Università
Ca'Foscari
Venezia

Corso di Laurea magistrale (*ordinamento ex D.M. 270/2004*)
In Relazioni Internazionali Comparate – International Relations

Tesi di Laurea

Ca' Foscari
Dorsoduro 3246
30123 Venezia

Turkey and the New Global Economic Context : The Expansion of National Firms into the Romanian Market

Relatore
Ch. Prof. Vera Costantini
Correlatore
Ch. Prof. Giancarlo Corò
Laureando
Stella Martini
Matricola 818099

Anno Accademico
2012/2013

A

CONTENTS

TURKISH PRONUNCIATION GUIDE

A, a = short “a” as in “art” or “star”

Â, â = faint “ya” sound following preceding consonant, as in

“harekât” (harek-yahh-t)

E, e = “eh” as in “send” or “tell”

İ, i [dotted i] = as “ee” in “see”

I, ı [undotted i] = “uh” or the vowel sound in “fuss” and “plus”

O, o = same as in English “phone”

Ö, ö = same as in German

U, u = “oo”, as in “moon” or “blue”

Ü, ü = same as in German, or French “u” in “tu”

C, c = pronounced like English “j” as in “jump”

Ç, ç [c-cedilla] = “ch” as in “chair”

G, g = always hard as in “go”

Ğ, ğ = not pronounced; lengthens the preceding vowel slightly

H, h = never silent

J, j = like French “j”

S, s = always unvoiced as the “s” in “sun”

Ş, ş [s-cedilla] = “sh” as in “show”

Z, z = always soft as in “please”

ABSTRACT

Con questo lavoro intendiamo analizzare la recente espansione economica delle imprese turche nei mercati internazionali. In particolare, ci interessa capire quali strategie esse adottino nel penetrare le economie dei paesi vicini alla Turchia, prendendo come caso specifico la Romania. Il recente successo di gruppi aziendali provenienti dai mercati emergenti sta attirando molta attenzione, poiché preannuncia un cambiamento progressivo nelle strutture e gli andamenti dell'economia internazionale. Le imprese turche sono parte di questo fenomeno, nonostante la Turchia abbia un impatto limitato rispetto ad altre potenze economiche più influenti a livello globale.

Abbiamo scelto la Romania come fulcro di questa ricerca per una serie di ragioni. Innanzitutto, il suo recente ingresso nell'Unione Europea la rende un passaggio privilegiato verso opportunità redditizie in Europea occidentale. Inoltre, seguendo una tendenza più generale, le aziende turche iniziano il loro processo di internazionalizzazione in paesi vicini alla madrepatria per poter acquisire i vantaggi strategici necessari per espandersi in mercati più sviluppati. Un altro punto di forza della Romania in quanto destinatario di investimenti diretti esteri (IDE) è l'ampiezza del suo mercato : con 21 milioni di abitanti si posiziona seconda in Europa Centro-orientale dopo la Polonia. Inoltre, la sua forza lavoro istruita e ancora competitiva la rende ancora più invitante, afferma l'Istituto Italiano per il Commercio Estero (ICE) di Bucarest.

La Romania attira sostanziosi investimenti turchi, e quindi anche il nostro interesse, anche per i saldi legami che esistono tra i due paesi sia a livello politico che umano. Infatti, i rispettivi governi conducono relazioni diplomatiche e politiche intense, soprattutto a partire dal crollo del regime socialista, cooperando a diversi livelli. Tra i due paesi esiste inoltre una relazione storica molto antica, rappresentata dalla presenza di una comunità di turchi che abitano il territorio romeno dal XIII secolo e che, come ogni minoranza presente in Romania, hanno oggi una propria rappresentanza parlamentare. Tutto questo ha permesso la creazione di solidi legami fra le due popolazioni, che sono sopravvissuti al periodo comunista per poi fiorire dopo la sua caduta (Iordache 2005).

Per capire i variegati rapporti internazionali coltivati da Ankara, sia a livello politico che economico, è utile fornire qui una panoramica generale delle sue scelte politiche più recenti. Dal punto di vista storico, culturale e politico, da più di un secolo la Turchia è attratta da tre poli di civiltà : l'Asia Centrale, da legami culturali, linguistici e affettivi; il mondo arabo, dalla condivisione della tradizione religiosa; l'Europa, soprattutto a partire dai cosiddetti movimenti di occidentalizzazione che nacquero nell'Impero Ottomano durante i secoli XVIII e XIX e durante i quali le élite turco-ottomane si consideravano di fatto europee.

La Turchia è un paese ad alta importanza strategica, sia dal punto di vista politico/militare, che economico. Durante la guerra fredda rappresentava il pilastro orientale della NATO contro il nemico sovietico e il supporto al "mondo libero" nel Medio Oriente (Jorland 2011). Economicamente, essa rappresenta un passaggio importante verso l'Asia Centrale e le sue risorse naturali. Nonostante la fine della guerra fredda causò lo stravolgimento del sistema delle relazioni internazionali del tempo, non favorì la nascita di un nuovo ordine mondiale ben definito. In questo contesto, la Turchia perse il suo ruolo chiave, ma guadagnò la possibilità e la libertà di sfruttare la sua posizione di perno eurasiatico per il proprio interesse.

Il risultato fu l'emergere di una nuova tendenza alla fine degli anni '90. Infatti, il Ministro degli Affari Esteri Ismail Cem introdusse una politica più aperta nei confronti delle repubbliche turcofone dell'Asia Centrale e della Grecia. Dobbiamo però aspettare l'ascesa del partito Giustizia e Sviluppo (AKP) di Recep Tayyip Erdoğan nel 2002 per assistere a una vera e propria svolta nelle relazioni della Turchia con i suoi paesi vicini.

Considerata la riluttanza dell'Unione Europea ad accettare l'ingresso della Turchia nella stessa, quest'ultima ha progressivamente adottato politiche più autonome, in cui l'Europa non è più il motore delle riforme. Pur confermando la sua vicinanza all'UE, il governo dell'AKP è anche interessato a costruire relazioni di vicinato stabili e pacifiche. Stabilendo nuovi equilibri nella regione, la Turchia vuole presentarsi quale mediatore dei conflitti che vi scaturiscono. Questo tipo di politica estera mira a rinforzare il ruolo strategico del paese rafforzando il suo vantaggio di essere un ponte fra due mondi e una guida per molti. La nuova politica di vicinato è presentata da Ahmed Davutoğlu,

Ministro degli Affari Esteri dal 2009, nel suo libro “Profondità strategica”. Questa politica, chiamata “Zero problemi con i vicini” è volta alla soluzione dei conflitti regionali e alla realizzazione di una maggiore integrazione tramite il commercio, il trasferimento di tecnologie e la circolazione delle persone.

La profonda interconnessione che al giorno d’oggi lega la sfera politica a quella economica ha stimolato il nostro interesse verso una maggiore comprensione delle relazioni economiche che emergono da questo orientamento politico e con cui procedono fianco a fianco. Il mondo di oggi è governato da forze di mercato che restano oscure per la maggior parte di noi. Corporazioni enormi sono diventate attori globali molto potenti, che possono influenzare le scelte di imprese più piccole, ma anche di stati nazionali. In Turchia, l’élite politica è strettamente legata a quella economica e la recente crescita degli investimenti diretti esteri in uscita è dovuta anche a scelte politiche favorevoli.

L’obiettivo di questo studio è dunque analizzare il comportamento e le strategie di queste imprese che, pur mantenendo saldi legami con la madrepatria, si espandono all’estero e permettono alla Turchia di ottenere un peso sempre maggiore sulla scena internazionale. Al fine di garantire una comprensione chiara dell’attuale relazione economica fra Bucarest e Ankara, presenteremo una panoramica storica dello sviluppo economico di entrambi i paesi. Inoltre, per capire meglio i modelli di investimento delle imprese Romania, discuteremo i paradigmi generali degli investimenti diretti esteri, in particolare quelli in uscita dai paesi emergenti.

Il primo capitolo è interamente dedicato alla storia economica della Turchia, partendo dalla fondazione della Repubblica fino ai giorni nostri. Tuttavia, ci concentreremo sugli ultimi vent’anni, durante i quali la Turchia ha attraversato tre crisi economiche violentissime che ne hanno profondamente segnato la società nel suo complesso. Una crisi monetaria scoppiò nel 1994 a causa di enormi richieste di prestito del settore pubblico combinate con gravi errori delle politiche per finanziare il deficit. Il risultato fu il crollo della produzione del 6 percento, l’aumento dell’inflazione fino a tre cifre per la prima volta nella storia della Turchia, la perdita di metà delle riserve della Banca Centrale e il deprezzamento della lira turca del 50 percento in tre mesi. (Celasun 1999).

L'economia si riprese in fretta ma rimase instabile e, solo sei anni più tardi, il paese dovette affrontare un nuovo crollo, che ebbe conseguenze ancora più drammatiche. Infatti, a causa di fattori sia interni che esterni, una prima crisi della moneta colpì verso la fine del 2000, ma il vero colpo arrivò nel febbraio del 2001. Gli effetti sull'economia reale furono devastanti e la Turchia ne uscì profondamente cambiata. Tenteremo di comprendere le principali cause e conseguenze di questa crisi all'interno del capitolo. Infine, esamineremo la crisi economica e finanziaria globale del 2008, concentrandoci sui principali effetti che ha avuto sull'economia turca. Causando un improvviso collasso della domanda esterna, ha intaccato soprattutto le esportazioni turche e di conseguenza, il PIL. Gli investimenti sia interni che esteri sono crollati e lo stesso hanno fatto i consumi. Tuttavia, dopo il declino iniziale, l'economia turca si è ripresa e sta attraversando un periodo di forte crescita. Sebbene i flussi di investimento estero in entrata siano incoraggianti, l'affidabilità dei capitali finanzianti il deficit non lo è altrettanto; al contrario, solleva ultimamente numerosi dubbi (The Economist 2012).

Successivamente, il capitolo due riguarda l'espansione delle imprese multinazionali (IMN) provenienti da economie emergenti, con un'analisi teorica delle modalità e strategie di investimento. Nonostante la letteratura economica non abbia ancora approfondito con teorie esaustive il fenomeno dell'internazionalizzazione delle multinazionali dei mercati emergenti, evidenzieremo le caratteristiche principali di questo fenomeno partendo dalle teorie tradizionali sugli IDE. Una delle principali differenze fra queste nuove multinazionali e quelle provenienti da paesi avanzati sta nel fatto che esse si espandono all'estero ad uno stadio molto precoce della loro crescita, al fine di ottenere all'estero le risorse strategiche necessari al loro successo. Le multinazionali turche condividono questo modello e molte di loro, specialmente le holding multi settore, stanno diventando reali attori globali. La destinazione principale degli investimenti turchi è l'Unione Europea. Parte della sua attrattiva sta nella sua ampia capacità di mercato e nei suoi canali di distribuzione già funzionanti, ma le imprese turche mirano soprattutto a ottenere accesso diretto a risorse non tangibili strategiche, quali tecnologie e marchi (Deng 2012). Nonostante questa posizione privilegiata dell'Europa, altri paesi stanno diventando destinazioni significative per gli IDE turchi e minacciano di battere il record europeo. Principalmente le repubbliche ex-

sovietiche dell'Asia Centrale, ma anche l'Europa centrale e sud-orientale attraggono investimenti sempre maggiori.

Data l'importanza di questi mercati per le imprese turche, il capitolo tre è totalmente dedicato a loro, in particolare al processo di transizione che essi hanno affrontato in seguito al collasso dell'Unione Sovietica e dei suoi alleati. Capire questo processo è fondamentale per interpretare le loro attitudini economiche e il loro ruolo sulla scena internazionale. Per aprire l'economia alle forze di mercato, le cosiddette economie in transizione hanno dovuto attraversare una trasformazione economica lunga e dolorosa sotto la guida dell'FMI e delle altre istituzioni economiche internazionali. Nonostante l' accordo generale sui modi e tempi della transizione, qualche voce critica si è sollevata. Cercheremo di trattare la questione all'interno del capitolo analizzando il processo di transizione da diverse prospettive. Successivamente, studieremo il caso romeno, con un approfondimento sugli investimenti esteri. La Romania diventò un polo attrattivo per gli IDE con un certo ritardo rispetto agli altri paesi in transizione, tuttavia, ha raggiunto buoni risultati nel corso degli anni 2000. Il processo di privatizzazione e l'imminente adesione all'UE, uniti ad un quadro legislativo riformato, agirono come fattori di richiamo. La maggior parte degli investimenti in Romania proviene dall'Europa occidentale ed è diretta principalmente al settore manifatturiero. Il profondo coinvolgimento della Romania nei mercati internazionali e la sua instabilità politica resero il paese altamente esposto alla crisi del 2008, che lo colpì violentemente e i cui effetti sono visibili ancora oggi.

Infine, il quarto e ultimo capitolo è dedicato alla relazione economica tra Turchia e Romania, in particolare all'analisi dell'espansione imprenditoriale turca nel mercato romeno. Come abbiamo accennato in precedenza, i due paesi sono strettamente uniti da legami sfaccettati, tra cui molto rilevanti sono gli investimenti delle imprese turche. Essere una comunità storica ha aiutato questi imprenditori a fondare attività di successo e attirare altri uomini d'affari, creando così una rete e una comunità imprenditoriali consolidate. Le prime attività erano di piccole dimensioni e principalmente impiegate nel settore alimentare. Nel corso degli anni, tuttavia, gli imprenditori turchi si allargarono in più campi e oggi operano nella maggior parte dei settori. Essi sono ben integrati nella società ospitante e, nonostante il brusco ridimensionamento che gli IDE

turchi hanno subito con la crisi del 2008, gli imprenditori affermano di voler mantenere forti relazioni economiche con la Romania nei tempi a venire.

INTRODUCTION

This work aims at analyzing the recent economic expansion of Turkish business groups in foreign markets. The global surge of emerging markets' firms is attracting a lot of attention, as it announces a progressive change of the international economic structure and trends. Turkish enterprises are among this group, although with a relatively limited impact compared to other globally oriented economic powers. Therefore, it is out interest to understand how firms from Turkey operate in the international market and which strategies they pursue when entering Turkey's neighboring economies, in particular Romania.

We chose Romania as the focus of this study because of several reasons. First of all, it recently entered the EU and therefore, it represents an easy passage to profitable opportunities in Western Europe. Coherently with a general tendency, Turkish companies often start their internationalization in close countries in order to gain the required strategic assets allowing them to penetrate more developed economies. Moreover, with its population of around 21 million people, Romania is the second largest market (after Poland) in Central and Eastern Europe, thus representing an attractive destination for foreign direct investment (FDI). Its educated and still competitive workforce makes it even more profitable, claims the Italian National Agency for Foreign Trade in Bucharest (ICE).

Another element making Romania attractive for Turkish firms investing abroad, and thus for us, is the excellent relationship the two countries share at the political and human level. Indeed, the respective governments conduct intense diplomatic and political relations and cooperate at several levels. Moreover, since the 13th century Romania have been hosting a Turkish community, which, like all minorities living in Romania, has its own representatives in Parliament. This created solid ties among the two populations, which survived the communist period and flourished after its end (Iordache 2005).

In order to understand the variegated international ties that Ankara cultivates, both at the economic and political level, it is useful to provide a general overview of its recent

political choices. From the historical, cultural, and political point of view, Turkey has been attracted by three civilization poles for more than one century : Central Asia, by its cultural, linguistic and affective links; the Arab world, by its shared religious tradition ; and Europe, mostly since the so-called « Westernization » movements that rose in the Ottoman Empire during the XVIII and XIX centuries, during which the Ottoman-Turkish elites considered themselves as Europeans.

Turkey is a country with high strategic importance, both at the political/military and the economic level. During the Cold War it represented the orient pillar of NATO against its Soviet Enemy and the support to the "free world" in the Middle East (Jorland 2011). Economically, it is a significant passage to Central Asian natural resources. Although the end of the Cold War caused a deep upheaval in the system of international relations of that time, a new defined order did not come into light. In this context, Turkey lost its key role, but it gained the possibility and freedom to exploit its position of Euro-Asian pivot for its own interest.

Indeed, a new tendency started to emerge at the end of the 1990s. The Ministry of Foreign Affairs Ismail Cem introduced a more open policy towards the Turkish-speaking republics of Central Asia, and Greece. However, we have to wait for Recep Tayyip Erdoğan's Justice and Development Party (in Turkish : Adalet ve Kalkınma Partisi, AKP) to come to power in 2002, in order to witness a true turning point in Turkey's relations with its neighbors.

