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A research to determine the role of process of Turkey's entry to European Union on the foreign direct investment

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Abstract

Nowadays direct foreign investments are important implements used especially by developing countries on the purpose of financing of economic development. Multinational Corporations' heading towards developing countries with the purpose of making more profit from international trade has provided a considerable extent of foreign resource entry into these countries. While foreign resource entry to Turkey had realized by the way of foreign indebtedness before, beginning from 2000s the way of direct foreign investments came into prominence.

Declaration of Turkey as a candidate country for EU in 2004 was evaluated as an important step in the process of its articulating with one of the most stable markets of the world by foreign investors and after this date massive increases occurred in the amount of direct foreign investments heading for Turkey.

Keywords: Turkey's economy, Foreign Direct Investments (FDI), developing countries, European Union.

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1. Introduction

Foreign Direct Investments are now used as indispensable means of economical growth for especially developing countries. Particularly since the 1980s, improvements in the transportation, communication, production and information technologies fields have accelerated the process of integration of national economies into the world economy. Countries make efforts to take more shares from the local markets by

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economical integrations on one hand and from global trade by Multicultural Companies on the other hand. Developing countries that can not use their existing resources wholly because of lack of capital make political and juridical arrangements to constitute appropriate base for Foreign Direct Investments.

In order to encourage the entry of FDI important steps have been taken at Turkey's economy since the second half of the 1980s. Efforts put forward, yielded results especially in 2000s, the amount of FDI which was 18 million dollars in 1980s eventuated over 16 billion dollars in 2011. It is real that the efforts to regional and global integration especially the customs union agreement to become effective in 1996, regulations about the acceptance of ICC International Court of Arbitration and signed Free Trade Agreements rised the credit note of Turkey in the eyes of foreign investors. But it can't be ignored that the year 2004 when Turkey was announced to be a candidate country to European Union became a threshold for the rise in the amount of FDI.

The aim of this project is to investigate whether Turkey's acceptance as a candidate country to European Union in 2004 is effective or not to rising amount in FDI after the period following 2004. Revealing whether Turkey's candidacy to enter to the EU is effective on the said rise in the amount of FDI or not will clarify economically the concerned arguments about this process which has lasted about half a century

2. A General Outlook of the Foreign Direct Investment Concept

Foreign direct investments are one of the essential principles that provide the integration of national economies with the world economy. In our day governments make an effort to integrate with international markets with the purposes of providing economic stabilization, reviving economic growth and improving the current social structure together with some other factors.

Foreign direct investment signifies a firms' establishing a facility, integrating existing production facilities or purchasing facilities outside of its origin country (Seyidoğlu, 2003:451). According to Karluk, apart from purchasing a firm or increasing the capital of an existing firm, foreign direct investment also means foreign investor's bringing his own management knowledge and technology together with him (Karluk, 2001:14).

Economy is defined in the OECD-Organization for Economic Cooperation and Development resources as "an international investment made by a resident investor with the purpose of establishing a continuous benefit relationship with a company which is built in another country" (OECD, 2008: 56). According to IMF-International Monetary Fund foreign direct investment is defined as "making a capital investment to an organization which operates in a foreign country with the purpose of gaining continuous profit and to maintain control". According to this definition there are four different forms of foreign direct investments; establishing a business abroad, purchasing at least 10% of an organization operating abroad, making new investments in a foreign country with the profits gained as a result of the investment done in that foreign country, increasing the capital between a registered office of an international company and foreign operations, being involved in activities such as providing loans or advance. On the other hand, there may be a relation between these capital movements and foreign-source dependency of these countries and it is possible to define capital movements as "regulator-destabilizing", "normal-abnormal", "speculative-commercial", "dependent-independent" in line with the purposes (Kindleberger, 1963:333).

François Perroux classifies investments in three sub models (Perroux, 1965:52): *Firstly*, it is possible that a company which made investments in country A can also make investments in neighbouring country B. For example a company which drills oil in Russia (country a) makes an investment for refinery in

Turkey (country B). In this case being a neighbouring country encourages the investors from other side of the boundary. *Secondly*, a company from country A which has made investments in country B can make another investment in a different field again in country B. For example, investments for infrastructure of a gas company, terminal investments. In some cases, investment in the country B may be connected to an agreement center in country A. *And thirdly*, a company which is in country A as a foreign investor directly affects the investment result in country B and also it indirectly affects and results in an investment in country C. A company established in USA encourages a network establishment in Germany and this encourages a network establishment in France.

