

# The Mafioso State: state-led market bypassing in South Korea and Turkey

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**ABSTRACT** *'Developmental' states often obfuscate the distinction between the state and the market, as state actors prefer political over economic solutions to market problems (market bypassing). Market bypassing is a process of replacing monopolies in the private sector with state monopolies; in so doing, the state transforms itself into a mafioso state. The business of the mafioso state is selling 'protection' to businesses and collecting extracts, either legal or illegal, in return. The result of the mafioso state in the economy is the conglomeration of businesses, as is clearly the case in both South Korea and Turkey.*

State-led developmental programmes produce sundry consequences. Whereas countries such as South Korea and Taiwan have demonstrated an enormous developmental success, others such as Indonesia and the Philippines remain developmental basket cases. Existing studies offer conflicting arguments on these different outcomes of what we call state-instigated market bypassing (or political solutions to economic problems).<sup>1</sup>

For example, the statist argument embraces Japan as its paradigmatic case and highlights the apparent importance of the Japanese 'developmentalist' state *vis-à-vis* the free market in the Japanese mode of rapid growth (Johnson, 1987, 1995; Appelbaum & Henderson, 1992; Fukui, 1992; Williams, 1994). Other scholars, however, take the very existence of the strong state as a defect in the economic system that ultimately damages capitalist economic development (Krueger, 1974, 1977, 1995; Buchanan *et al.*, 1980; Krugman, 1990, 1994).

*Pace* disagreement on the politico-economic legitimacy of market bypassing during a developmental phase, we intend to move one step further by addressing *why market bypassing can be occasionally successful, when elsewhere it is not*. Recently, Waldner (1999) has introduced an important and timely theoretical question in the developmental literature—what are the origins of successful developmental institutional profiles? For Waldner (1999: 9) low levels of elite conflict evident in the cases of Korea and Taiwan were instrumental in the formation of narrow coalitions among elites, which then enabled the formation of the developmental state that eventually resolved the problems of what he calls

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Gerschenkronian and Kaldorian collective dilemmas.

However, as in similar attempts by others, Waldner's developmental state remains a black box, not readily explaining what product cycle theory has been used—what are the organisational or economic mechanisms of innovation despite different developmental institutions in Japan, Korea and Taiwan? Although elite coalitions explain state building in the way Weber and Bendix explained it for their European cases, they cannot account for technological or organisational innovations.

To capture the mechanism of both state building in the public sector and innovation within the private sector, we introduce a more concrete concept than such a tautologous one as developmental state—the mafioso state. The concept of the 'mafioso state', whose meaning will be expounded in detail in the course of this paper, can be more useful than that of the 'developmental state' in explaining the efficiency and effectiveness of state-initiated market bypassing: the term 'developmental' only assumes such efficiency and/or effectiveness.

We posit that there is a possible linkage between the different types of mafioso state and the final organisational form of private business corporations, and that this linkage holds a key to understanding the innovation structure of the entire state-led developmental programme (ie market bypassing). Briefly, the mafioso state in South Korea created the *chaebol*, an organisational innovation that was critical in promoting innovation for economic development, whereas the mafioso state in Turkey engendered the Holding, an organisational development that was not sufficient enough to induce economy-wide innovation.

### **The theoretical backdrop to the 'mafioso' state**

As Migdal (1988) poignantly spelled out, sweeping land reform is critical in establishing a developmental state (see also Haggard & Kaufman, 1995; Lie, 1998). Developing economies which completed full or partial land reforms, such as Korea and Turkey, however, faced another choice of whether to actively involve themselves in the rising urban market.<sup>2</sup> If the choice is made to intervene in the market, bureaucrats of a strong developmental state face a third choice of whether to demand extracted payments from market actors for their regulatory intervention (eg taxation, political contributions, forced bribery, extortion). If they decide to pursue the collection of both legally and illegally extracted payments, as in the cases of South Korea and Turkey, they begin what Tilly (1992: 97) calls the process of 'adjudication' and 'extraction' in exchange for 'protection'. It is in these cases that we can label a state, a *mafioso state*.