Given the European hesitations towards its entry to the Union, Turkey has started to adopt more autonomous policies, where Europe is no longer the engine for reforms. While still confirming Turkey's closeness to Europe, the AKP government is rather interested in building stable and peaceful relations with its neighboring countries. By establishing new balances in its region, Turkey tries to present itself as the mediator of the conflicts bursting there. This kind of policy aims at reinforcing the strategic role of the country, by strengthening its advantage of being a bridge between two worlds and a leading figure for many. The new neighborhood policy is well explained by Ahmed Davutoğlu, Minister of Foreign Affairs since 2009, in his book titled "Strategic Depth". This policy, called Zero Problems with Neighbors is directed towards the solution of

regional conflicts and the realization of a deeper integration through trade, technology transfer, and the circulation of people.

The high interconnectedness existing today between the political and the economic sphere stimulated out interest towards the understanding of the economic relations emerging out of this political orientation and proceeding hand in hand with it. The world of today is governed by market forces obscure to the majority of the people. Giant corporations have become powerful global players and can influence the choices of smaller companies and even of national states. In Turkey, the political elite is strongly tied to the economic one, and the recent surge in outward foreign direct investment (OFDI) is also due to favorable political choices.

Therefore, the main objective of this study is to analyze behavior and strategies of these firms which, by expanding abroad while keeping solid links at home, help Turkey become more relevant on the international stage. In order to guarantee a clear comprehension of the current economic relationship between Bucharest and Ankara, we will provide a historical overview of both countries' economic development. Moreover, to better understand the investment patterns of Turkish firms in Romania, we will discuss the general paradigm of foreign direct investment, in particular that from emerging economies.

The first chapter is entirely dedicated to Turkish economic history, starting from the foundation of the Republic up to the present day. However, we will concentrate on the last twenty years, during which Turkey experienced three violent economic crises that heavily marked its society as a whole. A currency crash erupted in 1994 due to huge requirements for public sector borrowing combined with major policy errors in financing the deficit. As a consequence, output fell by 6 percent, inflation rose to three-digit levels for the first time in Turkey's history, the Central Bank lost half of its reserves, and the Turkish lira depreciated by 50 percent in three months (Celasun 1999). The economy recovered quickly, yet it remained unstable and Turkey had to face another downturn only six years later, with even more dramatic consequences. Indeed, because of different internal and external factors, a first monetary crisis hit Turkey at the end of 2000, but the real crash arrived in February 2001. The effects of real

economy have been devastating and Turkey came out of this crisis deeply changed. We will try to understand the main causes and consequences of this crisis in the chapter. Finally, the 2008 global financial and economic crisis is also examined. Causing a sudden collapse of the external demand, it mostly affected Turkey's exports and therefore, GDP. Domestic and foreign investments fell sharply, and so did consumption. However, after the initial decline, the Turkish economy recovered rapidly and is now experiencing high levels of growth. The FDI performance is also encouraging, but the reliability of the capital flows financing its deficit are raising widespread concern (The Economist 2012).

Subsequently, chapter two is about the expansion of multinational companies from emerging markets, with a theoretical analysis of their investment patterns and strategies. Even though economic literature has not provided exhaustive theories about emerging markets' multinational companies' (EMNCs) internationalization yet, we will highlight the main characteristics of this phenomenon by starting from traditional FDI theories. One of the most important differences between EMNCs and multinationals from developed economies is that they pursue internationalization at an early stage of their growth in order to gain the required strategic assets abroad. Turkish multinational companies share this pattern, and many of them, in particular multi-industry holdings, are becoming true global players. The most preferred destination of Turkish outward FDI is the European Union. Part of its attractiveness lies on its large market capacity and well-established distribution channels, but above all, Turkish enterprises aim at acquiring direct access to strategic intangible resources, mainly technology and brands (Deng 2012). Despite the European preferential position, other countries are becoming significant hosts of FDI and are on the way to challenge that record. The former Soviet Republics of Central Asia most of all, but also Central and South Eastern Europe countries are attracting Turkish investment.

Given the significance of these countries as hosts of Turkish FDI, chapter three is all dedicated to them, in particular to the transition process they lived after the collapse of the Soviet Union and its allies. Understanding this process is fundamental to interpret their economic attitudes and their role in the international stage. In order to open the economy to market forces, all so-called transition countries had to go through a harsh

and painful economic transformation, under the guidance of the IMF and the other major international institutions. Despite widespread agreement on transition modes and timing, a few critical voices also raised. We will try to address this question in the chapter by analyzing the transition process from different perspectives. Subsequently, we will study the Romanian case, with a focus on its FDI performance. Despite initial delay in attracting foreign investments compared to other Central and Eastern Europe countries, Romania attained high FDI levels in the 2000s. The privatization process and the forthcoming adhesion to the European Union, together with a revised legal framework, acted as significant pull factors. The bulk of investment to Romania comes from Western Europe and is mainly directed to the manufacturing sector. The Romanian deep involvement with foreign markets and an unstable internal political situation made the country highly exposed to the 2008 global crisis, which hit Romania hard and whose effects are yet to be eliminated.

Finally, the fourth and last chapter is dedicated to the economic relationship between Turkey and Romania, in particular to the analysis of Turkish enterprises' expansion in the Romanian market. As we stated before, the two countries are firmly tied by multifaceted relations, one of the most relevant of which is investment of Turkish entrepreneurs. To be a historical community helped them found successful activities and attract other businessmen, thus creating a functioning and well-established business community. Early ventures were small and mostly engaged in food production. During the years, however, Turkish entrepreneurs increasingly enlarged their industry range and today, they operate in almost all sectors of the Romanian economy. Indeed, they are well integrated in the host society and despite the serious slowdown that Turkish FDI experienced after the 2008 global crisis, the entrepreneurs are said to be willing to maintain strong and durable investment relations in Romania for a long time to come.

CHAPTER 1

TURKISH ECONOMIC PERFORMANCE : HISTORICAL OVERVIEW AND A FOCUS ON AKP

1.1 – Introduction to the chapter

Turkey is a restless and variegated country, and it has always been so during its fairly short life. Due to numerous social, political, and economic factors (that will not be analyzed here), it maintains deep internal differences and contradictions, which affect its economic outlook. Modern industries coexist with pockets of subsistence agriculture, and major western Anatolia cosmopolitan centers of industry, finance, and trade grow next to the eastern, relatively underdeveloped part of the country (Chapin Metz 1995). Despite its contradictions, Turkey has been experiencing an extraordinary economic growth in very recent years, mainly sustained by the industrial and service sector. Today, it is included among those emerging economies experiencing large economic successes and gaining increasing global influence.

Indeed, Turkey's growth rate has withstood well to the test of the 2008 global crisis, inasmuch after the initial decline, it quickly reverted to respectable rates following the rebound. However, if we look beyond growth and the macro-economic policies behind it, we can see a less encouraging picture. In particular, despite macro-stability and confidence, domestic savings have fallen, and unemployment does not give significant signs of decrease. Moreover, the external deficit has kept on widening, and investment has remained low. Considering Turkey's still high reliance on external borrowing, one can easily understand that the economic boom it is experiencing does not have true solid foundations (Rodrik 2012).

Recent economic events helped uncover important vulnerabilities of Turkey's economy, as well as its strong points and assets. In its history, Turkey went through numerous crises, which have left long traces and deep wounds in the country and the population. Economic crises were often followed by, and were the trigger of, major

transformations, both at the economic and the political level (Öniş 2010). Now the country is going through another crisis, yet deeply different from the previous ones. Many analysts praise the way the government took to exit the catastrophe. But will it be able to build a strong and secure economy and share the benefits with all sectors of the population? The challenge is hard to face and other experts say that first results are not encouraging.

We will now look back at the economic history of the Turkish Republic, by analyzing the crises it went through and by concentrating on the events of the last decade.

1.2 – From the origin of the Republic up to the "lost decade"

Economic growth is considered one of the fundamental, if not the most important, parameters to measure one country's economic performance. The economic analysis of ancient empires also relies on it. We can say that, throughout the centuries of its supremacy in the Middle East and the Mediterranean, the Ottoman Empire "created strong economic growth ending in long-lasting sustainable welfare creation that lasted for more than 500 years" (Görmez and Yiğit 2009). However, at the end of its life, the Ottoman Empire had lost all its favorable economic conditions. The lack of social rule of law prevented the already scarce resources to finance a new development initiative, and the huge external debt represented a very heavy burden.

The last fifty years of the Empire were characterized by frequent and disastrous wars bringing to "border losses and devastating destruction of an already scarce infrastructure" (Görmez and Yiğit 2009). World War I and the following bloody internal conflicts increased this destruction. Basic infrastructure like schools, roads, and railways were lacking, and the economy was largely based upon agriculture, while the manufacturing industry practically did not exist. Despite this, until the early twentieth century, no economic or financial stability concerns were felt, and the main worry of the young Turkish Republic was to guarantee social law and order in a society whose human capital had been destroyed by dramatic global and national conflicts.

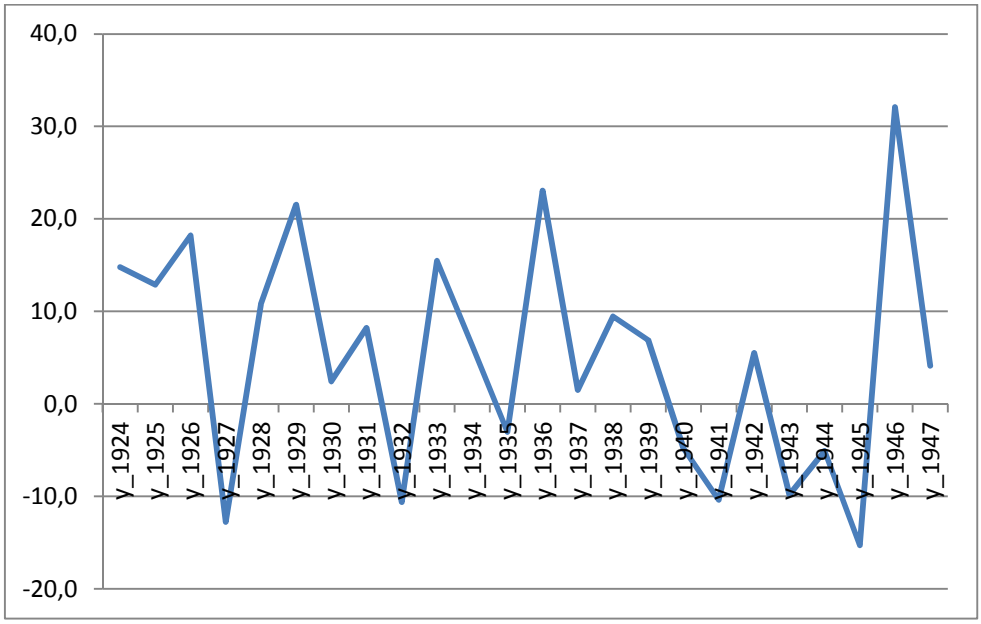
The Republic of Turkey was founded in 1923, after the War of Independence that followed the collapse of the Ottoman Empire in the late 1910s. The early phases of

political construction, led by the first President of the Republic, and hero of the War of Independence, Mustafa Kemal, named Atatürk, took Western methods and institutions as a model. The new political class undertook deep social and cultural reforms, the most significant of which was the adoption of secular principles in the political life of the country (Celâsun and Rodrik 1989).

In this context of state reorganization, often carried out through armed conflict, and of chaotic world conditions, they were concentrating all resources in the struggle for survival. Two sets of economic policies were challenging the national leadership the most : the renegotiation and servicing of the external debt, and the dismantling of what remained of the capitulations.[1]

Figure 1. GDP growth rate at constant prices, 1924-1947

(percent)



Source : TURKSTAT

According to Görmez and Yiğit (2009), approximately 77 percent of the Turkish population in the 1920s lived in villages, 82 percent of the working population was employed in agriculture, 6 percent in industry, 5 percent in trade, and 7 percent in the

[1] The Capitulations were legal contracts through which the Sultan accorded specific privileges (usually economic) and granted concessions to European citizens living in the borders of the Empire.

service sector. The share of agriculture in national income was 67 percent, while that of industry was only 10 percent. However, agricultural production was primitive, it utilized obsolete machinery, and did not have resources for innovation. The dominance of agriculture is reflected in the high volatility of the early years of the Republic, caused by the impact of good and bad weather conditions.

Atatürk and his party, the CHP (Republican People's Party, in Turkish : *Cumhuriyet Halk Partisi)* "engineered a state building project, modernizing the economy and strengthening the control of the state over the economy and society" (Acemoğlu and Robinson 2013). As part of this project, they encouraged industrialization and reformed the Turkish economic institutions under certain aspects. However, this did not involve any provision including large segments of the population. On the contrary, the state played a major role in the economy and the private business class was deeply related to it. Indeed, through subsidies and protection, the state aimed at keeping the control over the economy and society.

During the 1930s, like many other countries, Turkey was severely hit by the consequences of the dramatic fall of the American stock exchange. However, in the same years, a first wave of import-substituting industrialization (ISI) policies took place, and a national entrepreneurial class started to develop. The official ideology of this time is called "etatism" (statism), a sort of middle way between Soviet-style total planning, and Western-style market economy system. This government-led industrial drive succeeded in mobilizing resources, generating growth and considerable structural change in output. The public sector was given the primary role in savings generation and in "carrying out key entrepreneurial functions in industrial development and technological improvement" (Celâsun and Rodrik 1989). However, all state institutions were still under the control of the CHP, which had no intention to remove its constraints from the exercise of economic, political, and social power (Acemoğlu and Robinson 2013).

There followed World War II, preventing the Republic to create a strong economic and financial stability. Although Turkey did not enter the war, the chaotic external environment and high defense costs negatively affected the economic development

efforts and reduced the growth rate. Therefore, in the early 1940s, the country faced severe commodity shortages, and was dominated by black market and extremely high inflation rates. Immediately after the war, Turkey received international aid under the Marshall Plan and US bilateral assistance programs. However, in order to receive the aid, one major condition was required : a shift in economic priorities from industrial development towards industrial production. At the same time, also Turkey's political structure was under transformation. For the first time since the foundation of the Republic, it was witnessing the political change from one-party rule towards a multiparty parliamentary system (Celâsun and Rodrik 1989).

For all these reasons, the statist, protectionist model was reformed in the second half of the 1940s; the deep state involvement in the economy was relaxed, and financial incentives were given to private entrepreneurs. It is arguable that the events of the first half of the twentieth century prepared the ground for the subsequent economic growth, starting in the 1950s, with significant structural change and economic transformation (Öniş 2010).

The 1950 elections saw the rise of the DP (the Democratic Party, in Turkish : *Demokrat Parti), the contributor to the economic boom of the 1950s.* indeed, that was the decade of the liberal turn and the beginning of welfare creation. Turkey began to integrate into the world economy, still mostly relying on agriculture. Private banking started to rise, investment increased, and agriculture output abruptly rose. Despite these transformations, the economic production of Turkey was still prerogative of a few established companies, which the ruling party did not intend to undermine. On the contrary, it had the precise design to "turn connections with the conservative Anatolian businesses and landowners into a clientelistic patronage network". Just like its predecessor, and many of its successors to be come, the DP strengthened its control over the state institutions. Coherently, "once electorally challenged, it did not hesitate to pursue unsustainable macroeconomic policies, with significant costs on the Turkish economy" (Acemoğlu and Robinson 2013).

During these early decades, the Republic of Turkey was experiencing a rapid transformation from an agricultural towards an industrial society, which created

distortions in the labor market and led to unequal income distribution. As a result of agriculture modernization, small farms became economically nonviable and many rural people migrated to urban areas. However, many of them were lacking skills needed in modern industry and therefore, could find employment only in the informal sector of the urban economy. Moreover, the growth rate was fairly high, thus contributing to high levels of unemployment, especially in the post-war period (Chapin Metz 1995).

The unstable character of the Turkish economy was emerging, and especially from this moment onward, it was characterized by the alternation between periods of growth and downturn. Indeed, the country would be hit by deep crises, both at the economic and the political level. The military coup of 1960 can be considered the first dramatic turning point leading to an important shift of the economic strategy of the country.

In fact, the 1960s are the decade of the so-called import-substitution phase, when policy makers started to implement heavy protectionist economic policies. The industrial capital was directed to the domestic market, and a five-year plan was enforced under the direction of the newly established State Planning Organization (SPO). Almost every aspect of the economy was planned, with the public sector gaining importance. Interestingly, the decade was characterized by a long period of sustainable growth, reaching an average 5 percent level, and stability was the dominant general feature (Görmez and Yiğit 2009). Indeed, development policy improved considerably from 1962 onward, with a successful noninflationary resource mobilization and industrialization. However, trade policies had a restrictive and largely ad hoc character, discriminating exports and limiting imports without creating a “selective and increasingly competitive import-substitution pattern in the economy” (Celâsun and Rodrik 1989).

