follows: *There is a positive relationship between firms' perception on policy and regulatory predictability and their economic development-inducing market activities.*

The interaction and complementarity between formal and informal institutions, as well as the drivers of their evolution, are also key considerations to understand the impact on economic performance. The past research demonstrates that alignment between formal and informal institutions is a critical factor to support business activity (Williams & Vorley, 2015). The asymmetry between formal and informal institutions, and lack of complementarity between the two is likely to cause a slowdown of entrepreneurial activity. Pejovich (1999) finds that

transaction costs tend to increase when newly introduced formal rules are in conflict with established informal rules, which in turn decreases potential returns from the aggregate effect of complementarity (P. A. Hall & Gingerich, 2009; P. A. Hall & Soskice, 2001). Estrin & Prevezer (2010) develop four types of relations between formal and informal institutions, according to institutional effectiveness and compatibility of goals: accommodating, substitutive, complementary and competing. The second proposition is as follows: *Complementarity between formal and informal institutions are conducive to firms' market activities that are positively related to economic development.*

The shared sense of purpose between public institutions and firms regarding the goals of the markets and activities of the private sector can be a significant driver of macroeconomic performance (Heilbroner & Milberg, 2011). The question of “in whose interests should economic actors operate” is a key driver of how formal and informal nonmarket institutions need to be structured (Yoshimori, 1995). This is why the distinction between liberal market economy and coordinated market economy as discussed in the varieties of capitalism literature has a direct relation with corporate governance. Whether shareholder value should be prioritized or firms should fulfill broader responsibilities for societies is what determines how informal political institutions affect market actors (Block & Somers, 2014; Micklethwait & Wooldridge, 2005). The third proposition is as follows: *A shared sense of purpose between public institutions and firms regarding the goals of the markets and activities of the private sector has a positive relationship with economic development.*

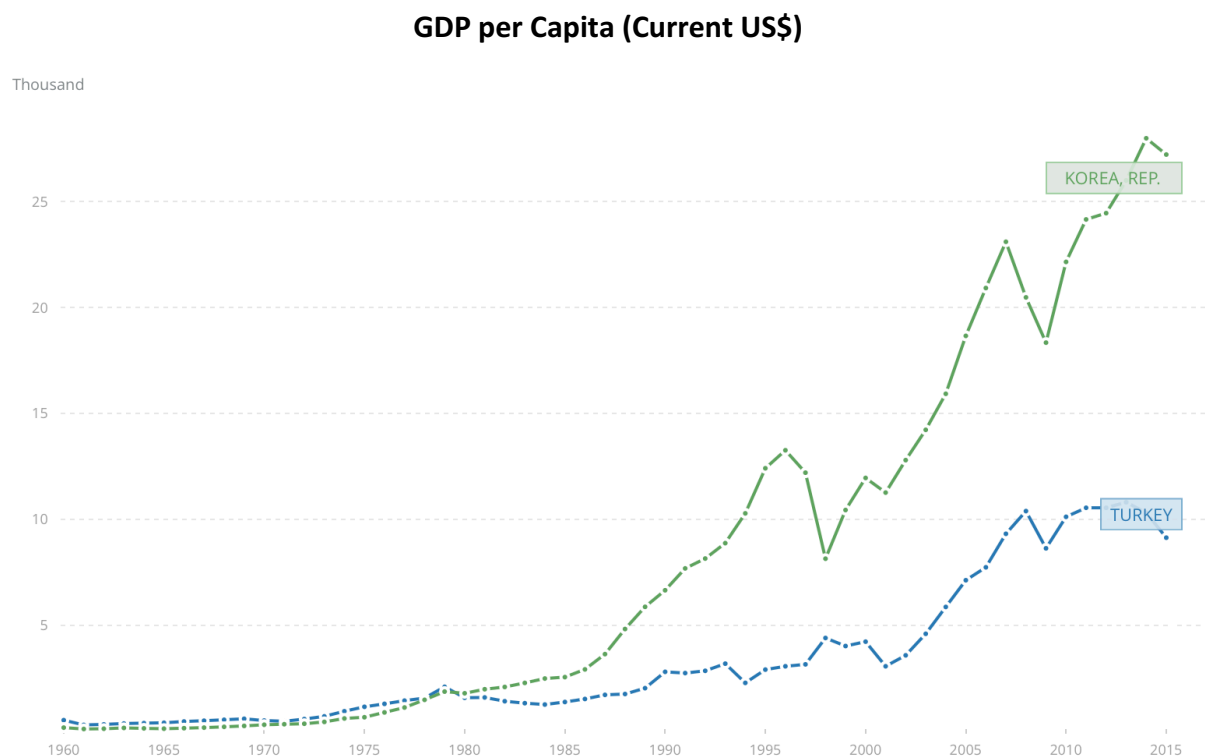
The next section will discuss how these propositions will be studied.