Therefore, this concept absolutely does not mean that all state-led market bypassing results in mafioso states. First of all, many states do not openly collect illegal dues despite market bypassing, except only in third world countries. Second, although illegal extraction exists, some third world capitalists may in fact initiate market bypassing, consequently reducing state officials to acting as their servants (this is an instrumentalist view of the state). Third, many third world countries have not completed either sweeping or partial land reforms, discouraging the birth of a new urban merchant class completely devoid of any rural land properties. Fourth, although growth is there through rapid industrial-

isation, if the government is democratic (ie there is a constitutional guarantee of government alternation through free competition among political parties), a Mafia clientele network between state officials and capitalists can hardly develop.

The mafioso state is a *stable* alliance between enemies in the marketplace. The mafia analogy works like this. The state bureaucrats act as hostile mafia members against street merchants, demanding illegal fees for protection. Simultaneously, without such an alliance in the marketplace, street vendors would not be able to continue their business, unless they defied the mafia in a unified manner. Often, they fail to maintain unity, for mafia threats work as incentives to defect. Over a period of time, these street vendors react differently to the mafia on a collective level—they develop various organisational forms. In South Korea the merchants formed the *chaebol* and in Turkey the Holdings.

The *chaebol* was highly innovative in leading economic development, simultaneously paying large sums of money to the leaders of the mafioso state. The Turkish Holdings, however, have achieved only limited economic success. This difference in the level of economic success leads to the conclusion that different patterns of market bypassing yield different developmental results. Other things being equal the organisational structures of a big business corporation in a developing state depend on the type of the mafioso state in place. The organisational structures then have different impacts on the overall innovation structure of the entire industry, which eventually determines the success of industrialisation.

### **State–business interaction under the mafioso state**

We can characterise the state–business interaction (SBI) during market bypassing in a developing economy in the following way. First, SBI is a political organisation that substitutes for price and trust in the marketplace. Market price is a social mechanism that regulates human actions in the market through allocative efficiency. Trust, on the other hand, is a social mechanism that discourages allocative efficiency, since trust usually promotes motivational efficiency, such as X-efficiency (see Leibenstein, 1966). These two mechanisms do not create conditions for the rise of the mafioso state, although they certainly invite state intervention in the market.

Second, there is no perfect market-based or trust-based society. Usually, price and trust coexist in any market institution. Consider the following example. A peasant father in a third world country would never sell his daughter to a pimp for a price, no matter how lucrative it is (trust). On the other hand, some fathers do sell their daughters for a price, no matter how scant it is (price). These contradictory social actions coexist in a developing society, although we still do not know why they do so.<sup>3</sup> However, this contradiction, rampant in our real market institutions, leads us to a third point.

The confusing nature of the coexistence of price and trust in the market often forces some market actors to seek political solutions to their market problems. A typical third mechanism in the market is the mafioso. A market actor essentially hires a ‘hit man’ to collect a loan extended to his friend. Neither high loan interest as a price mechanism nor friendship as a token of trust has worked in this

case (Gambetta, 1988, 1993). While the hit man operates as an external intervention in the market institution, this substitution of trust and price by the mafioso is costly and unstable (Gambetta, 1993: 32). The secret deal between a market actor and the hit man can always go wrong. Even when successful, the hit man can always come back for more fees, and the market actor has to hire another hit man, this time more costly and dangerous, to stop the previous one.

Now, what if the state itself is interested in assuming this third mechanism of mafioso and its role in the market (ie the mafioso state?) According to Tilly (1992), such transitions from normal state to mafioso state have in European history by no means been few and far between. His model of war making and state making in Europe, where the state acted as a protector and extractor of its subjects, explains the process of the transition to a mafioso state, highlighting the historical significance of the state's market intervention. 'Adjudication', 'distribution' and 'production' were part of the daily functions of the mafioso state (Tilly, 1992: 97).

According to Gambetta (1993: 2), the Mafia can be defined as a business organisation that intends to expand through violent means. Violence is then funded by extraction from its subjects in exchange for protection. The political meaning of this economic sense of 'protection' is none other than what Tilly refers to as 'adjudication', as long as it is done by violent and authoritarian means. Authoritarian adjudication, with military domination, has been the norm in politics during the state-making and/or capitalist developmental periods in Europe and Asia. For instance, Mann (1986: 511) finds that, even in England, where diffused power relations emerged for the first time in human history, military domination in political and economic matters was obvious.