The maintenance of an increasingly overvalued fixed rate regime caused the tension on the external balance to intensify in 1969. An IMF-supported stabilization program was needed and implemented in order to avoid the emergence of a payment crisis. It involved a number of liberalization objectives, among which a maxi devaluation. This measure contributed to the rise in exports and the expansion of GNP in the early 1970s.

This period also witnessed the first massive arrival of remittances from workers abroad, whose emigration had accelerated in the late 1960s.

Despite this encouraging performance, economic conditions rapidly worsened in the 1970s, when the heavy dependence of Turkey on foreign energy revealed itself as a double-edge sword. Two global oil crisis shook the whole world, and Turkey failed to adapt to high energy prices as well. Policy makers did not implement medium and long term measures, and the country was hit by a persistently high and volatile inflation (Görmez and Yiğit 2009). The unstable political situation of that time did not help the economy, and neither economic nor financial stability programs were proposed.

The economic and the political sphere have always been interdependent in Turkey, with major economic crises having political consequences, and major political crises having economic implications (Öniş 2010). Indeed, the domestic conflicts among social groups and political parties during the 1970s and 80s worsened the impact of economic measures, and Turkey ended the 1980s with an inflation rate of above 100 percent.

As we stated before, the economic activity in the 1970s collapsed, due to a shortage of raw materials, including energy, for the production of basic goods. On the other hand, financial stability was guaranteed, thanks to "the lack of market influence on deposit and credit rates in addition to negative interest rates imposed on the banking system by the regulators" (Görmez and Yiğit 2009). However, the absence of a capital market in Turkey in the pre-1980 period was creating significant difficulties to the private firms increasingly participating in industrial activities. Moreover, the government was not able to adopt proper measures up against price distortions, including overvalued exchange rates, and large public sector deficits (Celâsun and Rodrik 1989).

After a few years of fluctuating performance, with encouraging rise of investment and growth, and some improvements in income distribution, 1977 is remembered as the year of the big crash. Turkey found itself in a "monumental debt crisis", causing high decline of growth, and the rise of inequalities, mostly at the expense of urban workers and the peasantry. Several reasons laid behind this collapse, yet it can be argued that the fundamental element accelerating the crisis was the dynamics of the debt accumulation process itself (Celâsun and Rodrik 1989). Indeed, the process was based on a type of

foreign borrowing called “convertible Turkish Lira deposit”, designed to attract the savings of Turkish nationals working in foreign countries and other cash deposits that might have been earned in black-market trade, smuggling, or the mis-invoicing of imports and exports.

The Central Bank granted interest rates on foreign exchange deposited in Turkish commercial banks 1¾ points above the Euromarket rate, while also guaranteeing the foreign exchange value of both principle and interest. Starting from 1975, the program was broadened to allow all non-residents to hold deposits (IMF financial programming and policy). The key feature of this scheme was that it protected domestic borrowers from all exchange risk. This had the fatal consequence of engendering an ever-expanding spiral of over-borrowing by the private sector. In a context of current account deficit, the public sector experienced an investment boom, yet “sustained only to the extent that foreign banks were willing to increase their exposure to Turkey at an ever-increasing pace. Once foreign banks slowed their net lending, the edifice collapsed” (Celâsun and Rodrik 1989).

Besides deep economic troubles, Turkey in the 1970s was shaken by unprecedented political violence, mainly driven by the opposition between left-wing and right-wing political organizations. Politics itself was paralyzed, with no credible government able to implement significant measures of any kind. This chaotic situation paved the way for a military coup, the third of the Republican history, which took place on September 12th, 1980. From a political and social point of view, this coup d’état had dramatic consequences. It undermined the Turkish democratic system, by imposing an authoritarian constitutional framework, de-institutionalizing the party system, and creating an impediment for the country’s quest for EU membership. From the economical point of view, the 1980 coup played an important role in the subsequent radical neo-liberal restructuring (Öniş 2010).

The government had declared its intention to liberalize the economy already before the coup, with the so-called January 24 program, whose initial objectives, such as lowering the inflation rate, fostering GDP growth, and liberalizing external trade and the financial system, were attained very soon (Ertuğrul and Selçuk 2001). The military

regime retained Turgut Özal, the main creator of the new program, first as Deputy Prime Minister, later as elected Prime Minister, in 1983. Indeed, the program was maintained and sustained by the military rule, and the new liberalizing measures were further extended and strengthened (Celasun and Rodrik 1989).

Table 1. Turkey's basic economic indicators, 1985

A. Major indicators, 1985	
Population	49,8 mln
Employment	15,9 mln
Unemployment rate	12,6 percent (excluding labor surplus in agriculture
GNP	53,0 US$ bln at current prices
GNP per capita	1.064,0 US$ at current prices
Gini coefficient	0,51 (1973) - 0,50 (1978) - 0,525 (1983)

B. Sectoral structure, 1985	GDP	Employment
Agriculture	18,4%	58,9%
Industry	30,6%	22,9%
Services	51,0%	28,2%

C. Growth rate (percent)	1953/63	1963/73	1973/77	1977/79	1979/85
GNP	4,8	6,7	0,1	1,2	3,6
Agriculture	3,2	2,3	6,8	2,8	2,4
Manufacturing	8,5	10,1	7,9	-1,7	5,7
GNP per capita	2,0	4,0	4,7	-0,9	1,2

Source : Celasun and Rodrik 1989

Turkey was one of the earliest cases of neoliberal restructuring in line with the Washington Consensus. Therefore, the post-1980 strategy benefited from debt relief, balance of payments assistance, and policy support of the major bilateral creditors and multilateral lending institutions. The size and time of this external assistance was indeed beneficial for Turkey's recovery in the early 1980s. Conformity with the IMF and the World Bank policies helped debt relief agreements and bilateral lending (Celasun and Rodrik 1989).

Thanks to export-led growth strategy, the annual growth rate of real GDP registered a positive trend throughout the 1980s. Between 1981 and 1988 the average growth was

5.8 percent, and the country did not experience any recession. Industrial production also increased in this period. However, starting from 1988, Turkish economy entered a new phase called “boom-bust”, when the average growth rate decreased and became very volatile during the 1990s. The main reasons behind this performance can be found in the unsuccessful disinflationary efforts and debt-financing policies of the government, as part of the exchange rate policy (Ertuğrul and Selçuk 2001).

During early 1980s, Turkey suffered of a financial shock, when a number of private banks were bankrupt, also because of fraudulent conduct. These banks were bound to merge with public ones, even if the reformed regulatory framework was yet to be completed and refined. Indeed, the liberal reform with the new financial market infrastructure “needed a better oversight, which the Turkish economy learned later on at a heavy price” (Görmez and Yiğit 2009). Although financial deepening increased over the 1980s, inflation at relatively high levels supported inefficiencies in the financial service provision, and short-term gains were eventually lost.

Turgut Özal was the key figure of the liberal turn of the 1980s. According to Öniş (2004a), he was also “the most influential political leader since the time of Kemal Atatürk” (and before the advent of Recep Tayyip Erdoğan, we can easily say today). His multifaceted personality, both as moderate Islamist and as Western-style modernizer, granted him broad support, from the conservative masses of the periphery of the Turkish society, to the secular elites. As a technocrat, he was respected both in national and transnational circles. All over the 1980s, and despite political fragmentation, he brought economic continuity to Turkey, by playing different institutional roles, from Deputy Prime Minister in charge of Economic Affairs during the military regime, to Prime Minister elected with the Motherland Party (ANAP) both in 1983, and in 1989, and even to President of the Republic until his death in 1993.

The reforms of the 1980s were highly financed by the IMF and the World Bank. This was facilitated by Özal’s leadership, his credentials, and his negotiating skills, which also helped the domestic business community to gain confidence and operate in a more attractive environment. In this design, closer relations with the European community were seen as fundamental for Turkey’s consolidation of the reform process. Moreover,

it could help the Turkish industry to become more competitive at the domestic front. Turkey applied for full membership in the European community in mid-1987. Although being rejected, the initiative paved the way for the Customs Union of 1996, that represented a crucial step for full-scale liberalization of the Turkish economy (Öniş 2004a).

Özal's approach to reform was direct and confident : the implementation of market-oriented measures needed to be quick and without impediment. New bureaucratic organizations, such as the Privatization administration, and the Under-Secretariat of Treasury and Foreign Trade, were created in order to implement key elements of reforms (Öniş 2004a). However, to be more effective, economic processes had to bypass democratic rules like bureaucratic and parliamentary norms. Representative democratic institutions were seen as limiting and even detrimental to free market progress. Moreover, the economic growth of this period was not translated into a broad-based improvement in standards of living. On the contrary, it fostered increasing inequalities and was largely sustained by domestic monopolies and traditional connections. Corruption became the main business vehicle (Acemoğlu and Robinson 2013).

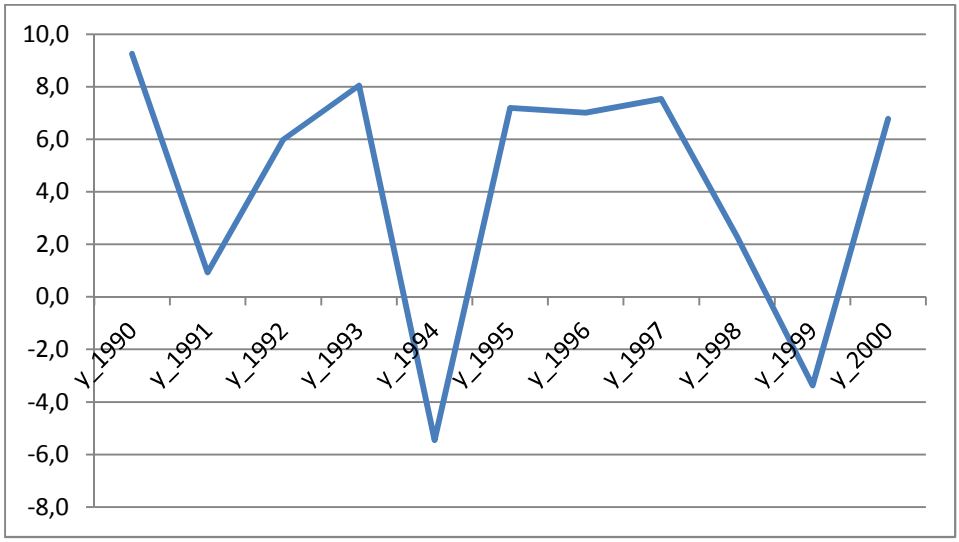
In 1989, a critical step was taken towards external liberalization : the so-called regulation on "convertibility". Foreign exchange controls on capital outflows were removed, and both the current and the capital account completely liberalized (Erdem 2009). Yet the Turkish economic environment was one of high macroeconomic instability in absence of an adequate institutional framework to regulate the financial sector. The overvaluation of the Turkish Lira and high interest rates became instrumental in attracting short-term and highly speculative capital flows. These inflows of capital contributed to intensify the degree of instability of the Turkish economy, "as political actors used these funds to finance rising budget deficits thereby postponing costly adjustment decisions to the future" (Öniş 2004a). The 1989 liberalization of capital account would be recognized as a significant catalyst for future economic and financial turmoil.

1.3 – Turkey coping with crises : from the 1990s up to the 2001 economic disaster

Because of the disastrous economic performance characterizing their whole duration, the 1990s are commonly defined the "lost decade" of Turkish economy (Görmez and Yiğit 2009). Even though hyperinflation has never become a threat, inflation remained high and volatile in those years, while economic growth witnessed one of the worst performances of its history. Public sector borrowing maintained high levels and very high interest rates, and domestic debt stock continued to increase.

Figure 2. GDP growth rate at constant prices, 1990-2000

(percent)



Source : TURKSTAT

The highly fragile character of its economy brought Turkey to a major financial crisis in 1994. At the macro level, unsustainable fiscal balance and insufficient primary surplus to counter-balance external debt fragilities are said to have played a key role in pushing the economy into double deficit. Stabilization programs were continuously delayed, and the Turkish Lira sharply depreciated in January 1994. In the need of capital, the Treasury started to sell bonds with a maturity of three months at an interest rate of 50 per cent. The prompt intervention of the IMF did not succeed in sustaining recovery nor preventing more catastrophic successive breakdowns (Görmez and Yiğit 2009).

At the micro level, financial liberalization allowed credit interest rates to rise to excessively high levels, thus increasing the cost of firms relying on credits and the number of insolvents. Speculative activities increased heavily, and financial instruments such as repos were legalized. Moreover, external financial liberalization and tax-exemptions broadened the spectrum of financial activities, also raising the risks of operations. A few banks went bankrupt and others were transferred to the Saving Deposit Insurance Fund (SDIS) up until the 2000s (Erdem 2009).

The 1994 financial crisis was indeed one of the worst recessions in Turkish history, with a contraction rate of the economy of 6 percent in 1994. However, Turkish economy experienced a quick, even though short-term recovery, with a growth rate of about 8 per cent the following year. Some reasons behind recovery are the fact that the banking system came out of the crisis relatively unharmed, the private sector regained external borrowing opportunities quite quickly, and the Turkish Lira went through real depreciation (Yilmazkuday and Akay 2007).

Despite the negative aspects hitherto listed, the 1990s are also the decade in which important steps towards the building of strong regulatory institutions were taken. Indeed, the country needed the effective implementation of key aspects of the neoliberal program, such as privatization and banking sector reform. Yet, the main initiatives were coming from external subjects, such as the Customs Union with the EU of 1996, which brought to the creation of the Competition Board, or the IMF, supporting the introduction of the Banking Regulatory and Supervisory Authority (BRSA) (Öniş 2004a).

The EU-Turkey Customs Union

The relations between Turkey and the European Union (at that time European Economic Community, EEC) date back to the 1960s, with the creation of the Association Agreement, the so-called Ankara Treaty, in 1963. The agreement envisaged three main objectives : the creation of a Customs Union (CU) between the EEC and the Republic of Turkey free mobility of labor and eventually the integration of Turkey into the EEC.

The Additional Protocol of 1973 modified the Treaty and outlined 1996 as the final deadline for the CU, which was actually enacted on January the 1st, 1996.

This Customs Union required Turkey to eliminate all customs duties, quantitative restrictions, all charges having equivalent effect to customs duties and all measures having equivalent effect to quantitative restrictions in trade of industrial goods with the EU. Moreover, Turkey was required to adopt the Common Customs Tariff (CCT) of the European community (EC) against third parties imports, and to adopt all preferential agreements that the EU has concluded and will conclude with third countries (Togan 2012).

The scope of the CU is limited to industrial products and processed agricultural products, which can circulate freely between Turkey and the EU. Agricultural products and coal and steel products are not covered.

By boosting the process of trade liberalization, the Customs Union played a very important role for Turkish industry consolidation and competitiveness in the international market (Öniş 2004a). It gave powerful tools to Turkey to reform its economy and has "credibly locked Turkey into a liberal foreign trade regime for industrial goods and holds a promise of Turkey's participation in the EU internal market for industrial goods" (Togan 2012).

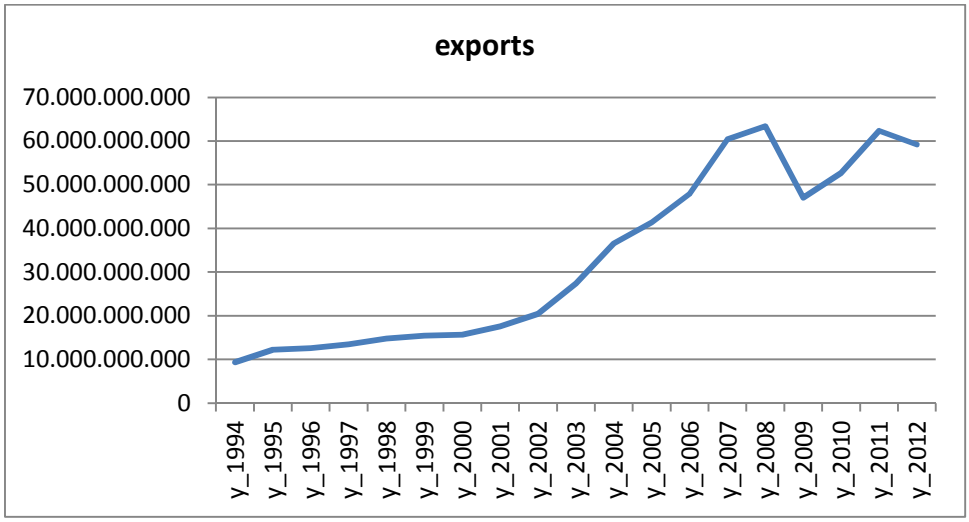
Turkey has made and is still making hard efforts to fulfill the requirements of the CU, which are yet to be completed. It also accepted and implemented a number of measures and provisions in order to stay in line with European trade standards. A strong political will to integrate into the European economy as a way to achieve EU membership was sustaining all these efforts and costs. However, the EU is showing a behavior at least ambiguous, when not clearly opposed to Turkey's accession, which allows numerous voices to rise against Turkey's blind accordance to European directives.