3. Cases and Methodology

3.1. Why Turkey and South Korea

Understanding the importance and explanatory power of informal institutions require studying cases that beg explanation for divergent outcomes, yet allow us to control for other variables. Turkey and South Korea can provide the necessary context in this regard. The two countries had similar development levels in the 1960s. Indeed, Turkey was a more developed country in the mid-1950s, regarding GDP, exports and savings rate (Krueger 1987). However, as the chart below shows, GDP per capita levels have significantly diverged since then.

Currently, Turkey is at a critical juncture and needs to implement long-awaited institutional reforms to avoid being stuck in the middle-income trap (Onis & Kutlay, 2013). South Korea has successfully transformed into a technology-driven economy.



Source: World Bank national accounts data

To justify the importance of informal institutions, the cases should demonstrate that the variations in formal institutions are insufficient to explain the divergence in the dependent variable, which is in our case the difference in economic development. North argues the importance of informal institutions can be observed: “from the evidence that the same formal rules and constitutions imposed on different societies produce different outcomes (North, 1990, p. 115).” In this regard, Turkey and South Korea have similarities in formal institutional structures that allow the tracing of how and to what extent informal institutions have made a difference.

Since the divergence in GDP per capita has begun taking place in the 1960s, this study considers that period as the inflection point and focuses on the development since then. External factors indicate similarities. Both Turkey and South Korea found themselves in

geopolitically tense regions at the beginning of the Cold War. While Turkey has become the south-eastern flank of NATO against Soviet containment, South Korea has become the main pillar of the US-led order in East Asia. Both countries benefited from US aid, but experienced macro-economic imbalances. While Turkey is close to Europe as the main economic powerhouse, South Korea is close to Japan (Krueger, 1987).

Internal political and economic structures also share commonalities. Both countries experienced military coups in the early 1960s, which was followed by short-term military regimes and subsequent elections. Both countries went through periods of military authoritarianism, though electoral politics have always been important in Turkey (Bugra & Savaskan, 2014). General Park has served as the President until 1979, while Turkey experienced military disruptions since then. Regarding economic coordination, both countries adopted state interventionism as the main policy paradigm (Ozel, 2015). State Planning Organization (SPO) in Turkey and Economic Planning Board (EPB) in South Korea were entitled with providing general guidance to public and private market activities. However, it should be noted that EPB were granted unprecedented regulation and enforcement powers, while SPO had to share its authority with other public institutions (Aydin, 1997; Minns, 2001). The developmental alliance has been replaced with export-led growth and liberalization policies during the 1980s. But as we will see in detail, South Korea maintained its regulatory and coordinating institutional mechanism, while Turkish economic landscape has mostly been a rent-seeking area. Finally, both Turkey and South Korea went through major institutional transformations after the financial crises, 2001 and 1997 respectively.

Given the similarities in political and economic institutions, it becomes more intriguing to explore the informal institutions that could explain the difference in macroeconomic performance.

3.2. Methodology and Data

This study employs the method of extensive archival research to make historical case comparison. The case study is a common methodology to investigate the complex structures of institutions and their interactions with the economy. As Alston argues, in studies where the interaction between institutions and economic performance is investigated, case study gives

the possibility of providing analytical narratives based on the use of historical qualitative evidence. (Lee J. Alston, 2008). Analytical narratives are tools “to test the hypotheses with methodological rigor and also describe the historical context, norms and beliefs, and institutional adaptations (Shirley, 2008, p. 634).” Since the causal link between institutions and economic development is well-established in the literature, the research agenda also aims to find out how successful institutional changes can happen. Alston argues that the method “allows us to produce a more general framework for the determinants of institutional change (L J Alston, 2008, p. 9).