### Three types of mafioso state

In modern mafioso states market bypassing (or authoritarian adjudication) dominates the economic realm. There are three general patterns of market bypassing or mafioso state-business interaction: (1) victor mafioso states; (2) top-down mafioso states; and (3) defeated mafioso states.

The *victor mafioso states* are former imperialist states, including all types of mercantilist states, which developed and managed a network of colonies. International or long-distance war making looms large in this category as it encompasses most Western European countries, the USA, and Japan up until the end of the Second World War (Tilly, 1992). Since neither South Korea nor Turkey belongs to this group, we will not elaborate on this category any further.

The *top-down mafioso state* is one in which the state initially demands market actors seek state protection. State bureaucrats are not willing to provide business permits or legal protections (eg property rights) to market actors if businesses or business owners do not remit extracted payments (ie illegal forms of rent) to the former. This process is what we would call 'market suppressing' to highlight the fact that it is the state that initiates market bypassing. Market suppressing is widespread in the top-down mafioso state when state bureaucrats successfully create a 'prisoner's dilemma' situation among market actors. The banking sector, mostly owned by the state, is one key element of the top-down mafioso state.

When the sole source of capital is the state bank, division among the capitalist class is rampant. As we will show in our case studies, market actors are forced to give up the option of relying on prices or trust and rush to the state bureaucrats for protection under the prisoner's dilemma. Prototypes are South Korea, Turkey, Prussia and the 1930s totalitarian Japan.

The top-down mafioso state invites strong resentment from the business sector, which the hunts down every possible option of countervailing state hostility. Business actors do not remain mere lame ducks and will utilise every other option available in order to be less dependent upon the mafioso state apparatus. Diversification with centralised ownership (ie conglomeration), has proven to be effective for this purpose, because the growing size and power of the business can neutralise state hostility. More importantly, when either external or internal forces challenge this type of mafioso state, business actors show every interest in abandoning state-client relations.<sup>4</sup> Furthermore, intra-business competition intensifies, because the mafioso state plays business organisations off against each other (prisoner's dilemma).

The third type is the *defeated mafioso state*. When a mafioso state is overrun by a bigger and better mafioso state in an international war, the former is defeated and then subjugated into a larger mafioso system. The domestic mafioso state, under the auspices of the victor mafioso, creates a new system of levying extracts. Extracts are then shipped to victor states, creating a situation where the domestic systems of extraction are harsher than in either of the first two types of mafioso state. In return, the defeated mafioso receives protection from the victor mafioso. Most third world mafioso states, the prototypes of dependency theory, which include former colonies, fall into this category.

### **Innovation under the mafioso state**

The top-down mafioso states have historically demonstrated their uniqueness in inducing innovation among business actors. When market bypassing is initiated by the state, market actors strive to find ways of coping with the hostile environment (Gargiulo, 1993). Although co-optation is a common form that appears in the initial phase of economic development, market actors soon resort to size expansion to reduce their reliance on the hostile state. Innovation here thus refers to organisational innovation, given the fact that all business organisation can obtain technological innovation through piracy, state-run research and development (R&D) projects (if the state decides to subsidise R&D through policy networks), or technology transfers from foreign direct investments. The result of organisational innovation is enterprise diversification, a clear tendency in South Korea and Turkey.

Both South Korea and Turkey maintain the centralisation of corporate ownership with a high degree of diversification, being military states that actively intervened in the market by means of top-down market bypassing. However, the South Korean military manifesto had by law prohibited the *chaebol* from possessing holding companies, which were central organisational components of the pre-war Japanese *zaibatsu*. Consequently, although *chaebols* do maintain family ownership and control subsidiaries, this is done through family stock

concentration and/or inter-member firm stock ownership (ie subsidiaries own each other's stocks). Turkish conglomerates, on the other hand, maintain direct family ownership and the control of subsidiaries through holding companies, which most closely resembles the pre-war Japanese *zaibatsu* (and therefore have relatively weak organisational innovation).

This difference of the level of organisational innovation derives from the lack of additional military pressures on big business in Turkey, besides typical hostility to business in any top-down mafioso state, in the form of banning holding companies. Such pressures existed in both postwar Japan and Korea, where organisational innovation meant business survival (see Aoki *et al*, 1997). Indeed, except during the Kemalist republic and the 1960 military state, the Turkish military has not directly ruled the country, rather playing a critical role only in the background. The Kemalist republic was mainly interested in the nationalisation of foreign firms, while the 1960 military state could not last long because of political instability. Subsequent military coups in 1971 and 1980 encountered similar fates, and the military is now playing only a behind-the-scenes role in major political decision making (Savran, 1986).