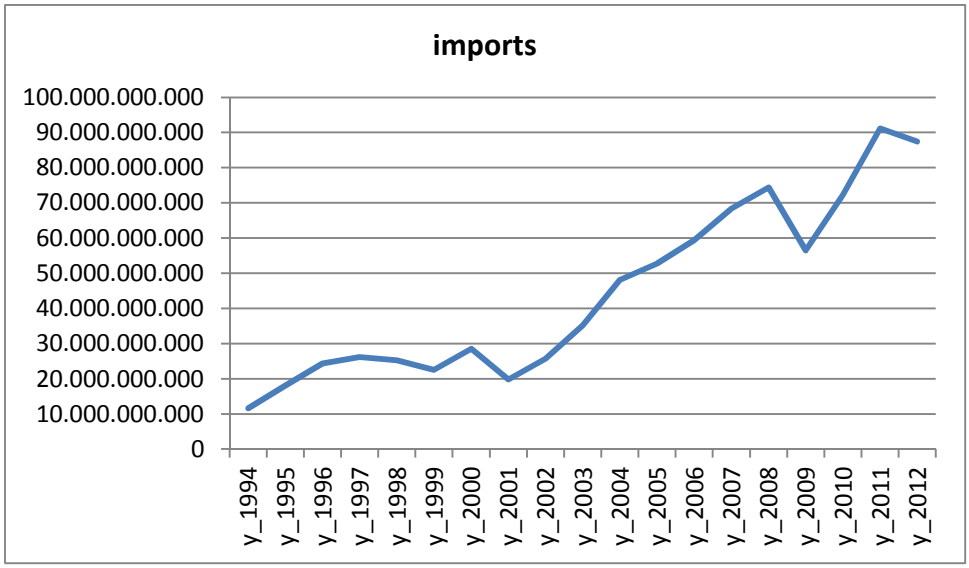
Today, the EU and Turkey enjoy a deep trade relationship. By 2012 the EU ranked number one in both Turkey's imports and exports, while Turkey ranked 7th in the EU top import and 5th in export markets.

However, it is fair to state that this relation have been downsizing in recent years. Indeed, the EU share in Turkey's exports has fallen from 56 percent in 2000 to 47 percent in 2011. This can be explained by considering the relative decline of the European economy compared to more dynamic markets, especially in the Middle East and other natural resource-rich countries (Gros and Selçuki 2013).

Figure 3 and 4. Turkish trade with the EU27, 1994-2012

(US$)





Source : TURKSAT

Textiles and clothing, and transport equipment dominate EU imports from Turkey, accounting respectively for 7.3 + 17.5 percent and 24.2 percent. There follow other machinery (10.7) and agricultural products (7.5). The main EU exports to Turkey include transport equipment and other machinery (19.1 + 18.2 percent), chemical products (16.9), and fuels and mining products (10.7) (source : EUROSTAT).

The late 1990s show again variable and fluctuating trends, preparing the ground for the unprecedented economic and financial crisis of 2000-2001. Under the guidance of an IMF Staff Monitored Program, the Turkish government started to implement a disinflation program, which obtained some results concerning inflation rate and fiscal imbalances, “but it could not relieve the pressures on the interest rates” (Ertuğrul and Selçuk 2001). Since inflation was attributed to large budget deficits, the stabilization program included strategies for debt reduction, in particular an ambitious privatization scheme. Foreign ownership was favored by a constitutional amendment allowing international arbitration for contracts between the state and foreign investors. The government also agreed to completely liberalize capital flows and to reduce trade restrictions. Public spending was to be downsized by reducing labor costs and reforming social programs. To do so, public sector employee wages were to be frozen in real terms, and the financing and accessibility of important social programs, such as social security, was to be cut (Dufour and Orhangazi 2009).

In contrast with tight budgetary policies, banking laws were amended to force the Savings Deposits Insurance Fund (SDIF) to recover insolvent banks for restructuring or liquidation, while forbidding to provide liquidity to any bank not under its full control (IMF 1999a). At the eve of the financial crisis, the SDIF was given full authority to borrow from the Treasury, and full protection was granted to the creditors and depositors of domestic deposit-taking banks, “ostensibly to restore confidence in the program. […] Thus while social spending and public wages were capped, investors were guaranteed full reimbursement for any loss incurred” (Dufour and Orhangazi 2009).

Chronic inflation was causing severe stability problems in the Turkish economy. Moreover, the fiscal balance of the public sector deteriorated because of several factors :

the Russian crisis of 1998, the general elections in 1999, and two devastating earthquakes in August and October 1999. Therefore, in December 1999, the government signed a three-year Standby Agreement (SBA) with the IMF and initiated an exchange-rate-based stabilization program (ERBS). The main purpose of this program was to carry out extensive structural reforms mostly directed to the public finance (Yilmazkuday and Akay 2007). The CPI and WPI were to be brought down to 25 and 20 percent respectively by the end of 2000, and to a single-digit level by the end of 2002, starting from 63 percent in 1999. The inflation rate was anchored to a preannounced crawling peg designed to move with anticipated inflation. A gradual shift towards a more flexible exchange rate regime was planned to begin in July 2001 (Akyüz and Boratav 2003).

Initially, the program was successful. Inflation started to fall slowly, while interest rates decreased quickly. Meanwhile, domestic currency appreciated steadily, thus fuelling a boom in domestic demand and leading to a widening of the current account deficit. At the same time, fiscal consolidation and structural reforms lagged behind, and market anxiety around SBA program started to spread over (Macovei 2009).

During the first ten months of 2000, the economy enjoyed a positive net capital flow of $12.5 billion on account of a large net inflow by nonresidents, financing the mounting current account deficits, as well as net outflows of residents and increases in reserves. On the other hand, residents were reluctant to concentrate their asset holdings in Turkey, and a net acquisition of foreign assets was registered. Significantly, over the 90 percent of total inflows by non-residents were debt-creating, with FDI and portfolio investment reaching no more than 1/10 of net private capital flows (Akyüz and Boratav 2003).

Crisis broke out in November 2000, when non-resident capital flew out of the country in a rapid and dramatic way. Many reasons lay behind this event, we summarize them here, referring to Akyüz and Boratav (2003). They include : disappointing inflation results for October, unexpectedly high monthly trade deficits, political difficulties encountered in privatization, worsening relations with the EU, the influence of the economic situation in Argentina, and the disclosure of irregularities in the banking

system and a criminal investigation into several banks taken over by the Saving Deposit Insurance Fund (SDIF). Only after having signed a new agreement with the IMF in December 2000, financial markets could stabilize to some extent. By mid-January, international reserves had been replenished to the pre-November level, and interest rates had fallen below 60 percent (Yilmazkuday and Akay, 2007).

The IMF authorities declared to be fully confident that the program was working and that positive results were to be expected for the year 2001. However, the underlying weaknesses of stability were not relenting, as the slow decline in inflation prevented the Turkish lira to devaluate. Moreover, in January 2001, "the first signs of an economic slowdown started to appear". In February, the sustainability of the domestic public debt was at risk, as maturities in Treasury bill auctions started to shorten, and interest rates rose by 70 percent (Yilmazkuday and Akay, 2007).

The last straw arrived when a harsh dispute between the Prime Minister and the President broke out about the measures to be taken, followed by a massive attack on the lira on February 21st, 2001. The major index of the Istanbul Stock Exchange dropped by 14 percent, and a massive capital flight caused the international reserves to deplete by $5 billion. The whole financial system was threatened, and the authorities decided to let the lira float, thus leading to a depreciation of around 40 percent against the dollar. The devaluation proved very costly for the government. Indeed, while the government was fighting to maintain the peg, interest rates rose to triple digits, so that implicit and explicit liabilities of the government highly increased, as well as the strain on private institutions (Akyüz and Boratav 2003) .

On the whole, the crisis pushed the government to borrow an amount equivalent to 17 percent of GNP, that is an increase of 66 percent in its foreign liabilities. The IMF heavily contributed to these funds, with an unprecedented loan of almost 9 billion SDRs. In the year of the crisis, the amount owed by the government to multilateral agencies increased from $11.4 billion to $22 billion (Dufour and Orhangazi 2009).

Following the crisis, the total cost of external debt servicing grew up to 17 percent of GNP, and was still exceeding pre-crisis levels three years later. In 2001, total interest charges on the public debt surpassed tax revenues, thus increasing by more than 20

percent from the previous year. This debt service burden was a hard obstacle for Turkeys economy : after five years, the interest charges paid to the IMF still had not diminished. A large portion was spent to reimburse foreign financial institutions through the bailout of the domestic institutions that had borrowed from them. Therefore, foreign indebtedness heavily lied on the domestic population at large.

As a consequence of international debt commitments, “Turkey was effectively pushed into debt peonage” (Dufour and Orhangazi 2009). Indeed, the IMF and other international creditors were provided with leverage vis-à-vis government policymakers, both at the moment of lending, and as long as the debt overhang persisted. In this way, the government experienced in this way a loss of autonomy, which along with the large interest burden, largely came in exchange for a bailout of international capital, through an increase of the liabilities of the government. International capital was protected through the quick enactment of laws that considerably reduced the risks. More specifically, Turkish banks were granted full guarantee of loans, which, along with the necessity for the SDIF to take over any insolvent bank, amounted to the nationalization of the debt of all financial institutions facing the risk of insolvency.

The breakdown of the peg and the financial turmoil had catastrophic consequences for the real economy : real GDP declined by 5.7 percent, investments collapsed in volume terms by 30 percent, and the industrial output dropped by 8.7 percent yearly. Moreover, the manufacturing sector registered a decline of 9.4 percent, with the automotive industry declining by 26 percent. Exports of goods and services did not record a significant downturn, while imports collapsed by 8 percent in volume terms, as a consequence of weakened domestic demand and sharp currency depreciation. Along with contracting economic activity, unemployment rose from 6.5 in 2000, to 8.4 in 2001, to 10.4 in 2002. Moreover, manufacturing wages suffered a correction of about 15 percent in real terms. The depreciation of the lira and the recapitalization of banks provoked a staggering increase in public debt, which doubled from 38.2 percent of GDP at the end of 2000, to 74.1 percent of GDP at the end of 2001. Bank were highly affected by the crisis, with a loss to the budget of about 30 percent of GDP. The decline of the lira did not stop, reaching a depreciation rate of about 60 percent against the US dollar from February to October (data from the World Bank and Macovei 2009).

The reasons behind this crisis are several and not easy to determine. The IMF gave its explanation by referring to a stalemate in the implementation of policies agreed, as well as on some adverse external developments. It substantially blamed “political uncertainty, policy slippages, and a weakening of economic fundamentals” (IMF 2001b). Responsibilities were also given to a problematic banking sector and to the failure to undertake corrective fiscal actions when the current account widened.

By contrast, a number of Turkish economists challenge these explanations, by arguing that they do not take into account any possible miscalculation in the design of the stabilization program, nor any misguided intervention in the crisis. On the contrary, the reform policies are said to have been based on a poor diagnosis of economic conditions of the country and on programs lacking solid theoretical underpinnings. Though recognizing that the extent of fiscal profligacy and financial fragility were a high obstacle to surpass in order to stabilize economy, it is also fair to state that, in many respects the Turkish economy was worse after two years, than it was on the eve of the December 1999 stabilization program. In particular, “all targets set for the real sector for 2001, including those revised in the middle of the year, have been missed by a large margin” (Akyüz and Boratav 2003). The exchange rate-based stabilization program is also criticized by arguing that, in the absence of measures designed to increase domestic savings capacity and export competitiveness, it was likely to generate stability in the short-run at the cost of amplifying instability in the future (Öniş 2006).

Nevertheless, it is commonly agreed that one of the crucial elements behind the crisis was the combination of a fragile banking sector together with a high public sector borrowing requirement. Indeed, the high current account deficit and the appreciation of the Turkish lira were not enough on their own to precipitate the crisis : a fragile banking system and triggering factors proved to be determinant. The banking system was accumulating risk in the period before the crisis, for example because of an increase in currency and maturity mismatches, as well as a rise in non-performing loans. Therefore, “the banking system was highly vulnerable to capital reversals” (Özatay 2002). Although both commercial and state-owned banks had mismanaged risks before the crisis, the risk accumulation was not homogenous throughout the system. On the one hand, private banks were more exposed to the exchange rate risk, while on the other,

state banks were more open to interest rate risk. Consequently, “the prudential indicators of the banking system had deteriorated to the point where the sector could no longer ensure a smooth financing of the public debt and was actually undermining its sustainability” (Macovei 2009).

Just like it happens in many situations of this kind, the crisis had different impacts on different subjects. Indeed, while the Turkish workers and the whole population suffered of heavy repercussions, “international capital emerged largely unhurt from the crisis, thanks to protections introduced that guaranteed foreign investments at public expense” (Dufour and Orhangazi 2009). In fact, via foreign direct investment and external debt, international capital could increase its assets, subsequently increasing income repatriated from Turkey. Moreover, losses registered by insolvent domestic banks were also covered by the public. Paradoxically, large domestic banks even benefited from the crisis, thanks to increased interest income.

The financial and economic crisis of 2000/2001 and the previous events that Turkey went through, confirm the assumption that financial liberalization without a strong institutional and regulatory environment is a significant source of vulnerability. A sound bank regulation and supervision, effective law enforcement, and good governance in the private and public sector are required to allow effective liberalization policies. During the 1990s, Turkey did not comply with these conditions : inflation remained long high, and public sector borrowing requirements did the same. Moreover, the delays in setting up an adequate Banking Regulation and Supervision Agency (BRSA) and in implementing other structural and privatization measures did not help (Macovei 2009).

Differently from other emerging economies experiencing harsh crisis, such as Argentina, Turkish society did not experience a wave of massive social and political unrest in the aftermath of the crisis. The 2001 Argentinean economic crisis, which presented common elements with the one hitting Turkey, was followed by a major wave of protests directed both to the government and to the IMF. In contrast, Turkish society did not blame the IMF at large, but it recognized the coalition government in office as the main responsible for the economic catastrophe they were living. According to Öniş (2006), “the communitarian elements that exist in Turkish society, based on informal

ties of reciprocity, have historically played an important role in preventing the worst forms of poverty and deprivation. The strength of the informal economy proved to be a key element in containing violent forms of reaction also in the post-crisis context".

The governmental reaction to the crisis was determined and effective. In the spring of 2001, the government embarked on a set of structural reforms and macroeconomic policies under the New Economic Program. Recovery was supported by a medium-term policy perspective, thus allowing GDP to grow again robustly in the second quarter of 2002. The recovery of domestic demand, in particular of investment, largely contributed to general improvement. The regained political stability, with a single-party majority government emerging from the November 2002 elections, contributed to bring economic stability as well (Macovei 2009).

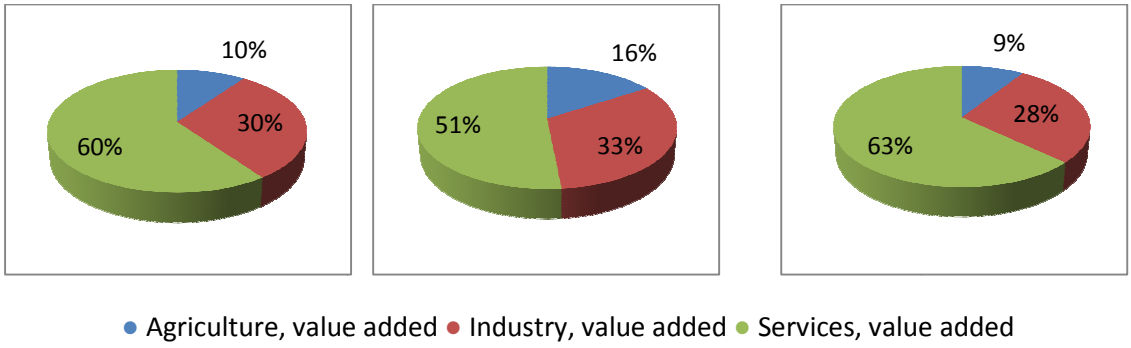
In 2002, a new SBA was negotiated by the government and the IMF. Its two main pillars were : inflation targeting and floating exchange rate regime. Moreover, the independence of the Central Bank of Turkey was sought, by prohibiting short-term advances to the Treasury, and incorporating it into the Law that included a ban on the purchase and sale of Treasury bonds and bills in the primary market. A Monetary Policy Committee was established in order to set interest rates, while the new memorandum of understanding had the purpose to guarantee transparency and credibility of the Central Bank (Görmez and Yiğit 2009).