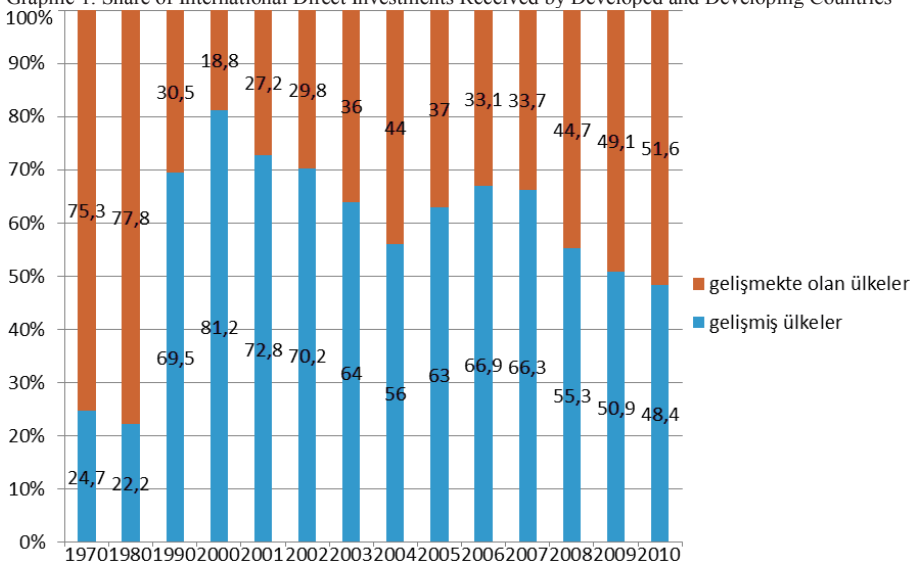
According to the 4875 numbered ‘Foreign Capital Law’ which became effective in 2003 foreign direct investor is defined as; “capital in cash, marketable securities, machinery and equipment, proprietary rights brought from abroad by foreign investor and domestic profits used in new investments, right of use and exploitation of natural resources, newly established companies and branches, company partnerships providing 10% voting right” (Official Gazette, 2003).

2.1. Development of Foreign Direct Investments in the World

Some political developments occurred since the Second World War and globalization process which gained speed as of 1980s have left their marks on the foreign direct investments' increase in amount and expansion in local areas.

As it is stated in the world investment report published in 2012, amount of foreign direct investment in the world has reached 1 500 billion dollars in the year 2011. Although it falls behind foreign direct investment amount of 2 000 billions in the year 2007, it becomes more of an issue when taking into consideration the financial crises happening in the countries during the recent years (T.C.K.B., 2012:55). Although foreign direct investments generally prefer developed market economies, countries with high growth rate are also preferred. Distribution of foreign direct investments between the developed and developing countries are given in the graphic below.

Graphic 1. Share of International Direct Investments Received by Developed and Developing Countries



Source: UNCTAD, 2012

According to this table, FDI share of the countries which have received approximately 70% of the total FDI has shown more increase in 2000 comparing the previous year. It is seen that it constantly decreases beginning from 2004 and recedes to 48% in 2010.

2.2. Development of Foreign Direct Investments in Turkey

Just as other developing countries, Turkey faces with problems of national savings and lack of foreign current which are indispensable factors in providing the sustainable economic growth. Foreign direct investments are important tools in the way of providing the financial need of Turkey's economy (Eğilmez, 2006). Foreign direct investment amount which was low in the 1980s started to have importance on the development of Turkey's economy as of 1990s.

Promoting the foreign capital was one of the primary goals of 24 January 1980 Resolutions. Actually foreign capital was seen as an important factor in development of Turkey's economy since the First Izmir Economic Congress organized in 1923 (Dura, 1991:10). In addition to this, the first legal regulation regarding the foreign capital is 6224 Numbered Foreign Capital Promotion Law which effectuated in 1954 (Erçakar and Karagöl, 2011:9). According to this law; agriculture and business sectors were opened for foreign capital entry, machinery and equipment, instruments import were authorized (Official Gazette, 1954). Cooperation made with foreign capital played a significant role in development of Turkish entrepreneurship; multinational corporations such as General Electric, Singer, Philips, Hoechst, Pirelli, Mobil, Shell benefited from foreign capital promotion laws introduced in 1950s (Ongun, 2001:328).

However the desirable foreign investors in the period before 1980 were not provided due to several reasons, initially political and economic instability (Erdal and Tatoğlu, 2002). Foreign capital entry into the sub branches of agriculture, mining and service industries was facilitated in virtue of providing stability, continuing economic reforms, extending the areas of activity of foreign capital with regulations in the period after 1980 Foreign direct investments coming to Turkey since 1980 were shown in the Table 1 below.