This approach is particularly useful for studying the research question of this study: the impact of informal political institutions on economic performance by determining growth-inducing market activities of firms. Since informal institutions are hardly measurable, the purpose of this part cannot be to test them as hypotheses. Rather, by exploring the two cases empirically, the goal is to discuss the validity of these propositions as possible explanations of the difference in economic performance between the two countries. The below chart demonstrates how the causal mechanism is established.

4. Empirical Study

This chapter examines the three propositions suggested in the second chapter. As the previous chapter pointed out, Turkey and South Korea are two similar cases regarding formal institutions. However, their development path indicates significant differences. Thus, the discussion of the informal political institutions that allegedly determine growth-inducing business activities can address such the economic difference.

The scope of this chapter is confined to the empirical information that is relevant to the suggested theoretical framework. Therefore, subsequent sections neither aim to provide a detailed account of both countries’ development path, nor discuss the existing literature on developmental state or state interventionism. Rather, I explore the causal processes that constitute the nonmarket environment in each country, as determined by the informal institutions within the context of the three propositions.

4.1. Perception on Policy and Regulatory Commitment

Perception of business actors regarding the policy and regulatory certainty is a significant driver of market activity (Busse & Hefeker, 2005; Williams & Vorley, 2015). Researchers and managers have long tried to analyze and mitigate the risks associated with uncertainties in the nonmarket environment (Jha, 2013; G. Jones & Lubinski, 2012). Political risks and “even moderate amounts of uncertainty” is considered as a significant cost on investments and market value of firms (Bekaert, Harvey, Lundblad, & Siegel, 2014; Rodrik, 1991, p. 1). A firm’s capacity to assume political risks have a direct effect on its performance (Jimenez & Delgado-Garcia, 2012). Though Rodrik argues that investor perception does not reliably indicate why firms perceive their environment in a certain way, there is no doubt that it is a driver of business activity (2004). Firms take growth-inducing actions when they feel safe about returns. Therefore, the differences in literature’ perception on policy and regulatory certainty in Turkey and South Korea can explain the difference in macroeconomic performance.

Despite going through similar political trajectories that include military coups, geopolitical tensions and changes in economic policies, Turkey and South Korea have caused different perceptions in their business environment. The difference becomes even more salient given the fact that firms in both countries have been substantially dependent on government policies during the developmental stage that took place between the 1960s and 1980s (Bugra, 1994a; Im, 1987; M. K. Park, 1987). In a way, Turkish and Korean firms owe their very existence to the State. In the case of Turkey, the creation of a Turkish-Muslim bourgeoisie has been the main pillar of the State’s nation-building policy since the beginning of the 20th century (Keyder, 1988). Thus, a certain part of the Turkish business class has enjoyed privileged treatment by the State to make pecuniary gain and emerged as a social project rather than as a result of market forces. In both Ottoman Empire and Turkish Republic, the source of business power has always been found in State-centered explanations (Bugra, 1991). Korean case indicates similar features. The big business, known as chaebol, have emerged in the aftermath of liberation from Japanese occupation (L. P. Jones & Sakong, 1980). As major conglomerates owned by prominent families, these business groups have played an important role in Korean economic development (Witt, 2012). The fact that chaebol did not own their banks until the liberal policies were implemented made them financially dependent on the State’s discretion (L. P. Jones & Sakong, 1980). Even though chaebol leaders have had long-standing relations

with state officials, their businesses have always been under strict subordination to the public and economic policy making (Kuk, 1988).