Another important point was full commitment to fiscal discipline, with the adoption of a target for the public sector primary surplus of 6.5 percent of GNP for 2003 and beyond. In such a way, fiscal and monetary consolidation "succeeded in restoring short-term confidence on the markets and taming inflation, without preventing a strong recovery in output" (Macovei 2009). Moreover, public sector borrowing requirement fell from 10 to the negative zone in a few years, and inflation fell to single digits, for the first time since the 1970s. Exchange rate volatility also lessened and appreciated for some years (Görmez and Yiğit 2009). A positive element supporting recovery during those years was also the prospect of EU membership, which functioned as catalyst for economic and political reforms (Öniş 2006).

A new privatization scheme was implemented under the Expanded Privatization Laws of 2003. The Parliament revised Law n. 4046 of 1994, by extending the scope of assets to be privatized; by providing adequate framework, funds and mechanisms to speed up privatization; by establishing a social safety net for workers who lose their jobs as a result of privatization; and by establishing the Privatization High Council and the Privatization Administration to facilitate the decision-making process in the privatization effort. As a result of these new laws, a surge in privatization revenues was registered, reaching USD 30 billion, thanks to privatization between 2003 and 2009 (Uckun and Doerr 2010).

If it is true that strong recovery reflected the natural rebound after deep recession, like it happened in other countries, it is also correct to state that early indications of an improvement in long-term growth prospects had already been observed in the Turkish economy. Real GDP grew again by 6.2 and 5.3 percent in 2002 and 2003 respectively, and the external financing side also improved, as portfolio investment flows, together with IMF loans and other kinds of investment, allowed the gross foreign reserves of the Central Bank to increase (Macovei 2009). Indeed, the above-mentioned regulatory reforms set the stage for broad economic expansion and contributed to attract the attention of the global financial markets (Uckun and Doerr 2010). Moreover, the significant depreciation of the Turkish lira and the improved external competitiveness led the exports of goods and services to rise in volume terms by around 7 percent year-over-year in 2002 and 2003.

Figure 5. GDP by sector, 1991, 2001, 2011
(percent)



Source : EUROSTAT

The period 2002-2007 saw an average GDP growth rate of 6.8 percent annually, with the strongest growth performance taking place in 2004/2005, followed by a certain slowdown in 2007. Growth was driven by increasing private consumption and by a "boom in investment which grew on average by 15 percent in real terms during 2002-2007" (Macovei 2009). A major part of this investment was built on foreign finance capital, which was mainly attracted by significantly high rates of return offered domestically. This surge of investment was yet accompanied by high levels of unemployment (Yeldan 2006).

In order to attract more permanent and job-creating foreign capital to Turkey, the FDI regulation had also been reformed. The new provisions removed the requirement that, in order to create a new company in Turkey with foreign capital, a foreign company should obtain a permit. In addition, they established the principle of equality between foreign and domestic companies, both for duties and privileges (Uckun and Doerr 2010).

As we stated before, one of the main concerns of the reform policies was inflation targeting, to be addressed by the Central Bank, whose sole mandate was to maintain price stability. This could help the government and the new monetary regime to regain credibility and to reduce the country risk perception (Yeldan 2006). However, the restructuring of the economy following the new IMF program, and the transition to the newly floating exchange rate system were contributing to high market volatility. This, together with "excess sensitivity to economic and political news in international and domestic markets", made inflation forecasts by the Central Bank very unstable. This is why an implicit inflation targeting was pursued until 2006. This strategy proved to be effective, by allowing the Central Bank to restore credibility to the new monetary regime, and by favoring a considerable inflation drop.

Table 2. Historic inflation (CPI) – by year

(percent)

annual inflation (dec vs. dec)	inflation	annual inflation (dec vs. dec)	inflation
2012	6.16 %	**2002**	29.75%
2011	10.45%	**2001**	68.53%
2010	6.40%	**2000**	39.03%
2009	6.53%	**1999**	68.79%
2008	10.06%	**1998**	69.73%
2007	8.39%	**1997**	99.09%
2006	9.65%	**1996**	79.76%
2005	7.72%	**1995**	76.05%
2004	9.35%	**1994**	120.31%
2003	12.71%	**1993**	71.08%

Source : www.inflation.eu

On the other hand, these policies led to the appreciation of the exchange rate. Following the restriction on the Central Bank to reduce inflation only by targeting monetary policy, the value of the Turkish lira was bound to market forces' behavior. Just like other emerging economies, Turkey experienced a "policy dilemma" around the fact that, along with enhanced credibility of a given macroeconomic framework, market interest rates remain high compared to international standards. This fosters capital flows, thus making the economy "fragile to a sudden stop of those inflows" (Uckun and Doerr 2010).

Nevertheless, numerous favorable developments, among which a strong primary surplus, fostered an impressive decline in public debt from around 74 percent of GDP in 2001 to less than 40 percent of GDP in 2008. A number of factors were contributing : high real GDP growth rate, the appreciation of the Turkish lira, the privatization process, and real interest rates, but only in 2002. In fact, real interest rates remained considerably high during all the 2000s. The improved management of public debt and the benefits of the structural reforms in the banking and enterprise sectors had a positive impact in optimizing the cost of public debt and on the stock of contingent liabilities and the accumulation of quasi-fiscal deficits respectively (Macovei 2009).

As the banking sector is concerned, it is argued that it registered an increasing performance every year over the period. Credit and deposit rates decreased to unprecedented levels, and the vulnerabilities of the sector induced by the crisis disappeared, thanks to restructuring and re-capitalization. Moreover, asset quality and profitability rose to extremely high levels and international banks started to show real interest to buy a bank or to look for opportunities for mergers and acquisitions. The Financial Stability Report was introduced in order to give an independent assessment of the financial system, and which, together with the Inflation Report, completed the Central Banks communication set (Görmez and Yiğit 2009).

Sustained growth in that period was accompanied by a marked increase in labor productivity, which on the other hand hided a high level of unemployment. Indeed, the performance of labor market indicators was disregarded against the strong growth cycle that the Turkish economy was experiencing, which has been defined as "jobless growth" (Voyvoda and Yeldan 2006). The unemployment rate increased from 6.5 percent in 2000, to 10.3 percent in 2002, the problem being more severe among the young urban labor force. The persistence of unemployment can be attributed to two main factors, namely fast-growing population, to which labor demand could not keep the pace, and labor market rigidities. Indeed, many obstacles to employment, such as : "a high tax wedge on labor, large severance payments, high minimum wages, worker skill mismatches, and a need for further improvement in educational and vocational training achievements" persist both in the formal and informal economy (Macovei 2009). Moreover, constant resource reallocation, increasing competition from low-cost countries, and real currency appreciation are said to contribute to increase the unemployment rate.

An important development of the post-crisis period is the surge in foreign direct investment to Turkey, along with increasing domestic investment as well. Foreign investors have long been suspicious because of the high political instability characterizing Turkey during several decades. This is why the electoral victory of the Justice and Development Party (AKP) led by Recep Tayyip Erdoğan, which created a single-party government in November 2002, favored a significant improvement in the FDI environment, both by bringing political stability, and by providing a clearly pro-

FDI official stance that lacked in the past. (Erdilek 2005, YASED Conference) Through an ambitious privatization program, the new government fostered FDI, which, during 2002-2008, reached the cumulative amount of US$ 76 billion, nearly eight times higher than between 1995 and 2001, when the total amount was US$ 10 billion.

1.4 – The rise of AKP and recent economic developments

The 2001 economic crisis marks a breaking point for Turkey also in terms of democracy. Indeed, in contrast with past experiences, Turkish democracy proved to be resilient to massive economic shocks. The major defeat that the coalition government experienced in the early elections of November 2002 was totally and only electoral, without any intervention of the armed forces, which proved so costly in the past (Öniş 2006).

The three parties composing the 1999 coalition government, namely the Democratic Left Party, leading member of the coalition led by Bülent Ecevit, the Nationalist Action Party, and the Motherland Party, experienced a dramatic collapse in their electoral support and paved the way to the subsequent exceptional success of the AKP. The Turkish Parliament emerged from the elections in a brand new shape. Indeed, only two political parties shared the benches of Parliament : the AKP, with 35 percent of the vote and 2/3 of the seats, and the Republican People's Party (in Turkish : Cumhuriyet Halk Partisi, CHP), with almost 20 percent of the vote and a third of the seats.

The Justice and Development Party was the real newborn star of the Turkish political environment : it gained three subsequent elections with large majority in 2002, 2007, and 2012. It has its roots in political Islam, even though its leaders had dissociated themselves from the more radical principles of their "ideological forefather" Necmettin Erbakan, and presented themselves as adherents of a "conservative democracy" (Öktem 2011). The party committed to continue the policies of the preceding government in two crucial areas : the IMF program of economic recovery agreed by former Minister of the Economy Kemal Derviş, and the pro-EU reforms, which had been introduced by former Minister of Foreign Affairs Ismail Cem as part of Turkey's long term European policy.

The AKP succeeded in creating a broad electoral support based on an inter-class alliance, which encompassed the more dynamic and prosperous segments of society, as well as the more disadvantaged and underprivileged ones, both in rural regions and on the margins of the main metropolitan areas. A key factor fostering the rise of the predecessor of the AKP, the Welfare Party, during the 1990s, was the active support of small and medium-sized business units, especially in the rising Anatolian cities, under the umbrella of the MÜSIAD, the Independent Industrialists and Businessmen's Association (Öniş 2004b). These religiously conservative but market-oriented middle classes had transformed from merchants and pre-industrial small producers into an increasingly globally oriented business and industrialist elite.

Kerem Öktem (2011) describes the economic base of the Justice and Development Party as follows : high level businessmen owning highly sophisticated industrial holdings and exporters of furniture or textiles, whose origins can generally be traced back to two generations, when the pious grandfather founded the business, usually a manufacturing workshop. His sons would have expanded the business during Özal years, probably taking advantage of the new opportunities in the Middle Eastern and Central Asian markets. Finally, his grandsons and sometimes also his granddaughters would have studied at the Fethullah Gülen schools and at university, speak foreign languages, travel the world searching for new business opportunities, and vote for the AKP. Their personality smoothly combines religious piety and self-discipline with profit maximization and rent generation. Their definition in circles sympathetic to the AKP would be "Islamic Calvinists", while they would be called "green capital" by the guardian state, which feared their wealth and political power.

Similarly to other emerging economies, the economic boom of the last decade and the surge in investment that came along is heavily based on "the powerful nexus between ambitious governments eager to promote high-profile investments and politically connected business groups ready to take on such projects". In Turkey, there exists a very tight relationship between the government and these conglomerates that achieved extraordinary success since Erdoğan came to power in 2003 (Landon 2013).

FDI to Turkey : a new growing trend

The 2000s are the years in which, after many decades of non-attractiveness, Turkey became an important host country for foreign direct investment, as we mentioned before. Compared to other emerging markets, however, it still lags behind in terms of inward FDI stock as percentage of gross domestic product. The same can be said about FDI outflows, which are still considered to be lagging by global standards (Erdilek 2009).

This performance can be explained by referring to Turkey's unstable and turbulent past. Indeed, through the early 1980s, the country showed ambivalence, and at times outright hostility toward IFDI, to be followed by the deep economic and political instability throughout the 1990s and the beginning of the 2000s, which we treated extensively in the paragraphs above. Unsurprisingly, this condition made Turkey chronically unattractive for foreign investors.

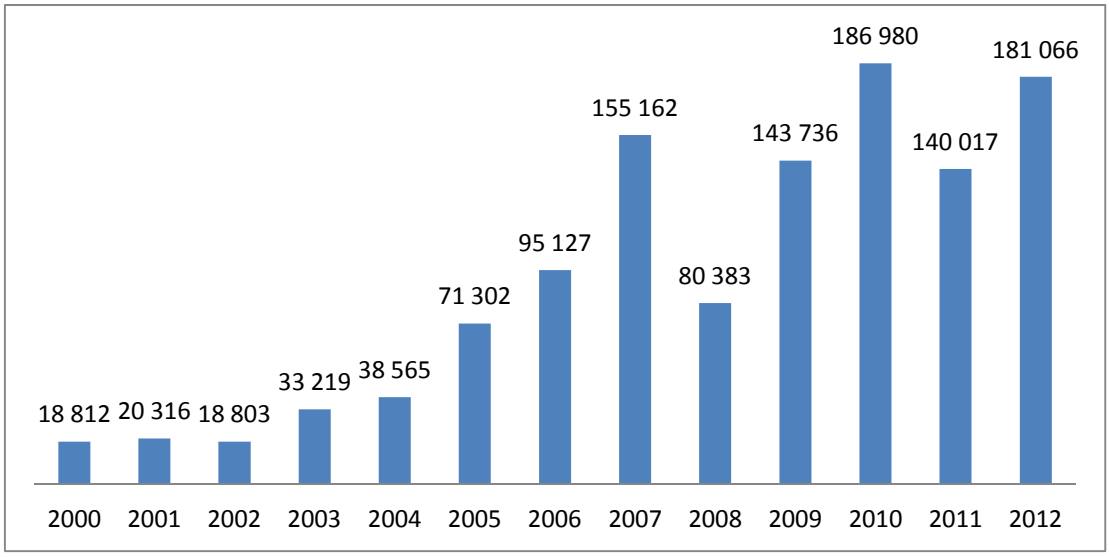
As part of the conditionality for IMF financial assistance during the years of the 2000-2001 crisis, Turkey was constantly encouraged to improve its FDI environment, both by the IMF and the World Bank. Two studies compiled in 2001 by the Foreign Investment Advisory Service (FIAS) from the World Bank highlighted the need of establishing an Investment Promotion Agency (IPA), developing a long-term FDI promotion strategy, building the political will required for an action plan with broad support, and of monitoring improvements as the plan was implemented. It is fair enough to say that these two studies have provided the basis for the recent changes in Turkey's FDI environment and policies (Erdilek 2005, YASED Conference).

As we stated before, the electoral victory of the AKP brought the needed stability to encourage foreign investors. The government proved to be deeply engaged to improve the FDI environment : it reorganized the Coordination Board for the Improvement of the Investment Environment (CBIIE), which had been established by its predecessors, and, most importantly, it enacted Law 4875 to replace Law 6224 in June 2003. The accelerated privatization effort and simplified procedures for setting up businesses also fostered FDI.

Indeed, along with the global surge in foreign direct investment, FDI to Turkey attained unprecedented levels in 2005, when it attracted almost as much FDI as in the previous twelve years combined (Demirbağ, Glaister, and Tatoğlu 2007). From an average of US$ 1.4 billion measured between 1994 and 2004, FDI inflows reached the amount of US$ 10.0 billion in 2005. Later, in 2007 they attained their peak, not yet replicated, of 22.0 billion US dollars (including real estate acquisitions of foreigners).

Figure 6. FDI stock to Turkey 2000-2012

US$ million

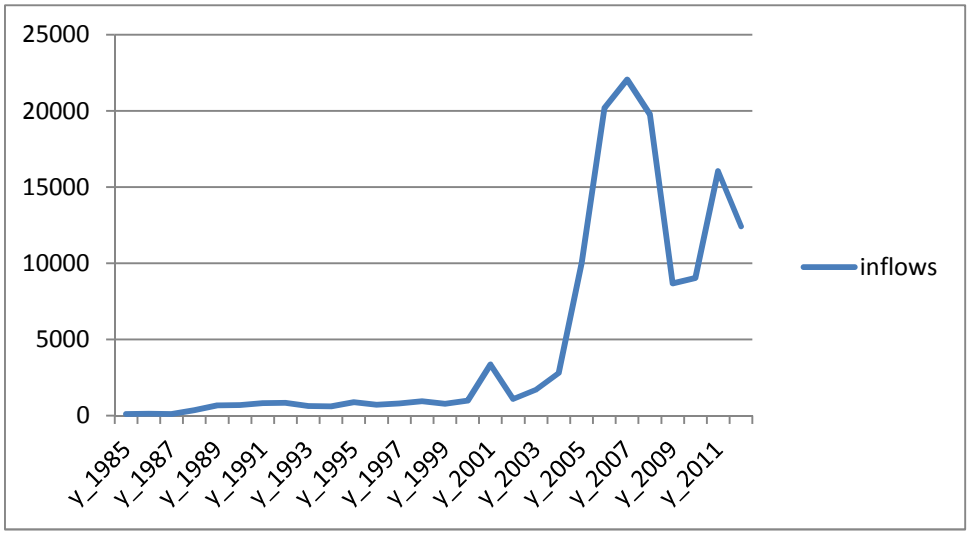


Source : UNCTAD

As a consequence of the global financial and economic crisis of 2008, Turkey's IFDI flows and stocks dropped to very low levels.