Therefore, elite conflict or stability *per se* is not as critical as the overall stability of the top-down mafioso in inducing organisational innovation for local firms.<sup>5</sup> Although state hostility towards big businesses, typical in top-down mafioso states, was sufficient to force market actors to bypass the market, the degree of state intervention in the market still determined the degree of organisational innovation. This point has rarely been made a theoretical focus among scholars of third world development. The rest of the paper offers a comparative case study of South Korea and Turkey.

### **The South Korean *Chaebol***

The *chaebol* (literally, families with a lot of wealth) officially appeared in South Korea in 1953, when Samsung added a sugar refinery to its trading company (Kim, 1991; Cho, 1994). In the 1950s and the 1960s, a handful of *chaebols*, all under state protection, were mere receivers of the US dole (in a classical import substitution). In less than four decades, however, 30 or so large *chaebols* have come to produce more than 80% of the total South Korean GDP (Hamilton & Biggart, 1992; Yoo in Hah, 1995).

The *chaebol*'s domination within the South Korean economy, along with the recent fervour for internationalisation via foreign direct investment, indicates high levels of business and organisational diversification within each *chaebol*. *Chaebols* are highly diversified business units each owned and controlled by a single person, the chairman (Cho, 1994). In a typical South Korean *chaebol* the chairman is either the founder or his familial successor.

Behind the success story of the *chaebol* is the untold saga of its troubled interaction with the military state. To our question, 'which environmental factor do you think has been the most critical to your enterprise group?' four of the five high-ranking *chaebol* officers we interviewed in 1995 answered: 'it has been the state' or 'it has been the government'. If the state is one of the most important business environmental factors, then the proactive managerial response to it

needs theoretical attention.<sup>6</sup>

*Chaebols* had been market monopolies with holding companies until the 1961 military coup. Unlike the post-coup *chaebol* or the Turkish Holdings, they had not pursued diversification, as they mostly concentrated resources in specialised markets. The military junta established under the leadership of Brigadier General Park Chung Hee relentlessly eradicated what it perceived as corrupt elements of the previous civilian regime, most importantly in the area of big business. Samsung, then the largest *chaebol*, therefore had to contribute its banking sector and Honam Fertilizer (valued at 15 billion won) to the state. Twelve other *chaebols* also had to pay similar fines under the Illicit Wealth Accumulation Law (Koo & Kim, 1992: 25; Fields, 1995: 51–53).

The confiscation of private property from capitalists involves enormous risk on the part of the state rulers. The threat of what economists call ‘deadweight loss’ is always present (Peltzman, 1976; Block, 1977; Lindblom, 1977; Browning & Johnson, 1984). Thus, *chaebols* faced a choice of whether to buy protection or to divest. In the end, a collective decision to divest from the market did not happen, because *chaebol* owners could not trust each other. Consequently, those who could buy protection bought it, and those who could not perished in the market. For example, Lee Byung Chul, then the owner of Samsung, asked the state to approve Samsung’s investment plans and supply foreign aid for its projects. In return, Lee promised to share the profit with General Park (Sohn, 1990: 58–60). This payment was not taxation or a political contribution. It was an illegal means of extraction of money from business leaders (a slush fund). Park happily accepted this arrangement, and a new state–business relationship was born.

Gambetta (1988: 167) explains the birth of the mafioso state succinctly in the following fashion:

[In] the example ... of South Korea ... an authoritarian and military rule ... in itself monopolistic, would not tolerate local monopolies [ie the 1950s *chaebol*]. In a sense, this implies that in order to get rid of the mafia, what we need is simply another—bigger and better—mafia.

From the *chaebol* owners’ standpoint, the military state was the most important source of environmental uncertainty that had to be controlled. There are two reasons for this observation. First, the *chaebol* had to create enough wealth to meet the state’s extraction demand; second, it had to grow big so that the mafioso would not whimsically destroy it. Samsung’s founder understood this very well, and he opted for diversification.