Political nonmarket environment matters in all institutional structures. However, it can be argued that policy and regulatory certainty is a more significant determinant in emerging markets, especially in countries where businesses are significantly reliant on states such as Turkey and South Korea (Cavusgil, Ghauri, & Akcal, 2012; Wells, 1998). The causes of difference, though, begs an explanation from the perspective of informal institutions. The argument asserted here is that “state autonomy” is the main reason of why the perception of business class in South Korea caused activities that are conducive to growth, not in Turkey. State autonomy refers to the bureaucratic ability to make decisions independent from the interests of various social classes (Levi-Faur, 1998). Korean bureaucratic elite had been entitled with decision-making capacity and insulated from the pressures of outside forces (Kuk, 1988). Minns argues that the high degree of autonomy reinforced by the General Park regime (1961 - 1979) allowed Korean elites to intervene private sector activities and became the main driver of industrialization (2001). This idiosyncratic nature of Korea can be best explained with the concept of “embedded autonomy” coined by Evans (1995). According to this, a dense network of actors (both public and private) can exchange information and negotiate policies. The embedded autonomy of the bureaucracy allowed the decision-makers to allocate resources to incentivize business activity in line with the goals of the developmental state (Haggard, Kim, & Moon, 1990; Johnson, 1987; Maman, 2002). President Park Chung Hee’s policy was to legitimize its increasingly authoritarian rule with the achievements in economic development, which resulted in centralized planning and hierarchical implementation (Heo, Jeon, Kim, & Kim, 2008; Scitovsky, 1985; Thurbon & Weiss, 2006).

State policy making, on the contrary, has been considered as the main source of uncertainty for businesses in Turkey (Bugra, 1994b). Despite the existence of formal institutions such as State Planning Organization and National Development Plan since the early 1960s, it is clear that they were not sufficient to create a perception of certainty (Yilmaz, 2002). This, however, does not mean that the State has been instrumentalized by Turkish private sector, even during the liberalization period (Onis & Turem, 2001). Despite the center of gravity has shifted from

bureaucratic-military establishment to the politicians, state's hegemonic attitude towards business has remained the same. Bugra asserts that Turkish business class has suffered from the lack of social legitimacy because its source of wealth is considered as illegitimate (Bugra, 1994b, p. 7). However, state autonomy has been eroded by political changes in the government and the Turkish State under the military dominance failed to create a top-down hierarchy (Oh & Varcin, 2002). Legal mechanism and bureaucracy have become subordinated to the constantly changing policy preferences. This can be interpreted as an indirect link between state autonomy and different interests of the society, since policy preferences are mostly shaped by electoral concerns, in line with the main premise of public choice theory (Kaempfer & Lowenberg, 1999). According to Ozel, this shaky ground undermined "state cohesiveness," described as state elites' ability to create a collective action for development (Ozel, 2015). The lack of coordination and internal competition for more authority among public institutions has therefore created uncertainties for the business class.

The discussion above demonstrates that the proposition that "there is a positive relationship between firms' perception on policy and regulatory certainty and their economic development-inducing market activities" holds true. The investigation also shows that difference in state autonomy, caused by the relative insulation of bureaucratic mechanisms from various social and economic interests in each country, is the main driver of this perception.

4.2. Complementarity of Formal and Informal Institutions

As we have discussed in the second chapter, the nonmarket environment of firms is determined by both formal and informal institutions. While formal institutions can displace informal institutions, both structures can also complement or contradict each other (Fafchamps, 2017). The difference in time and effort required to establish or replace formal institutions and informal institutions can create misalignment (Steer & Sen, 2010). Such misalignment, described as "institutional asymmetry" is found to be detrimental to growth-inducing business activity, especially in emerging markets where such arrangements matter the most (Williams & Vorley, 2015). Therefore, I assume that the difference in alignment of formal and informal institutions in Turkey and South Korea is an explanatory variable of economic performance between the two countries. South Korea owes a great deal of its

economic development to institutional alignment, while the relative underperformance of Turkey as been caused by institutional asymmetry.

Turkey and South Korea have gone through various stages of development. Both experienced a transition from import substituting industrialization (ISI) to liberalization throughout the 1980s (Aydin, 1997; Haggard et al., 1990; Y. C. Park, 1990; Thurbon & Weiss, 2006). Each stage of transition in the economy means a restructuring of the institutional environment, including those that arrange the relations between state elites and business class (Haggard et al., 1990). Therefore, corporations determine their relational, political strategy in response to the particular institutional features in emerging markets (Luo & Zhao, 2013). The changes in the economic and institutional environment in relations with the State have determining effects on firm performance, as well as their impact on macroeconomic performance (Ozcan & Gündüz, 2015; Rajwani & Liedong, 2015). The political institutional environment has particularly significant in regulatory sectors, where State's intervention create the most impact on market dynamics (Bonardi, Holburn, & Bergh, 2006). Therefore, the argument asserted here is that the complementarity of formal and informal institutions during transitions is a key determinant of aggregate firm impact on economic development.