The big bump was felt in 2009, when only US$ 8.7 billion FDI flew to Turkey, followed by the other disastrous performance of 9.0 billion in 2010. The recovery started in 2011, with an encouraging 16.0 billion to be followed by a decline of 23 percent in 2012, down to US 12.4 billion. (data from CBRT)

Figure 7. FDI inflows to Turkey 1985-2012
(US$ million)



Source : UNCTAD

The main source of investment to Turkey is Europe, with 202 projects from 2007 to 2012, primarily directed to high technology sectors, such as diversified industrial products (DIP) and automotive. Germany is the most investing European country, with 64 projects, followed by France with 30, the UK with 26, and Italy with 24. Despite Western Europe still remains the most significant regional source of FDI to Turkey, it has recently taken a declining trend and will probably be surpassed in the future. With 86 projects, the United States contributed by 28 percent of total FDI in the same time interval. The main sectors involved are business services, ICT, chemicals, transport and logistics, and DIP. Concerning Asia, Japan is the largest investor, and the sixth at the global level (data from E&Y European Investment Monitor – EIM).

Discordant and even opposed opinions are expressed when analyzing the recent recovery in IFDI to Turkey. On the one hand, despite Turkey's recent success in attracting FDI, its levels are still not satisfying compared to other emerging economies. This is the focus of numerous analysis, that interpret it as a consequence of persisting suspicion against foreign businesses in Turkey, and of the country's fragile economic and political stability. Under this view, the Turkish FDI-based globalization is said to be "promising but precarious" (Erdilek 2010).

On the other hand, more global-oriented sources give a more optimistic interpretation. Turkey is said to have undertaken a growth trajectory reinforcing its "investment appeal", which is expected to continue to rise in the future (Ernst and Young press release, May 2013). A survey conducted by Ernst&Young on over 200 global business leaders reveals that the main reasons sustaining investors' confidence are the country's strategic location, its stable and solid economic growth, and the size of its domestic market.

71 percent of the respondents to the survey think that Turkey's investment attractiveness improved substantially over the past three years and more than half of them expressed their intention to set up operations in Turkey within next year. Although location and size of market are unquestionable factors, the nature and quality of Turkey's growth are under debate. We will discuss this point below in the chapter.

As we stated before, the economic austerity program of the IMF and Kemal Derviş resulted in a reduction of inflation from 80 percent to 10 percent. On this basis, the government decided to bring a highly symbolic change in Turkey's everyday life : it slashed six zeros from the Turkish lira. Savers started to save accounts in the local currency, thus helping to increase confidence in the New Turkish Lira (in Turkish : Yeni Türk Lirası, YTL) (Öktem 2011).

After some years of strong and uninterrupted expansion, Turkey found itself again in crisis conditions in 2008-2009, yet this time not due to internal factors. The US subprime mortgage crisis had severe consequences on the Turkish economy, despite "the admirable resilience of domestic banks and the dramatic cuts in interest rates that the Central Bank undertook" (Rodrik 2012). Differently from previous downturns, this crisis was provoked by an unprecedented foreign demand shock, leading to a massive collapse in exports and consequently in GDP. However, as macroeconomic management is concerned, at the eve of the crisis Turkey was navigating in calm waters, and still is : an inflation-targeting approach determines its monetary policy, which is governed by an independent Central Bank; fiscal policy has been generally restrained; the public debt as a ratio to GDP is stable or declining; banks' balance sheets are strong; and final, the currency is floating (Rawdanowicz 2010). At the same time, other

important indicators, like current account, inflation rate, and the main real economy indicators register a negative performance and show important vulnerabilities.

Unprecedented in terms of speed and magnitude, the 2008 global downturn spread via financial markets and trade all around the world. In Turkey, like in many other emerging markets, it firstly involved net capital outflows, currency depreciation, a fall in stock prices, rising risk premia, and tightening liquidity in the banking sector. Exports dropped, provoking a substantial contraction in industrial output and investment. The sharp loss in business and consumer confidence was prompted by the deterioration of the international environment and large uncertainties, combined with competitiveness losses before the peak of the crisis. This also contributed to amplify the exceptional foreign demand shock. In this framework, "households cut consumption abruptly, while companies reduced their investment and greatly depleted inventories" (Rawdanowicz 2010).

To Turkey, the recent crisis has numerous elements in common with the previous ones, but also a few peculiarities. A first common aspect is the turnaround of capital flows as the main triggering factor. Indeed, at the eve of each crisis, in particular those of 2001 and 2008, Turkey was a large recipient of financial inflows, which rapidly evaporated and had been rapidly replaced by considerable net outflows. However, this decline in capital flows was prompted by domestic imbalances and macroeconomic instability in the past, while the huge negative foreign demand shock was the main trigger in 2008.

Moreover, these two crises diverge in terms of recovery of financial inflows. In fact, while it took nearly two years for capital flows to turn positive after 2001, in the recent crisis, the resurgence of capital inflows occurred much more quickly. Indeed, Turkey is now living a very positive juncture for financial inflows, which continue to increase up to levels that exceed previous peaks. The main reason behind this performance is that "the stabilization of global financial market conditions and the policy-driven sharp reduction in interest rates in the advanced economies produced a resurgence in capital flows to emerging markets" (Rodrik 2012).

At the same time, Turkey's growing dependence on foreign capital is a large source of vulnerability, especially because it is heavily basing its economic growth on these flows of capital. As a consequence, Turkey's current account deficit averaged 10 percent of GDP in 2011, which, measured in dollars, was second only to America's (The Economist 2012). Indeed, another element in common to all three crises was the large current account deficit in which Turkey found itself at the beginning of the downturns. Therefore, as a measure against the drying up of foreign financing, the current account deficit needs to be quickly reduced and eliminated. This was actually the case in all three instances, with major adjustments to the current account over a period of five to six quarters. However, this kind of adjustment tends to be temporary. Indeed, three years after the 1994 and 2001 crises, the country was again running large current account deficit. In order to adjust the external balance, a depreciation of the real exchange rate was pursued in all three crises, yet with short-lived effects in the recent one. In fact, the rapid resumption of capital inflows allowed the Turkish lira to appreciate quickly (Rodrik 2012).

Related to this, another weakness of Turkey's economy is that the foreign capital now financing its current account deficit is "of the flighty sort", meaning that it is mainly composed by flows into banks and purchases of stocks or bonds, which can be withdrawn quickly in any sign of trouble. Since a portion of Turkey's bank system is part-owned by banks from the euro-zone periphery and half its exports go to Europe, Turkish economy depends highly on the performance of European banks. Therefore, growing concerns about the banking activity in the euro-zone are directly affecting Turkey (The Economist 2012).

Once again, the vulnerabilities of a financially open economy come into light in the more dramatic way. External financial markets can determine the destiny of all countries around the world, and crises and contagion become endemic. Policy makers and economists need to take into great consideration this interconnectedness, and should avoid complete financial openness. More precisely, they should prefer a "counter-cyclical approach to the capital account", by encouraging inflows when finance is scarce, while discouraging them when finance is plentiful (Rodrik 2012).

The Turkish Central Bank's monetary and fiscal policy response to the deterioration of economic growth in 2008 was prompt and effective. The counter-cyclical policies had been made possible by the improved macroeconomic framework prior to the crisis, and its rapidity of implementation was important for reassuring the markets in the early phase of the crisis. Indeed, since October 2008, the CBRT cut the main policy interest rate by 1,025 basis to 6.5 percent in November 2009. In the same period, the Turkish lira required reserve ratio was cut from 6 percent to 5 percent, in order to further support liquidity and lending (Rawdanowicz 2010).

Since global imbalances were still causing macro-financial risks in the domestic economy, the Central Bank of Turkey designed and launched a new policy strategy by the end of 2010. In line with other emerging market central bankers, its governor, Erdem Başçı, introduced an unorthodox monetary policy tool, which raised numerous critics, but was also recognized to have helped to keep the economy "on a steady growth path with relatively little evidence of direct fallout" (Oxford Business Group 2013). Indeed, "instead of setting monetary policy by reference to a benchmark interest rate, the CBRT employs a wide interest-rate corridor" (The Economist 2012). This system has two different policy interest rates, and functions in the way that, when capitals are flowing, like they did until the summer of 2011, the Central Bank cuts the rate it pays on deposits at the bottom of the corridor, in order to discourage hot money and to avoid the appreciation of the lira. Vice versa, when capital flows reduce, the CBRT offers the lending rate at the top of the corridor, thus helping to support the lira. Banks wishing to borrow from the Central Bank are not told in advance which of the two rates they will be offered.

The high interest rates attracting hot money to Turkey and the large current account deficit creating the need for foreign capital have a common origin : the shortage of domestic savings. Indeed, a declining rate of private-sector saving concurs in making the external deficit to grow. Along with the newly gained economic stability, greater access to credit becomes a discouraging factor for people to save money (The Economist 2012). Long-term measures need to be taken in order to tackle with success all these issues. However, politicians and economists are often inclined to adopt short-term provisions which can bring immediate political consensus.

Differently from previous crises, the most recent one proved the resilience of the Turkish financial markets. In fact, after the 2001 downturn, the banking sector had been reformed and consolidated, as part of the stabilization program, through a number of provisions, such as the strengthening of capital structures, changes in the banking law, and the improvement of risk management and supervision. This modernization was fostered by the harmonization of financial regulations with the EU directives and best-practice international standards. Moreover, strong profitability allowed banks to enjoy large capital reserves and sound liquidity. At the same time, however, the ratio of non-performing loans increased, reaching a 5.4 percent level in October 2009, which was more than the double than a year before. Large part of these non-performing loans are for consumer loans, especially on credit cards, and for corporate loans for small and medium-sized enterprises (Rawdanowicz 2010).

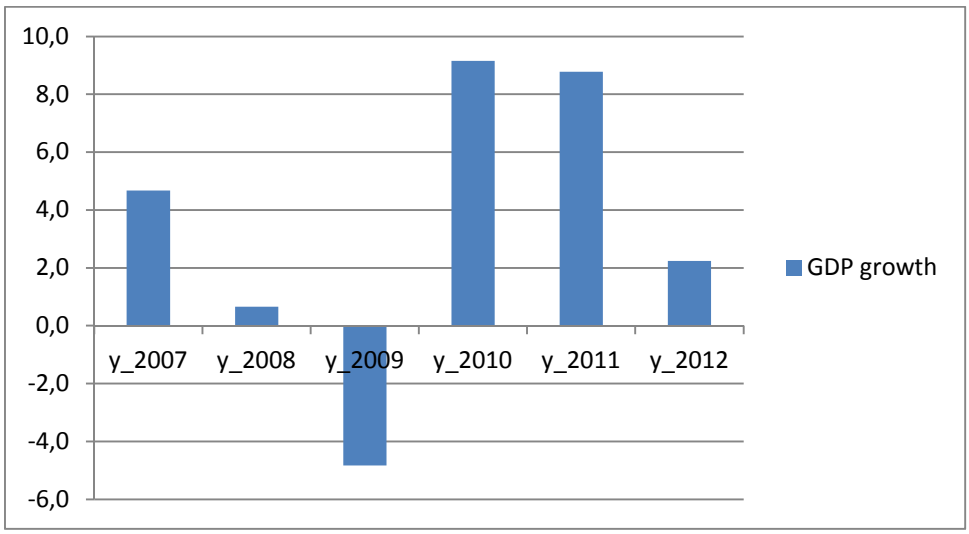
Concerning the crisis's effects on real economy, it is out of doubt that the 2008 crisis had a stronger and more rapid impact than the earlier ones. The turnaround of financial flows had a deep impact on industrial production and real GDP, as we stated before. The decline in real GDP over the first quarter of 2009 was the worst ever registered since 1945. However, recovery in economic activity also proved to be very quick, and by the end of 2009, positive signals were already to be registered (Rodrik 2012). Indeed, Turkey's well regulated financial markets and banking system helped the country overcome the crisis, and GDP rebounded strongly from -4.8 percent in 2009 up to 9.2 percent in 2010.

Nevertheless, after two years, the economy grew only by 2.2 percent in 2012, which is "a respectable figure in light of the sagging European economy" (Sidar 2012), but highlights the vulnerable nature of Turkish growth. Low domestic demand is said to be responsible for this reduction, as domestic consumption pulled the overall figure down by 0.6 percent. On the other hand, net exports and state consumption, and investment expenditures raised the rate respectively by 1.9 and 2.9 percent (Hürriyet Daily News 2013).

In this context, interpretation of data divides the opinions, as different parties report different figures in order to support their own theory. Government sources report that

GDP expanded by more than three-fold between in the last decade. (Invest in Turkey website) However, this figure is based on the dollar valuation of Turkish GDP based on current prices, thus misleading the real value of GDP growth, which, calculated at constant prices, reduces to 64 percent during 2002-2012, and real GDP per capita to 43 percent. These numbers are relatively good for Turkey, if considered in itself, or compared to European recent standards. However, when we compare it to other emerging and developing economies, which are experiencing an economic boom in recent years, we see how Turkish performance stays well under the average (Rodrik 2013).

Figure 8. Real GDP growth 2007-2012
(percent)



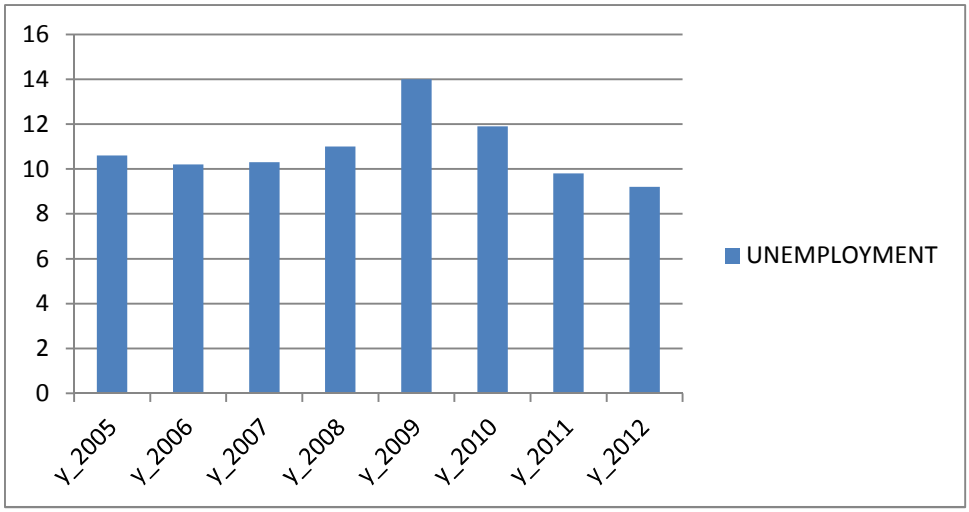
Source : TURKSTAT

The recovery in GDP growth is a consequence of the recovery in exports (Yalçin 2012). The export volume accounted for US$ 132,027,196 million in 2008, falling to 102,142,613 million in 2009, with a decrease percentage of -22.6 percent. In 2010 it was already recovering with a growth rate of 11.5 percent. It reached US$ 152,461,737 million in 2012, growing by 13.0 percent. First calculations in 2013 reveal a little decline compared to 2012. The main partner country for exports has been Germany since a long time, while Iraq became the second in the last years. In 2012, we find Iran at the third place, the United Kingdom at the fourth, and the United Arab Emirates at the fifth.

Imports suffered a severe contraction of -30.2 percent in 2009, but they also recovered quickly, growing by 31.7 percent in 2010 and by 29.8 percent in 2011. However, in 2012 they decreased by 1.8 percent, thus reducing the trade deficit a little. During the last ten years, Turkey has been importing products from almost the same countries, which are, in the order : Russia (11.3 percent in 2012), Germany (9.0 percent), China (9.0 percent), USA (6.0 percent), and Italy (5.6 percent) (data from TURKSTAT).

Despite positive performance in multiple areas of the economy, the unemployment front is still not encouraging. Unemployment rate reached a peak of nearly 16 percent in the first quarter of 2009, and has declined since then, yet maintaining quite high levels, as shown in figure n. 9. The decrease in aggregate demand is at the base of this condition, the construction sector being the most affected sector form this point of view (Yalçin 2012). However, it has to be mentioned that, compared to preceding crises, joblessness was enduring at much higher levels at the onset of the 2008-09 crisis. Indeed, despite sustained economic growth since 2001, unemployment maintained quite high levels, always around and above 10 percent (Rodrik 2012).

Figure 9. Unemployment rate 2005-2012
(percentage)



Source : TURKSTAT

To conclude, Turkey's economic performance of the last ten years has been at the core of widespread debate, and it has been analyzed from different point of views, some declaring open praising, while others sharp criticism. Even though all analysts agree on the fact that between 2002 and 2012 Turkey considerably improved its economic situation and experienced sustained growth, the quantity and quality on this growth are still matter of debate.