Table 1. Development of GDP and FDI in Turkey (With Current Prices Million \$ USA)

Years	GDP	FDI	Years	GDP	FDI
1980	68 789	18	1996	181 476	722
1981	71 040	95	1997	189 835	805
1982	64 546	55	1998	269 287	940
1983	61 678	46	1999	249 751	783
1984	59 989	113	2000	266 440	982
1985	67 234	99	2001	196 740	3 352
1986	75 728	125	2002	230 490	1 082
1987	87 172	115	2003	304 900	1 702
1988	90 852	354	2004	390 390	2 785
1989	107 143	663	2005	481 500	10 031
1990	202 380	684	2006	526 430	20 185
1991	151 041	810	2007	648 750	22 047
1992	159 095	844	2008	742 090	19 504
1993	180 422	636	2009	616 700	8 441
1994	130 690	608	2010	731 610	9 038
1995	169 486	885	2011	774 190	16 035

Source: Turkish Statistical Institute, DPT., T.C.KB.

24 January 1980 Resolutions have brought various facilities to foreign capital entry since economic growth was perceived as a result of external resources entry (Kepenek and Yenitürk, 2007:207). These primarily are; Law Regarding the Protection of the Value of Turkish Currency enacted in 1984, Free

Zones law effectuated in 1985, and regulations which gave permission to foreigners to make investments in Istanbul Stock Exchange in 1985. New regulations organized on Turkish financial sector started to bear their fruits at the end of the 1980s. While foreign investments made into Turkey was 18 million dollar in 1980, it exceeded 600 million in 1989.

Liberalization policies in financial sector which first started in 1980s continued their process in 1990s and gave permission to production and service operations of foreign investors in all sectors which are open for domestic investors.

In the period between the years 1990-2000, increase rate in foreign direct investments slowed down. In this period, foreign direct investment amount fell behind the permitted amount. Foreign direct investments of 684 million dollars made in the 1990, increased to 783 million dollars in 1999. Foreign direct investments were affected negatively by the financial crises happened in Turkey during this period, sudden decreases were seen in 1994, 1997, 1998 and 1999.

Financial crises that happened in the 1990s also took their effects in the first years of 2000s. Foreign direct investments which showed a significant increase by rising from 982 million dollars in 2000 to 3 352 million dollars in 2001, dramatically receded due to financial crisis happened in the late 2001. As for beginning from the year 2004 in which Turkey were accepted as a candidate country for European Union, foreign direct investment showed the greatest increase in the whole Republic history.

It is seen that 2004 was a significant threshold from the point of hot money coming to Turkey for making speculative portfolio investment. Foreign resources amount which came to purchase stock exchanges which are publicly-traded in Istanbul Stock Exchange or government debt securities and to benefit from high interest rates of the banks was 16,6 billion dollars in 2003, but it reached 32,8 billion dollars in 2004. Although it affected negatively from global financial crisis happened in 2008, foreign resources amount in question for the 2010 exceeded 115 billion dollars.

When it comes to the distribution of foreign direct investments made in Turkey into regions and countries, OECD countries and European Countries took the first places. Regional developments of foreign direct investments as of 2005 were shown in the table below.

Table 2. FDI Entry into Turkey According to the Geographical Distribution (Million\$)

	2005	2006	2007	2008	2009	2010	2011
Europe	6.652	14.574	12.974	11.367	5.234	4.920	12.369
European Union	5.006	14.489	12.601	11.076	4.928	4.719	12.369
EFTA Countries	41	75	262	202	281	196	324
Other European Countries	1.605	10	111	89	25	5	763
Africa	3	21	5	82	2	0	0
North Africa	3	12	0	82	1	0	0
Other African Countries	0	9	5	0	1	0	0
America	122	1.002	4.717	951	331	385	1.484
North America	114	969	4.223	891	312	378	1.423
Middle and South America	8	33	494	60	685	7	61
Asia	1.756	1.927	1.405	2.345	673	928	2.027
Near and Middle East Countries	1.680	1.913	804	2.280	439	518	1.835
Arab States of the Gulf	1.625	1.783	311	1.963	209	388	205
Other Asian Countries	78	17	797	161	312	455	505
Other	2	115	36	2	12	5	7
Total	8.535	17.639	19.137	14.747	6.252	6.238	15.887

Source: T.C.M.B.