In our 1995 interview with the Head of Chairman’s Office at Sunkyoung Group, he explained the logic of diversification in the following way:

When you are small, all kinds and levels of bureaucrats want to visit you and demand exacted payments. District police chiefs, district fire chiefs, district tax chiefs, district utility chiefs, and others are such thieves. But if you acquire two or three more subsidiaries, then these low-level gangsters are replaced by Seoul police chief, Seoul tax chief, and so on. And if you acquire 10 more, then you directly deal with section chiefs in state ministries. Finally, if you become big like us, the chairman bypasses all the middle bosses and directly talks to the real boss, the President.

Throughout the 1960s and 1970s, the *chaebols* struggled to steal each other's markets and to secure government loans for new ventures. During the period 1975–79 152 new corporations came into being, with 173 firms bought out, 13 companies merged into larger ones, and 17 joint ventures formed (Kim, 1987: 78). In 1977 the Blue House (the presidential residence) collected 365 million won from the *chaebol*, followed by 865 million won in the next year (Kim, 1993). The situation under the second military government (1979–87) did not change much. In 1985 the military government seized control of the then sixth largest *chaebol*, Kukje, and sold it to other *chaebols* and to independent firms. This was another attempt at creating the prisoner's dilemma. As state hostility continued, extracted payments also resumed. In 1982 major capitalists were asked to donate 1.1 billion won, followed by 2.04 billion won in 1984. The figures for 1985 and 1986 are 1.14 billion won and 2.04 billion won, respectively (Kim, 1993).

Diversification without a holding company system under the top-down mafioso state was effective in protecting the *chaebol* from the military's hostile and arbitrary intervention in its day-to-day business. Most importantly, however, diversification was pivotal in inducing innovation, as the *chaebol* were able to utilise economies of scale, exploit their oligopolistic position in the market, generate technological spin-offs from other member firms, and control agency problems through centralised governance.

## Turkey

Turkish 'Holdings' emerged when Deva Holding and Sinai and Mali Yatirim (Industrial and Financial Investment) Holding officially came into being in 1955 (MCI, 1997). This was possible, as we will explain below, thanks to the privatisation of the public corporation by the first civilian government under the leadership of the Democratic Party. However, more important and powerful Holdings emerged only during the military states, beginning with the 1963 inauguration of the Koc Holding. By 1969 Turkey had 33 holdings, and the number grew to 640 in less than three decades (MCI, 1997).

The role that the Turkish Holdings play in both domestic and international markets is noteworthy. The Koc Holding, a member of the Fortune 500, now has 81 subsidiaries, many of which are leading enterprises, while the second leading Holding, Sabanci, has 40 subsidiaries (MCI, 1997). Their investment ranges from automobile manufacturing to grocery store chains, from metal industries to private universities, and so on. Unlike in South Korea, however, in Turkey consortia of holdings exist, based on mutual stock ownership, an important characteristic of the Japanese *keiretsu*. For instance, Sabanci Holding and Sinai ve Mali Yatirimlar Holding bought each other's shares in 1994 and 1995 (MCI, 1997).

Similar to the situation in South Korea, in Turkey the state constitutes the most important environmental uncertainty for business. Business newsletters, press releases and business closed-door meetings are full of complaints about the structure of the state and state policies. In Turkey the majority of Holding leaders and managers that we interviewed in 1997 claimed that the state was the most



important business environmental factor.

As noted above, however, the Turkish military state failed to create a stable top-down mafioso state because three different military coups occurred within a single decade.<sup>7</sup> No mafioso state banned the holding company system in Turkey, providing no incentives for organisational innovation. Although the Kemalist republic successfully completed the state-building process in Turkey at the height of imperialist invasions, it pursued state monopoly by nationalising most foreign-owned corporations (Berberoğlu, 1982). The 1923 Economic Congress in Izmir legitimated the nationalisation of the railways, telecommunications, port facilities, and mining and textile corporations, most of which had been in the hands of foreigners (Herslag, 1968). Furthermore, the state also made clear efforts at weakening small industries owned and controlled by Greek, American, or Jewish entrepreneurs (Avcioglu, 1975).