On the one hand, some argue that "there is nothing flashy about Turkish rise, which have been based on fundamentals, rather than bubbles or resource discoveries" (Sachs 2013). Turkey's economic growth is defined "stable and solid", and expectations about the future are optimistic in terms of growth and investment attractiveness (Ernst and Young press release, May 2013). Indeed, thanks to a recovery in private investment and a gradual improvement in global demand, the World Bank forecasts Turkish growth to accelerate to 4.5 percent in 2014 and to 4.7 percent in 2015. The government's New Development Plan is said likely to boost productivity and competitiveness, and therefore, to ease the current account deficit to around 6 percent (WB Turkey Regular Economic Brief 2013).

On the other hand, worries about economic endurance are deep, and the recent uncertainty about financial flows is raising concerns. Western investors, who started to pour large sums into emerging markets because of low returns both in the United States and the European countries in the last years, are now reverting course. As a result, the main emerging economies' currencies such as, among the others : the Indian rupee, the Brazilian real, Indonesian rupiah, the South African rand, and the Turkish lira are dropping (Krugman 2013). Behind this situation stays the expected change of route of the Federal Reserve, which, after cutting interest rates sharply in 2009 and printing a huge amount of dollars, "may soon begin to tighten its monetary spigot". As a consequence, the vast investments that Turkish groups made thanks to cheap loans in dollars, "could well be a harbinger of an emerging market bust brought on by unpaid loans, weakening currencies, and, eventually, the possible failure of developers and banks" (Landon 2013).

CHAPTER 2

TURKEY AS A NEW INVESTING ECONOMY

2.1 - Introduction to the chapter

As it has been said in the previous chapter, Turkish economic history has been rather turbulent. It experienced different phases, often marked by severe crises, having important consequences on Turkey's economy and society. The most severe ones, those of 1994 and 2000/2001, left their heavy effects for many years to follow (Öniş 2004b). Internationally speaking, these economic crises had some interesting consequences : they became a push factor for Turkish enterprises to start investing abroad, as the domestic economic environment could not offer good profit opportunities (Erdilek 2003).

The Turkish outlook over the international environment will be presented in this chapter, focusing on its outward foreign direct investment (OFDI), an expanding and increasingly significant phenomenon. Led by big multinational corporations but also by small and medium-sized enterprises, OFDI helps Turkey to actively participate in the economic globalization and to impose its presence in its regional environment and the world. The motivations encouraging Turkish firms to invest abroad will be investigated here, as well as the choices of investment destinations and the reasons behind them.

After Europe, which is still the most important destination of Turkish outward FDI, Turkey's neighboring countries are also privileged hosts of investment (Aybar *et al.* 2009) : the Middle East, the Turkic Republics of Central Asia and the Caucasus, and Central and South-East Europe are becoming increasingly important for Turkish economic expansion abroad. These countries often present a high level of risk and uncertainty to foreign investors, due to economic and political instability, reason why they are not popular destinations among developed markets' investors. On the other hand, Turkish enterprises are not discouraged by these negative environments, as they present large similarities to Turkey's internal conditions. Indeed, they found the way to exploit the difficulties and create profit out of them (Anıl *et al.* 2011).

Economically speaking, Turkey is considered to be among the so-called emerging markets or economies, term that was coined in 1981 by economists at the International Finance Corporation (IFC) to give a different perspective on developing countries (IFC website). A common definition for emerging economies is "low-income, rapid-growth countries using economic liberalization as their primary engine of growth" (Deng 2012). The main economic features of such countries are recognized to be their high degree of volatility and their transitional character, at the economic, political, social and demographic level (Mody 2004). Nevertheless, the term is sometimes used as a synonym for developing countries, without recognizing any difference between the two groups. (Aykut and Goldstein 2006, UNCTAD) Authors like Sauvant (2005) include in this definition "developing economies and economies in transition". Emerging markets' patterns and characteristics of outward FDI will be presented in this chapter, preceded by a brief general overview on foreign direct investment.

2.2 – Brief analysis of foreign direct investment (FDI)

Since the end of the Cold War, the world reached unexpected levels of interconnectedness, as globalization involved many parts of the world that were completely or partly isolated before. The progressive liberalization of economies started to link all countries of the world through trade and investment and favored the rise of multinational enterprises, moving huge quantities of money and goods at the international level (Sethi 2009). Markets continue to move toward international competition, and nations are convinced that the only way to prosperity goes through the access to overseas resources and opportunities. Governments and firms often work together for the common goal of opening the economy, liberalizing international trade, attracting inward investments and support outward FDI. Indeed, The two main paths companies can follow to enter a foreign market are either exporting or FDI (Shenkar 2007).

In the last decades, foreign direct investment has grown at a faster rate than most other international transactions, particularly when compared to international trade (Blonigen 2005). The global economic and financial crisis, however, has given a significant slowdown to this growth, while it did not impact trade flows as much (data from

UNCTAD). This high growth can be explained by the common belief that, among other forms of capital inflows, FDI is more conducive to long-run growth and development. This hypothesis is most often based on the idea that "FDI brings with it foreign technology and management skills, which can then be adapted by the host country in other contexts" (Walsh and Yu 2010). Moreover, FDI is recognized to bring other advantages to the host economy, such as : "productivity gains, the introduction of new processes to the domestic market, employee training, international production networks, and access to markets" (Alfaro *et al*. 2000). The technology transfer is particularly important for emerging economies. It operates through different channels : vertical linkages with suppliers or purchasers in the host country; horizontal linkages with competing or complementary companies in the same industry; migration of skilled labor; and the internationalization of research and development (R&D) (Rajan 2004).

This process is undoubtedly full of risks and traps, as it is demonstrated by numerous failures. It also has several social and environmental spillovers, which are too often forgotten and left aside. For instance, the relationship between FDI inflows and income inequalities is highlighted by a few studies, whereas it is denied by many others (Choi 2006). Despite various kinds of criticism, today economic globalization and capital flows among countries are the basis of countries' and people's lives and are supported by the majority of international actors.

A brief analysis of foreign direct investment will be now presented, followed by a focus on emerging markets' outward FDI. The OECD defines FDI as "a category of investment that reflects the objective of establishing a lasting interest by a resident enterprise in one economy (direct investor) in an enterprise (direct investment enterprise) that is resident in an economy other than that of the direct investor" (OECD glossary). The "lasting interest" implies the existence of a long-term relationship between the direct investor and the foreign affiliate and a significant degree of influence on the management of the latter. For statistical purposes, FDI are classified as such when the ordinary shares of an enterprise are equal or exceed the minimum threshold of 10 per cent (Sauvant and Sachs 2009).

FDI is typically measured in flows and stocks : “Inward stocks refer to all direct investments held by non-residents in the reporting economy; outward stocks are the investments of the reporting economy held abroad. Corresponding flows relate to investment during a period of time” (OECD Factbook 2013). Differently from foreign portfolio investment, that is the investment in financial assets like stocks, bonds and other forms of debt, FDI is the investment in “real or physical assets, such as factories and distribution facilities” (Shenkar 2007).s

FDI can be of two major types : horizontal and vertical. Horizontal FDI occurs when a multinational corporation (MNC) produces the same products or services produced at home in multiple countries. Aimed at expanding into new markets, this type of FDI is most prevalent in countries that are similar in both size and relative endowments. On the other hand, vertical FDI occurs when “the multinational fragments the production process internationally, locating each stage of production in the country where it can be done at the least cost” (Aizenman 2004). We talk about backward vertical FDI when the operation fulfils the role of a supplier, while we define forward vertical FDI as the operation fulfills the role of a distributor. Today, horizontal FDI represents the bulk of the total amount of global FDI.

Why would a firm choose to start a production in a foreign country, rather than exploit exportation or licensing arrangements? At the firm level, a first answer could be that firms possess specific intangible assets, such as technologies and managerial skills, which foster the creation of multiple plants. More precisely, market failure related to these assets needs to be taken into account to explain the internationalization choice of a firm. “A standard hypothesis is that it is difficult to fully appropriate rents from such assets through an arrangement with an external party.” In order to maximize profits and to avoid uncertainties, “the optimal decision may be for the firm to internalize the market transaction, which would mean establishing its own production affiliate in the market” (Blonigen 2005).

Internalization can be led by different objectives that multinational companies would want to achieve. These objectives are normally classified in four categories : resource-seeking FDI, market-seeking FDI, efficiency-seeking FDI, and strategic asset-seeking

FDI. The first category refers to investments aimed at acquiring resources that are not available in the home country. They can be either natural resources, or cheap and/or skilled labor, or technological, organizational, and managerial skills. The second category aims at securing market share and sales growth in the selected foreign market. The third one attempts to restructure its existing investments in order to gain an efficient allocation of its geographically dispersed activities. Finally, the fourth one refers to the strategy of obtaining the assets of foreign firms through acquisitions or alliances with local companies. Today, MNCs often have diverse objectives and therefore, they do not engage in FDI referring only to one of the preceding categories (Shenkar 2007).

At the macro-level, literature recognizes numerous factors impacting FDI decisions. According to the study conducted by James P. Walsh and Jiangyan Yu (2010), the most significant are : the size and growth potential of the host market, economic stability, the degree of openness and income level of the host economy, the quality of institutions and level of development. These factors determine firms' decisions about where to invest and what kind of FDI strategy to follow. Moreover, they have different impact on different sectors. Primary sector FDI appears to have "no strong linkages to either macroeconomic stability, level of development, or institutional quality, though like other forms of FDI, clustering effects appear important, with larger stocks attracting greater additional inflows" (Walsh and Yu 2010). Similarly, secondary and tertiary sectors FDI both benefit from agglomeration or clustering effects; but on the other hand, they depend on macroeconomic conditions in a more determinant way. Differences in FDI determinants are also highlighted between developed and developing countries. An example given by Walsh is labor market flexibility : controlling for per capita income, the effect of increased labor market flexibility on the ability of an emerging market to attract secondary sector FDI is about three times greater than the effect on an advanced economy.

National policies play an important role in attracting or discouraging FDI inflows. As it has been said before, the current general policy trend is directed towards increased openness, thus favoring FDI. Governments willing to attract FDI need to enact investment-promotion policies, aimed at facilitating foreign firms' entry in the market.

These are primary based on the diffusion of information, the filling of perception gaps and the providing of investment services (Rajan 2004). They can comprise administrative and procedural changes toward simplification, as well as the creation of specific agencies acting as intermediaries between the company and the state, called Investment Promotion Agencies (IPAs). Other fundamental measures to attract FDI are fiscal incentives, aimed at reducing the tax burden of firms, and financial incentives, which are direct contributions to firms from governments (Rajan 2004). UNCTAD registers the ongoing trend to lower corporate income taxes, both in developed and developing economies, and the growth of the number of countries with flat tax systems. A new measure adopted by several countries is also the creation of special economic zones (SEZs) (UNCTAD WIR 2008).

A fundamental legal instrument favoring private foreign investment is bilateral investment treaties (BITs), which, along with double taxation treaties (DTTs), are the most common international investment agreements (IIAs). Countries conclude BITs and DTTs in order to, respectively, assure investors that investments are legally protected under international law and avoid the possibility of double taxation of foreign entities (Sauvant and Sachs 2009).

Despite being exalted by international economic institutions (for instance, the OECD emphasizes their utility in its model tax convention), DTTs are also criticized by a few experts. The main criticism is about the non-reciprocal nature of this type of treaties, in particular when signed between developed and developing countries. In desperate need of foreign capital, the latter conclude DTTs to attract FDI, without considering the related significant cost in terms of lost tax revenues (Baker 2012).

The first BIT ever existed was signed between the Federal Republic of Germany and Pakistan in 1959. The 1960s saw the proliferation of BITs, mostly negotiated by European and developing countries. In the same period, the Organization for Economic Cooperation and Development (OECD) worked on the protection and promotion of investments as well. In 1967 it presented the Draft Convention on the Protection of Foreign Property, which, however, failed to achieve any formal status. Nevertheless, it

contributed to the development and draft of subsequent treaties between OECD member states in a significant way (Dolzer and Stevens 1995).

Since the 1990s, an incredibly high number of bilateral investment treaties and other forms of international investment agreements has been signed between nations all around the world. The total number of IIAs by the end of 2011 was 3,164, including 2,833 BITs and 331 “other IIAs” (UNCTAD WIR 2012). Initially, BITs were mainly signed between developed and developing countries, whereas more recently, developing countries started to conclude agreements with other developing countries. Germany, China and Switzerland are the countries which concluded the highest number of BITs by 2011.

Since 2001, however, we are witnessing a progressive decrease in the closure of traditional investment agreements. UNCTAD explains this phenomenon with two principal causes : a gradual shift towards regional treaty making and the increasing number of IIA-based controversies between investors and states. Regional treaties are more convenient because they can replace a multitude of bilateral pacts. Very often they are at the same time Free Trade Agreements (FTAs), thus better responding to “the needs of today’s economic realities, where international trade and investment are increasingly interconnected” (UNCTAD WIR 2012).

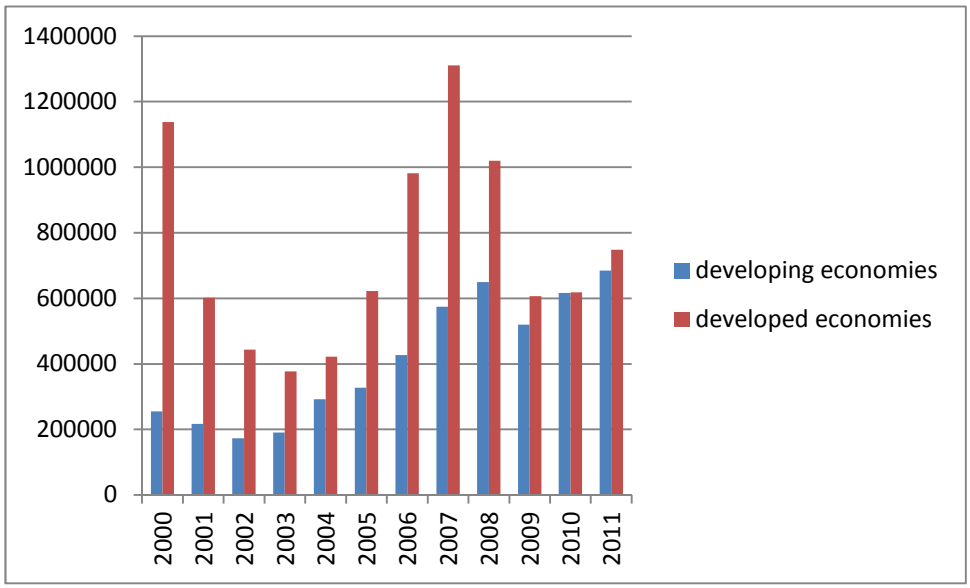
Despite the general tendency to sustain FDI, we also witness growing concerns and political debate over rising protectionism, often adopted by nations trying to safeguard local or state-owned firms. The principal sector involved in restrictive measures is the extractive industry, and the main and most well-known case is that of South America. In this continent, numerous countries are natural-resource-exporting and in recent years, a few governments like Bolivia, Ecuador or Venezuela, introduced new sectoral or ownership restrictions (UNCTAD WIR 2008). Since 2011, however, we register a significant decrease in the percentage of restrictive measures all around the world and the adoption of new measures to facilitate FDI in many countries. The highest concentration of regulatory and liberalizing measures are registered in Asia. Numerous other emerging economies are implementing this kind of acts (UNCTAD WIR 2012).

Regarding outward foreign direct investment, concerns are rising that it may cause job exports and the weakening of the industrial base. Worries about the stability of the foreign exchange market and improvements in the balance of payments are also growing among governments. All these concerns have been certainly intensified by the global economic crisis, which in recent years has been causing widespread growth of domestic unemployment. In response, countries adopted two categories of measures : restrictions of outward FDI and incentives to bring investments home (UNCTAD WIR 2012).

Despite these concerns, foreign direct investment has been rapidly increasing all around the globe, reaching the record rate of US $1,975,537 million inflows in 2007. After this, the global financial crisis of 2008 caused a serious decline in inward and outward FDI worldwide. However, flows in and out of developing countries have been much less impacted than those of developed economies. Data released by the United Nations Conference on Trade and Development (UNCTAD) confirm this statement.

Figure 10. Inward foreign direct investment flows, annual, 2000 – 2011

(US$ million)



Source : UNCTAD

After this decline, global FDI inflows started to rise again in 2011, rising by 16 percent compared to 2010; global inward FDI stock rose by 3 percent, reaching $20.4 trillion. Despite this, the global financial crisis is continuing to influence FDI flows around the world. This is why UNCTAD estimates that this rise will slowdown, as it already started to do (UNCTAD WIR 2012).