The link between economic performance and institutions has been proven in previous studies (Cetin, Cicen, & Eryigit, 2016). However, a closer investigation of institutional transitions shows that the development has been uneven. Turkey had experienced an abrupt transition from ISI to liberalization in 1980 when the government introduced a major economic transformation program with the aim of speeding up privatization (Ercan & Onis, 2001). The stabilization and structural adjustment program introduced by the government marked a shift towards export-led economic growth (Senses, 2001). The new policy meant opening some parts of the Turkish industry to competition and putting pressure on domestic production units through reduction of import tariffs. However, Onis argues that the privatization agenda has been slow in implementation until 2001 when the legal and institutional balance shifted for "pro-privatization" alliance (2011). Thus, the institutional asymmetry prevented a planned transition in Turkey. The widening gap between the institutions, most notably between state bureaucracy and coalition governments, was the biggest obstacle to bringing about the economic change, as well as to attract investments (Cetin, 2010). The cultural resistance of

the bureaucratic elite against the change has led to a rent-seeking society, as a result of the increasing influence of the business elite close to policy making (Cicen, 2015). Governments that were formed in the following years rather preferred to implement ad-hoc policies that produced “its own vested political and economic interests (Sonmez, 2011, p. 2).” Thus, Turkey’s regulatory reform did not take place during the first phase of liberalization. However, as a result of the increasing tendency of international economic institutions toward establishing good governance principles, as well as the ability of the Turkish elites to create a common narrative to implement policies that will improve the regulatory skills and capacity of the Turkish state led the period of institution building (Kutlay, 2014). Independent regulatory institutions (IRAs) aimed to provide credible commitment and reduce transaction costs to galvanize private sector’s growth-inducing activities (Cetin, Sobaci, et al., 2016; Zenginobuz, 2008). However, Turkey’s informal institutions (e.g., cultural codes of the political elite) have once again resisted the shift to delegating authority to those institutions. The main point of disagreement was the power of IRAs to determine market conditions, without being accountable to voters (Yeung, 2012). Consequently, the independence of IRAs has been increasingly undermined as a result of legal and institutional changes since 2001. According to OECD’s review in 2015, Turkey’s Regulatory Impact Assessment score remains well below OECD average (OECD, 2015).

The Korean example has both similarities and differences with the Turkish case. Broadly speaking, the transformation of the Korean economy was based on using State’s institutional power to implement a shift from labor-intensive to technology-intensive production, as proven with the introduction of Foreign Capital Inducement Act in 1984 to allow Korean firms to share technology with foreign partners. Despite the economic reform in South Korea that aimed to integrate the domestic industry with international markets, the government has maintained regulatory tools not to lose control over many sectors (Ha & Lee, 2007). The authoritarian state autonomy came under pressure in the 1980s, especially by the increasing power labor unions (Minns, 2001). The developmental alliance between State and chaebol transformed into the regulatory regime, where the interventionist state had to retreat from its direct role (E. M. Kim, 2011). The increasing autonomy and significance of the chaebol to the Korean economy meant that the developmentalism had reached limits regarding private sector’s subordination. The gradual integration of the Korean business with international

actors since the 1980s did not mean the abolishment of top-down and president-centered decision-making, though big conglomerates have also become a part of that process (Rodrik, 1994; Witt, 2012). Siegel asserts that economic liberalization has never aimed to loosen state's power on regulations or budget allocation (2007). Rather, it was a state-instituted transition process towards the high-tech economy. Nevertheless, the Korean government has begun allowing chaebol to own limited shares in bank and non-bank financial institutions, a major prerogative of the Korean state to control chaebol's productive activity (Schneider, 2009). Despite the changes in the financial domain, however, corporate governance and labor market reforms have not been successfully implemented even after the post-crisis reforms in Korea (Ha & Lee, 2007; S. Kim, 2000). The most effective informal institution that influenced the restructuring of relations between the State and chaebol was Korean society's traditional perception of the big business. Witt argues that a significant majority of the Korean population finds chaebol activities immoral, which gives the Korean formal institutions more power to maintain their grip on big business through regulations and corruption investigations (2012).