The Kemalist economic intervention resembled the Nationalist (Kuomintang) economic policy in Taiwan throughout the 1950s and 1960s. Unlike in Taiwan, however, the capitalists revolted (deadweight loss), and by 1946 were able to destroy the one-party dictatorship of the Kemalist People's Party and install a pseudo-democracy under the leadership of the Democratic Party (DP), which represented landlords and capitalists. Because of this DP-capitalist nexus, the new civilian state was nothing but a corrupt capitalist state (crony capitalism). It was the DP and its inner circles which distributed foreign loans to themselves (Sayibasli, 1976).<sup>8</sup> Deva Holding and Sinai & Mali Yatirim Holding took full advantage of this kind of crony capitalism.

Corrupt state-business collusion under pseudo-democracy invited further political instability, including a military coup on 27 May 1960. Military officials controlled key posts in the government and arrested the president, prime minister and members of the cabinet. The downfall of the DP meant the concurrent demise of the early holdings and their interest groups, including the Chamber of Commerce and Industry.

Unlike South Korea, however, this 1960 military regime did not sell protection to former DP-aligned holdings. Instead, the new top-down mafioso state bred and protected new holdings. Bigger holdings began to emerge, and their owners soon started the diversification drive on a similar scale to that of the South Korean *chaebols* under the first and second military states. Although we do not have concrete data regarding the actual amount of the extracts the military government collected in exchange for protection during this era, our interviews with the managers of major holdings acknowledge such payments.<sup>9</sup>

For instance, the Enka Holding owner, Tarik Sara, pointed out that one has to pay illegal fees to the state in order to survive in the market. He made it clear that these illegal extracts are much more than ordinary bribes:

Legal extracts are the amount of the money that one has to pay the state to do *legal* business in the market. The bribery is the amount of the money that one pays the state to do *illegal* business (*Yeni Yuzyil*, 13 May 1997; emphasis added).

Another holding leader, Lokman Kondakci, pointed out that, without state support, not only is it impossible to accumulate capital, it is also impossible to survive in the market. He also emphasised that 'bribery is the rule, not the

exception in state–business interaction’ (quoted in Colasan, 1986: 347).

The first military government of 1960 lasted less than three years, and in 1971 another coup occurred. This new military state, however, could not destroy the holdings formed in the previous decade, mainly because of their sheer size and market power in the Turkish economy. Furthermore, these holdings formed a new interest group under the title of the Association of Turkish Industrialists and Employers (Turkiye Snayici ve Isadamlari Dernegi—TUSIAD). TUSIAD confined its membership to large holdings, such as Koc, Sabanci, Tekfen, Eczacibasi and Yasar Holdings (Sonmez, 1992). The diversification efforts paid off, and these holdings further sought new markets for investment, while continually paying illegal extracts as protection fees. Again, this was necessary because most large banks were in the hands of the mafioso state, as was the case in South Korea.

Like the previous military regime, this second one also could not survive more than two years because of political instability, and a third military coup occurred in 1980. The absence of trust between the mafioso state and the holdings can be demonstrated by the fact that the latter openly endorsed the new military government, instead of supporting the old one. For instance, Koc Holding’s owner, Vehbi Koc, sent a letter to the new military leaders to publicise his support (Sonmez, 1992). Other holdings appointed retired military generals of the new military state to their boards of directors. However, the third military state did not intend to rule the country directly, unlike its predecessors. A national election took place in 1983 under the close supervision of the military.<sup>10</sup>

Although top-down in its nature, the Turkish mafioso state could not eradicate crony capitalism because of the instability that mainly derived from the ethnic and social cleavages in the country (Waldner, 1999). A bigger and better mafia did not replace the various local mafias which had instigated the political instability and failed to create pressure for organisational reforms. The military itself participated in the market in the form of holdings, blotting out the opportunities for organisational reform. Consequently, innovation within the Turkish holdings only occurred through joint ventures with multinational corporations.

### Conclusion

The overall economic growth of Turkey has not been as dramatic and successful as that of South Korea. Our mafioso state model provides a reason for this. The Turkish top-down mafioso has never been as stable as its South Korean counterpart and was not as aggressive as the South Korean military in intervening in the market as a mafioso protector. Corporate organisational innovation remained relatively stalled in Turkey in part because the military state did not ban the holding company system, which could have provided incentives for further organisational innovation.