It is seen that EU countries are ranked at the first place in the gradation of foreign direct investment made into Turkey. Especially after the acceptance of Turkey as a candidate country for EU, investments originating from EU increased from 6 652 million dollars in 2005 to 14 574 million dollars in 2006. However America-oriented financial crisis emerged in 2008, negatively affected the investors from EU as well as other countries of world and aforementioned investments made in Turkey in 2009 decreased around 6 million dollars in comparison with the previous year. With the improvement of confidence in international markets, interest of EU oriented direct investments to Turkey continued as of 2011 and incoming resource amount exceeded 12 billion dollars.

Up to this day, in terms of foreign direct investment made in Turkey, Holland takes first place with a total investment amount of 27,9 billion dollars it is followed by Germany (12,6 billion dollars), Austria (10,5 billion dollars), England (9,1 billion dollars), USA (7,9 billion dollars), United Arab Emirates (7,2 billion dollars) and France (7 billion dollars).

3. Development of Relations between Turkey and EU

Turkey's relations with EU started with Ankara Agreement signed with the European Economic Community on 12 September 1963 and enacted on 1 December 1964. With the termination of preparation period stipulated by the agreement, an Additional Protocol was signed on 13 November 1970 and enacted in 1973. Customs Union Agreement signed on 1995 enacted in 1996. In the Helsinki Summit held on December 1999, candidate country status was given to Turkey and in the European Council Summit held on 17 December 2004 Turkey was declared as a candidate country and accession negotiations were started in October 2005. Aforementioned negotiations are still in progress.

Up to this day, thirteen of 33 sections (Science and Research, Enterprise and Industry Policy, Statistics, Financial Audit, Trans-Europe Networks, Consumer and Health Protection, Intellectual Property Law, Companies Act, Information Society and Media, Free Movement of Capital, Taxation, Environment, Food Safety, Veterinary and Phytosanitary Policy) were opened for negotiations, and one of these (Science and Research) were closed temporarily (EU Commission, 2012:4).

3.1. Effect of European Union Accession Process to Direct Investments Coming To Turkey: Empirical Analysis

In our study, with the aforementioned time sequence analysis, it was researched if a structural breakage happened or not by examining the effects of foreign direct investments coming into Turkey after Turkey's being accepted as a candidate country for European Union. "Generally, changes created by changes in economical structure of economical policies or a significant development happening in a specific industry can be considered as reasons for structural breakage in economy."(Sevüktekin, M and Nargeleçekenler, M., 2010:399) Within this framework, a positive structural breakage seems probable in the development process of foreign investments made in Turkey, following the 2004 in which Turkey was accepted as a candidate country. In the same manner, results of our analysis confirm this thought. The great extent of positive structural breakage in the aforementioned macroeconomic time sequence is an indication of the effect of acceptance as a candidate country for European Union on the increase of the preferability of Turkey in terms of foreign investments.

At the same time, while examining the breakage that developed out of the process of Turkey's candidanship to European Union, the economic and political developments on a regional and global scale should not be disregarded.

3.2. Empirical Method, Variables and Model Results

Data used in the analysis are generated by organizing data published by Turkish Statistics Institute and Ministry of Development.

Annual time sequences between 1980-2011 were used in the analysis. Turkey's economy entered into a structural transformation beginning from the implementation of Economic Resolutions of 24 January 1980. Therefore, year 1980 was regarded as the start of the examined period. Time interval of the analysis consists of two sub periods: First one is the period of 1980-2003 before Turkey's declaration as a candidate country for European Union. And the second one is the period between 2004-2001 after its declaration as a candidate country. As our model tries to measure, it was examined if a structural change happened in the course of foreign direct investments made in Turkey between these periods. The Gross Domestic Product used as a dependent variable in the analysis was 1987-based real Gross Domestic Product and was denominated in the dollar. Foreign direct investments (FDI) were used as independent variables and were denominated in the dollar.

Dependent Variable: GDP				
Method: Least Squares				
Date: 03/18/13 Time: 23:37				
Sample: 1980 2011				
Included observations: 32				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
DYY	29.75691	3.055925	9.737446	0.0000
C	151269.7	23016.66	6.572182	0.0000
R-squared	0.759650	Mean dependent var		267120.8
Adjusted R-squared	0.751638	S.D. dependent var		223650.3
S.E. of regression	111458.2	Akaike info criterion		26.14115
Sum squared resid	3.73E+11	Schwarz criterion		26.23276
Log likelihood	-416.2584	Hannan-Quinn criter.		26.17151
F-statistic	94.81786	Durbin-Watson stat		0.675737
Prob(F-statistic)	0.000000			

The null and alternative hypotheses of structural breakage for 2004 as shown below:

H0: There is no structural breakage.