The differences between Turkey and South Korea are quite vague. Turkey has experienced an institutional asymmetry between the establishment of formal institutions and beliefs of state elite during the economic transition period. This prevented the emergence of economic change to boost export-led growth. South Korea has implemented a planned transition, in which State has kept its dominant position, though in a reciprocal way with big business. The transition to technology-driven economy has taken place, but not all reforms were successfully implemented due to the resistance in informal institutions. Therefore, the argument that "complementarity between formal and informal institutions are conducive to firms' market activities that are positively related to economic development" is partially substantiated.

4.3. Mutual Commitment to Economic Development

The developmental state literature suggests that nations can achieve economic progress as a result of state-supported industrial growth, in which private sector becomes an important driver. Even though previous studies have contradictory views on what exactly causes development, "careful policy interventions" is considered as the main pillar (Walden Bello, 2009, p. 185). Moreover, whether the institutional environment that allows state-intervention

should displace market reforms, or whether the same developmental paradigm can be successfully applied in other economies is questionable (Unay, 2011). While many countries have adopted a development-minded agenda, only a few have been able to implement them. This is why it is difficult to identify a single developmental recipe. A deeper investigation is required to understand the idiosyncrasies of successful developmental states. The argument asserted here is that the shared sense of purpose and mutual commitment by both the State and private sector towards the economic development goals of the country.

Turkey has adopted a developmental paradigm. However, its institutional structure did not allow to pursue a coherent strategy. Bugra argues that the importance of electoral politics is the main differentiating factor in Turkey (Bugra & Savaskan, 2014, p. 279). Party politics, weakness of bureaucratic autonomy and changes in political preferences were the main reasons of why developmental ideology did not achieve its purpose. The lack of private enterprise's self-confidence has been fostered by the rent-seeking attitude of various governments and businesses (Bugra, 1994b, p. 19). Bugra argues that it is not the extent but the "form" of state interventions that makes the difference between Turkey and South Korea. Turkish business class has not considered government's industrial strategy as reliable or fully committed. The mutual distrust between the two sides undermined the efforts to boost the export-led growth in the 1980s (Ozel, 2003). Therefore, the business - government relations in Turkey have not been complementary, but rather confrontational where the State has always held the upper-hand. The deep-seated suspicion regarding private enterprise and business activity has sustained since the early days of the Republic. Many Turkish businesses opted for diversification to hedge risks of becoming too dependent on the State for wealth creation (Colpan & Jones, 2015; Gundem, 2012).

The South Korean state had a robust institutional mechanism to ensure the alignment of business activity with its development goals. Korean businesses, though sometimes reluctantly, appear to have been supportive of this agenda. Two peculiar features make the Korean case particularly important. The first is the unwavering commitment and clear declaration of goals by the authoritarian State (Johnson 1987). The government's industrialization agenda has been the nucleus of high-speed growth (Lim 1998). The political and bureaucratic elite thus had a developmental ideology that - coupled with the state

autonomy discussed above - enabled them to make strategic decisions based on their expected impact on national development (Karsan & Atay, 2013; Maman, 2002). The second dynamic was the State's attitude towards private enterprise. Unlike Turkey, private firms in South Korea have never been dismissed. However, they were considered as mere instruments of the developmental state. Korean institutions had clear performance criteria for private firms (Erdogdu, 2000). Those firms that could achieve these criteria (e.g. Exports, employment) were given incentives, mostly in the form of the allocation of financial resources (Koo & Kiser, 2001). Jones and Sakong assert that South Korea owes a great deal of its economic development to the close working relationship between government and business, as well as alignment on the development goals (1980). It should, however, be noted that this partnership has been lopsided for the Korean State. In the case of contradiction between State's long-term development goals and chaebol's short-term profits, the managers were left with the choice of conforming to the State's plans or incurring penalties. Economic Planning Board has been a strategic institution of the developmental state (E. M. Kim, 2011). The state has supported the development of big business and played a critical role in determining their daily activities (Maman, 2002; Mody, 1990; Rodrik, 1994). The power of informal institutions has become more salient in how State supported the firms. Even though particularism has been prevalent and the vagueness of legal schemes allowed discretionary favors, recipients State support were associated with developmental purpose (Haggard et al., 1990; M. K. Park, 1987). Other features such as social cohesion, trust in government, Confucianism were also influential (Easterly, Ritzen, & Woolcock, 2006; Scitovsky, 1985).