External shocks of market suppression through confiscation and/or the nationalisation of domestic industries owned by indigenous capitalists pose a great threat to such capitalists. The South Korean mafioso state restricted the *chaebol*’s diversification drives through a nationalised banking system and a ban on the holding company system. In other words, the ‘bigger and better’ mafia (the military) replaced the local mafia (the *chaebol*) in South Korea. The con-

sequence was that the *chaebol* actively promoted diversification and organisational growth through innovation. The state also aggressively promoted the *chaebol's* growth as long as one unit of business growth equalled another unit of growth in extracted payments.

In Turkey the 'bigger and better' mafia (the military) did not replace the local mafia (Holdings). There was a pattern of coexistence between the two, the military not intervening heavily in the market. The diversification of the Holdings did not encounter harsh state restrictions, nor did the state abolish the holding company system. Diversification was simply a means taken by the Holdings to increase their size and fend off hostile military intervention in their day-to-day decision making. With local monopolies not destroyed the mafioso state, innovation stalled. The country was not able to transform the Turkish industrial structure as in South Korea. On top of that, frequent military coups further reduced the military's grip on the economy, while the Holdings could cash in on political instability by continuing to expand through co-opting each new set of military leaders.

Nevertheless, similarities between South Korea and Turkey support our model of the top-down mafioso state, which emphasises the strong correlation between the top-down mafioso state and the highly centralised and diversified economic organisation of the private sector. In addition, the past economic performance of both countries stood out in each region (East Asia and the Middle East, respectively), although stark differences exist in terms of industrial structures and absolute economic performance.

## Notes

A substantially different version of this paper was presented at the 1998 Annual American Sociological Association meeting. We thank the editor, Shahid Qadir, anonymous reviewers and Jennifer Tae for comments and support. Of course, all remaining errors are ours.

- <sup>1</sup> For instance, Moran (1999) takes the view that the difference between South Korea and the Philippines is not as important as the similarity between them in terms of economic devastation wreaked by economic, social and political corruption (an example of market bypassing). Nonetheless, his class-based explanation, which emphasises the absence of a strong landed class as the key to further growth, is not sufficient to identify other factors that are conducive to South Korean-style rapid growth (for this, see Lie, 1998).
- <sup>2</sup> The Turkish land reform had a dual structure, in which a sweeping land reform of Korean magnitude occurred in the Western region (Western Anatolia), but was not extended to the Eastern Anatolia of the Kurdish settlements. The political reason for this was to control the Kurdish population by incorporating the landed class into Anatolian politics.
- <sup>3</sup> Social science is not equipped with the proper methodological tools with which to search correct causal sets for contradicting mechanisms (Elster, 1989). In the case of trust vs price, we simply cannot tell when social actors will follow the norms of price or those of trust, although both trust-based and price-based actions occur concurrently.
- <sup>4</sup> Przeworski (1986, 1991), for instance, considers 'shirking' by elites during the peak of political instability as the most important factor of political liberalisation in the former Soviet-bloc countries and military dictatorships.
- <sup>5</sup> Elite cohesion is a necessary condition for a stable top-down mafioso state, although it is not a sufficient condition. Waldner (1999: 9) recognises this point. However, other necessary conditions (eg economic success) can play more important roles in sustaining a top-down mafioso state (eg Korea). In this sense, initial elite cohesion in building a developmental state is not sufficient to explain organisational innovation in Korea.
- <sup>6</sup> A proactive managerial response to environmental instability has been the core topic of resource dependency theory. See Pfeffer and Salancik (1978) and Pfeffer (1981, 1982, 1992).

- <sup>7</sup> Following the Kemalist era, Turkey experienced three military coups in 1960, 1971 and 1980. Unlike in South Korea and in most Latin American countries, each military coup in Turkey lasted a couple of years and then transferred power to civilian forces. However, the military always plays a behind-the-scenes role (Saylan, 1988; Ozdemir, 1989; Shick & Tonak, 1987).
- <sup>8</sup> Between 1957 and 1958 Turkey received US\$55.8 million in loans from the World Bank, another \$25 million from the IMF, and \$75 million from the OECD countries. The total credits extended to Turkey in 1958 alone were \$359 million (Herslag, 1968).
- <sup>9</sup> Because of political suppression and censorship of the press such information was not revealed to the general public.
- <sup>10</sup> The military did not stay in power more than three years after each coup. There were civilian governments between the direct military regimes. After the military coup, the Turkish military preferred to transfer power to civilian forces, although it nevertheless remained a background organisation.

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