H1: There is a structural breakage.

Chow Breakpoint Test: 2004

Null Hypothesis: No breaks at specified breakpoints

Varying regressors: All equation variables

Equation Sample: 1980 2011

F-statistic	14.97129	Prob. F(2,28)	0.0000
Log likelihood ratio	23.27194	Prob. Chi-Square(2)	0.0000
Wald Statistic	29.94258	Prob. Chi-Square(2)	0.0000

As a result of the analysis H_0 hypothesis was rejected. In other words, there is a breakage in 2004: in our examination time sequence composed of 32 observations, a level and declination variable (breakage) is seen after the 25th observation. Aforementioned breakage comes up steeply in the development of foreign direct investment in proportion to Gross Domestic Product. In the time sequence before the 25th observation, while an average fixed scattering on a lower level is seen, with the changes in the level and declination of the sequence after the breakage time an increase occurred in time. Thus it is also seen by the help of figure that a change occurred both in its level and declination. This change is interpreted as an effect of the increase in the foreign direct investments (FDI) which are the subjects of the study, seen after 2004 on Gross Domestic Product. On the other hand, as from the 28th observation a negative inclined breakage is seen and it indicates the negative effect of the decrease in the FDI on Gross Domestic Product.

4. Conclusion

Just as other developing countries, Turkey is trying to provide external resource entry for the financing of their investments since the internal savings fall behind. It is seen that beginning from 2000s, there have been significant changes on the structure of the foreign resources that came into Turkey. While resource entry to economy was only provided by loans and the way of portfolio investment, there has been a considerable amount of increase in the foreign direct investment since 2004. While foreign direct investment amount was below 3 billion dollars in 2004, it exceeded 10 billion dollars in 2005. In a longer process, while in the period between 1980 and 2004 17 billion foreign direct investments were made, this number reached 108 billion dollars only in the period between 2004 and 2012.

Our time sequence analysis has shown that in the year in which Turkey was accepted as a candidate country for European Union, there was a positive breakage in the increase of foreign direct investment coming to Turkey. In other words, Turkey's making progress in the full membership in the EU, make the country attractive from the point of foreign investors. Unlike other member countries, although Turkey's EU process has been continuing since half a century, the fact that no member country was rejected encourages the investors. Thus, increase in the prices of real estate properties after 2004, improvement in the transaction volume of Istanbul Stock Exchange, positive opinions of international assessment bodies are all indications of the improvement in the confidence of Turkey's economy. Turkey's declaration as a candidate country for EU, especially made EU-oriented investors think about the possibility of Turkey's integrating with the world's most reliable market smoothly. On the other hand, it is certain that there are some factors in the aforementioned increase of the foreign direct investment, other than the declaration of Turkey as a candidate country for EU.

First and foremost, a part of the foreign investors, preferred Turkey for its geographical position which has a strategically importance. Investors who want to become a regional power have made investments in Turkey together with other countries of their region. In this sense, Turkey's being a Middle Eastern region which faces west, good relationships established with Middle Asian Turkish Republic and especially with Azerbaijan are significant issues for foreign investors.

Despite the fact that legal infrastructure is incomplete, acceptance of international arbitration law in 2001 reassured foreign investors. Also decidedly implementation of stabilization measures given were taken after the economic crisis happened at the end of the same year, by the government, is another factor that develops the trust of foreign investors to Turkey's economy.

Nonetheless, at the end of the corporatisation process, especially having sold the big banks to foreigners and although this increased the entry of foreign resources, aforementioned foreign resources did not create sufficient employment capacity in the economy.

Especially beginning from 2004, foreign resources that headed for Istanbul Stock Exchange, government debt securities, interests allowed on deposits were not converted directly into foreign investments but remained as an element of risk which creates a vulnerability effect in the economy.

As a conclusion, Turkey's economy which is the sixteenth economy in the world and sixth in Europe provides opportunities that can be regarded as motives to be preferred by foreign investors:

In consequence of the reconstruction after the economic crisis of 2001, financial part was strengthened, stability was provided in the economic growth. Turkey's characteristic as an investable country is affirmed by various credit evaluation bodies. Although statistical data show that population growth will decrease in the long term, as of today two thirds of Turkey's population consist of young. Moreover it has the feature of potential market from the point of foreign investors due to its geostrategic position between Middle East countries, Europe and Middle Asia Turkish republics.

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