The discussion above demonstrates that the proposition that "a shared sense of purpose between public institutions and firms regarding the goals of the markets and activities of the private sector has a positive relationship with economic development" holds true for Turkish and Korean cases. While Korea has been able to synchronize its development goals with the business activity through a well-planned incentive mechanism, Turkey's electoral politics, weak bureaucracy, lack of developmental commitment to industrialization and historical legacy regarding the view on private sector inhibited a similar alignment.

5. Conclusion

The causal link between institutions and economic performance has been subject to investigation in previous research. The literature demonstrates that institutional determinants influence countries' economic performance by mainly decreasing transaction costs and ensuring property rights. Organizations act within the rules of the game set by the institutions. One such market organization is the firm, whose aggregate business activities such as investment, productivity, and innovation have determining effects on macroeconomic performance. The strategic management literature tells us that firms make decisions on growth-inducing market actions based on their analysis of external environment and internal capabilities. The institutional structures are significant determinants of their market activities. Nonmarket strategy research shows that the political climate is one of the most important external dynamic in business activity. Thus, political institutions of firms' business environment deserve further exploration.

In order to investigate this topic, this study explored the two similar cases: Turkey and South Korea. Turkey was a far richer country in 1960s. But South Korea has been able to successfully implement developmental policies and increase its GDP per capita to the upper-income countries level, while Turkey has remained in the middle-income trap. This study demonstrated that the difference in development has been for the large part caused by the institutions that arrange the relations between State and business class. However, the similarities between formal institutions required a deeper exploration of what really caused the economic divergence between the two countries.

This study suggested a theoretical framework with the aim of investigating the significance of informal political institutions that are conducive to business-driven macroeconomic performance. By pursuing a deductive research strategy, the framework included three main attributes: policy and regulatory commitment as perceived by the firms, complementarity between formal and informal institutions and a shared sense of commitment by public and private sector to the common national development goals. The existing literature suggests that these attributes allow us to explore the informal political institutions as the mediating variable of the causal link between institutions and economic development. Since informal

institutions cannot be reliably measured, these attributes are suggested as propositions to be studied, rather than hypotheses to be tested.

The empirical part of the study was based on the analysis of historical evidence. Since the purpose was to explore the attributes of informal political institutions, the analysis was limited to the comparative discussion as regards the three suggested attributes. First, the study demonstrates that “perceived regulatory and policy commitment” is an important driver of economic growth, especially in emerging countries like Turkey and South Korea where the business class is dependent explaining for wealth creation. My exploration uncovers that the concept of state autonomy (the relative insulation of state and bureaucratic elites from the pressure of social classes) is the underlying dynamic of such perception. Second, the impact of the complementarity of formal and informal institutions is not as clear as to argue that it is a significant driver. While the study shows that the complementarity argument becomes salient especially during the transition periods, which include a fundamental restructuring of political and economic institutions, its influence on economic performance remains vague. Third, the mutual commitment to national development goals makes the cooperation between public and private sectors possible, and as in the case of South Korea as opposed to Turkey, increases the chances of economic growth.

This study was an attempt to explore the attributes of informal political institutions that could explain the economic divergence of countries that have similar formal institutions. The underlying assumption was that informal political institutions have determining effects on firms’ business activities that are conducive to growth. While the discussion explored some part of the causal mechanism, further research is needed to examine the validity of these findings in other cases, as well as other explanations that can possibly adjust the theoretical framework suggested here.

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