Figure 11. UNCTAD's global FDI quarterly index, 2007 Q1 – 2012 Q1

Source : UNCTAD WIR 2012

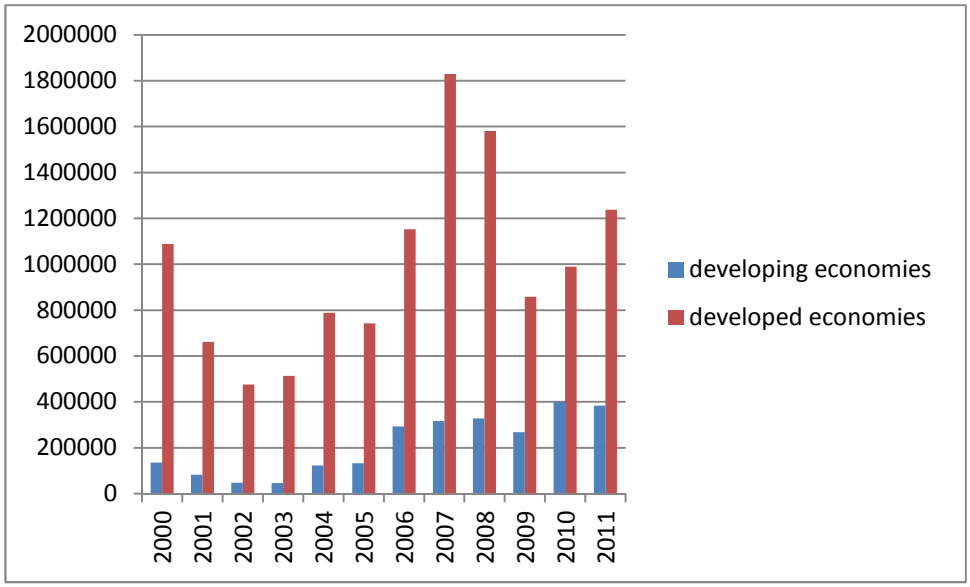
The recent rise was spread throughout developed, developing and transition economies, though with some differences in its intensity and motivations. First, FDI flows to developed countries grew stronger than flows to developing countries in 2011 : compared to 2010, they grew 21 per cent, while flows to developing economies grew 11 per cent. Despite this difference in growth, FDI inflows to developing countries account for nearly a half of global flows in 2011, reaching the record amount of $684 billion (flows to developed economies have been of $748 billion). The driving force is East Asia, followed by Latin America and the Caribbean (excluding financial centers). Transition economies are also witnessing a significant growth, whilst Africa and West Asia are experiencing a strong decline, cushioned only by the rise of FDI to Turkey (UNCTAD WIR 2012). Second, investment inflows to developing and emerging economies were largely driven by Greenfield projects, whereas FDI flows to developed countries were mainly due to cross-border M&As by foreign multinationals. Flows to

Europe, for example, are driven by cross-border M&As fostered by the ongoing and post-crisis corporate restructuring, and gradual exits from states by some nationalized financial and non-financial firms (UNCTAD WIR 2012).

After the strong fall caused by the global crisis in 2008, global FDI outflows have also started to rise again in 2011, precisely at a rate of 17 per cent, compared to 2010. This growth is driven mainly by developed countries, whose TNCs often invest in other advanced economies. On the other hand, developing economies are experiencing a slowdown in their outward FDI growth rates. In 2011, this rate even fell by 4 percent.

Figure 12. Outward foreign direct investment flows, annual, 2000 – 2011

(US$ million)



Source : UNCTAD

Despite general agreement on the beneficial effects of FDI on the host economy, we can also find a few economic schools arguing the opposite. An example is the Dependency or *Dependencia* School, a group of economists who believe that FDI represents a threat for developing countries. They assert that developing countries are suffering severe economic difficulties because of the unjust way the international system works. Large multinationals contribute to further pauperization of those economies by creating monopolies, by causing unemployment through transfer of

technologies, by deteriorating the host country's balance of payments, and by weakening local businesses.

According to this school, MNCs aim at creating dependency relations with developing economies by controlling technology and the consumer preferences. Attracted by the consumption standards of developed countries, the governing elites contribute to the sale of their own countries by making them mere exporters of raw materials or natural resources. Instead of sustaining shared development, the economic penetration of MNCs in developing countries only contributes to worsen inequalities (Serin *et al*. 2010).

Despite this and other forms of criticism or real opposition, the general tendency among governments and people is to count on FDI for greater development and economic growth. However, thanks to the rising performance of large industrial groups from emerging economies, global investment patterns are changing over time.

2.3 – Emerging markets' outward FDI : recent global transformations

"In 2012 – for the first time ever – developing economies absorbed more FDI than developed countries, accounting for 52 percent of global FDI flows. This is partly because the biggest fall in FDI inflows occurred in developed countries, which now account for only 42 percent of global flows. Developing economies also generated almost one third of global FDI outflows, continuing a steady upward trend" (UNCTAD World Investment Report 2013).

In the last decades, emerging markets have experienced fast growth and improving internationalization, which is why literature started to analyze their economic performances and the international trends they follow. Since the beginning of the '80s, the first developing countries' multinational enterprises started to appear in the global economic environment, claiming the definition of Emerging Multinational Corporations (EMNCs) (Aykut and Goldstein 2006). The diffusion of modern capitalism and the acceptance of the Washington consensus in the so-called South of the world fostered processes of economic reform and opening to the world economy. An important change has been the introduction of trade liberalization, which "has increased competition on

hitherto protected markets, reduced margins at home, and pushed surviving firms into export expansion" (Goldstein 2007). This is why foreign investment coming from this kind of countries started to become significant in recent years and it is now continuing to grow. The share of all developing countries in the global stock of outward FDI has risen from 7 per cent in 1990 up to 10 per cent in 2005 and to 17.5 per cent in 2011 (data from UNCTAD).

From the historical point of view, Latin American big companies have been the first developing countries' firms to expand abroad and to become real multinationals by establishing cross-border production. In particular, Argentinean MNCs "started to invest abroad as early as 1890s" (Goldstein 2007), followed by Uruguayan and Brazilian ones in more recent years. Since the early 1970s, Asian countries have taken the leadership among emerging economies and today have become "by far the largest active investors". In 2004, the so-called Asian Tigers (Hong Kong, Singapore, South Korea and Taiwan) plus China accounted for more than 2/3 of the total (Goldstein 2007). Given the very high growth experienced by the four Tigers since the 1960s, today the IMF comprises them among developed countries. Therefore, these countries and their development path have become a model for new emerging economies.

Russia is another significant source of outward FDI, mostly concentrated in natural resources, the transportation and metallurgical sectors. The main destinations of these investments are the Republics of the former Soviet Union in Eastern and Central Asia. More recently, these countries have seen the birth and growth of multinational companies as well. Given their familiarity with post-communist business environment, the bulk of investment takes place within the region (Goldstein 2007).

Today, the bulk of the studies on this field focuses on the so-called BRIC countries (Brazil, Russia, India, and China), a group of emerging economies that experienced an incredibly fast growth in recent years and are said to comprise 20 percent of the world economy in 2012 (Economist 2011). Beside BRICs, a high number of other states are growing very fast, giving birth to important global businesses, but they are not as much "popular" as those ones. South Africa and North African states are among these ones for example, and in the Middle East, Turkey and Saudi Arabia can be considered "emerging

giants" (Wooldridge 2010). Mexico, Malaysia, and Indonesia are other countries attracting a lot of attention.

Table 3. Top 30 emerging economies in terms of outward FDI stock (2011)
(US$ million)

Rank	Country	Amount
1	China	1.411.901
2	Russian Federation	362.101
3	Singapore	339.095
4	Taiwan Province of China	213.061
5	Brazil	202.586
6	South Korea	159.339
7	Mexico	112.088
8	India	111.257
9	Malaysia	106.217
10	South Africa	72.285
11	Chile	68.974
12	United Arab Emirates	57.738
13	Panama	33.828
14	Thailand	33.226
15	Argentina	31.329
16	Colombia	31.119
17	Saudi Arabia	29.970
18	Turkey	24.034
19	Kuwait	22.059
20	Kazakhstan	19.924
21	Venezuela	19.808
22	Qatar	18.572
23	Libya	16.848
24	Indonesia	9.502
25	Bahrain	8.776
26	Ukraine	8.158
27	Philippines	6.590
28	Azerbaijan	6.323
29	Angola	6.150
30	Egypt	6.074

Source : UNCTAD

When one starts to analyze emerging markets' outward FDI, they should always be aware of the limitations and incongruities they will find in the collection of data. A first problem to arise is corporate nationality. Very often in our deeply interconnected international business environment, one can have difficulties in identifying the ultimate source or destination of FDI. It is not rare, for example, that entrepreneurs from emerging countries establish their business in a developed economy, or that they "move their primary listing to an advanced country's financial market in order to benefit from lower currency risk and higher liquidity" (Goldstein 2007). A third case may be that of emerging economies' companies that become subsidiaries of OECD multinationals and fourth, the case of firms owned by financial investors based in advanced economies. In all such circumstances, determining the citizenship of corporations is a hard job, and statistics can be clearly affected.

Another critical point is data incongruities. In fact, large differences in collecting, defining and reporting data are very common among states, in particular among those emerging countries that do not have a long experience in this field (Aykut and Goldstein 2006). One example is that the creation of a subsidiary in the host country, with the sole purpose to acquire a local firm, is counted as a foreign investment only for the establishment part, while the acquisition is not included, because it is considered as intra-state purchase (Bower *et al.* 2009).

"Underreporting" is therefore a common problem in these states. Indeed, the real Turkish OFDI amount is said to be much higher than official data estimates (Erdilek 2005). Another big problem is that report of data is rarely up-to-date, a fact that contributes to underestimating outward FDI. But there are also cases of the opposite phenomenon, a kind of overestimation. In China, for instance, foreign investment is perceived as more favorable and therefore, domestic investment is sometimes labeled as foreign (Aykut and Goldstein 2006).

Round-tripping, that is "the practice of channeling investment through offshore financial centers and then redirecting the capital back in the country of origin, in order to make use of preferential treatment for "foreign" investment" (Bower 2009), is not rare in this kind of economies and can also distort statistics.

The conceptual framework used to explain internationalization strategies and motivations of emerging economies' transnational companies relies on the theories that were developed to explain developed countries' multinational behaviors. Bonaglia *et al.* (2006) argue that a specific theoretical approach to emerging markets' firms has not been elaborated yet, even if it is generally recognized that these companies have significant peculiarities in their investment behavior and start to operate in an international economic environment that is completely different from the one in which long-established MNCs have started their businesses.

The first theories analyzing MNCs have been developed during the 1960s. Stephen Hymer gave an important contribution to the theories of the multinational enterprise in 1960, preparing the ground for further developments. According to him, MNCs must have monopolistic advantages over local competitors, in order to invest directly in a country and assume the liability of foreignness. FDI is a "way of perpetuating the monopolistic role of the MNC in the international market", thus contributing to increase market power, the ultimate goal of multinational enterprises (Goldstein 2007).

In the 1960s, Raymond Vernon explained internationalization of MNCs by referring to the concept of product life-cycle elaborated in marketing. He explains the shift from exporting to FDI through the four stages of a product's life-cycle : introduction, growth, maturity, and decline (Goldstein 2007). First, firms start producing new products to satisfy the high-income local market. Thanks to product innovation, they gain a monopolistic export advantage and start exporting, first to countries that are similar to their home country in terms of consumers' income and needs, later to countries which differ in those terms. When the good's production becomes mature and standardized, competition increases and margins start to fall. For this reason, firms are incentivized to invest abroad in order to reduce costs. They will first invest in other industrial countries, where export sales are large enough to support economies of scale in local production (Shenkar 2007). Finally, once cost competition intensifies and production becomes no longer viable, MNCs will move production to developing countries.

The most cited and "presumed to be the most comprehensive" (Yaprak and Karademir 2011) theory about internationalization of firms is Dunning's eclectic Ownership-

Location-Internalization (OLI) paradigm, which represents a mix of three different FDI theories. It states that "the extent, form and pattern of international production was determined by the configuration of three sets of advantages as perceived by enterprises". First, "they must possess certain advantages specific to the nature and/or nationality of their ownership", the so-called ownership advantage (Dunning 1987). Second, the so-called internalization advantage is explained by Dunning as follows: "it must be in the best interests of enterprises that possess ownership-specific advantages to transfer them across national boundaries *within* their own organization rather to sell them, or their right of use to foreign-based enterprises". "The third strand of the eclectic paradigm is concerned with the "where" of production", in order to take advantage of different factor costs and resource costs, the so-called location advantage (Dunning 1987).

The eclectic nature of this model makes it useful to categorize the international operations of business in both developed and emerging economies, even if it suffers from two major limitations in the case of EMNCs. The first one refers to their lack of significant monopolistic advantages : The Ownership explanation is thus not suitable for EMNCs' FDI decisions, and "the parameters that determine the degree of Internalization in their foreign operations are different" (Goldstein 2007). The second one is about its basically static nature : it intends to comprise all significant factors determining entry-mode decisions, but in reality it disregards important ones, like strategic factors, characteristics of the decision maker, and situational contingencies.

Elaborated in response to these criticisms, the dynamic version of the OLI paradigm, the Investment Development Path model (IDP), is also used in literature to explain emerging firms' international expansion. Briefly, this theory suggests that the inward and outward FDI position of a country is related to its level of economic development. In particular, the relationship between FDI and its underpinning OLI factors "changes according to the country's stage of economic development and sophistication" (Goldstein 2007). Dunning identifies five development stages that countries should normally go through, from hosts to sources of FDI (UNCTAD WIR 2006). The IDP framework has proven to be useful in many cases and it can be also applied to non-

OECD economies, only if one takes into consideration its heterogeneous and idiosyncratic nature.

Another related theory, the Uppsala model, states that "internationalization is incremental, sequential and learning based, occurring in stages, based on cumulative market knowledge and commitment". It is evolutionary both in terms of successive stages of rising international involvement and in terms of entry into markets with increasingly greater psychic distance (Erdilek 2008). The main limitation of this theory is its behavioral and thus determinist nature, which does not take into account possible variations of the defined internationalization path. In fact, firms may not be able to complete all stages, or they may reach the higher ones, by skipping some others (Goldstein 2007).

Some authors like Erdilek (2003, 2005, 2008) use these theories to explain the internationalization path of emerging market firms, like Turkish ones, only recognizing a few discrepancies between EMNC's and developed MNC's behavior. On the contrary, other scholars question this point of view in different ways and call for the need to elaborate more reliable explanations (Bonaglia, Goldstein, Yaprak). Those theories were in fact elaborated for "big, predominantly Western, successful MNEs" (Bonaglia *et al*. 2006), definition that does not fit newly internationalized emerging markets' enterprises.

New emerging markets' multinational firms are in many ways similar to those established in OECD countries. Their motivations to invest abroad and the objectives they aim at, for example, are the same. Nevertheless, EMNCs often present different characteristics from developed countries' companies in their behavior and timing of internationalization. Indeed, they enter an already functioning scene, namely a highly globalised economic world, and therefore they follow different starting patterns than their predecessors. In particular, "they are pushed to internationalize via direct investment much earlier in their lifecycle" (Goldstein 2009). Moreover, they have to face strong competition by well-established incumbents, that is why they look for new growth strategies and development patterns.

It is recognized that the rise or downturn in outward FDI of a country is not always directly related to its level of economic development, and "TNCs from developing and transition countries are increasingly investing at an earlier stage in their country's (and their) development", as data from UNCTAD reveals (UNCTAD WIR 2006). Mostly among emerging markets, we can find numerous examples of countries (such as Brazil, China, India, Mexico, South Africa and Turkey) whose GDP level is not very high, while their firms' engagement in OFDI is significant, thus contradicting the IDP model. As we said before, the impact of globalization, which causes growing competition and opportunities, is decisive in this evolution (UNCTAD WIR 2006).

One essential difference between long-established MNCs and emerging economies multinationals, is that these "latecomer" firms, as Bonaglia *et al*. (2006) define them, do not wait for growth and success before expanding abroad, as multinationals from developed countries had to do before. On the contrary, "they internationalize in order to grow large", utilizing globalization and the networks it builds to create their own advantages. The condition of being "latecomers" opens numerous opportunities to these firms, like the possibility to internationalize very rapidly, by utilizing the above-mentioned networks (Bonaglia *et al.* 2006). Accelerated internationalization is in fact another important characteristic that emerging MNEs try to achieve with aggressive overseas acquisitions. These allow them to obtain intangible assets, especially technology and brands, and the external know-how needed to "quickly catch up with the existing global players" (Deng 2012).

In order to find this successful place in the crowded world of international business, emerging markets' MNCs need to find new strategies. They are doing so, by offering contract services to incumbents, forming joint ventures and alliances, licensing new technologies (Bonaglia *et al.* 2006). As a result of internationalization, these firms can acquire "portfolios of locational assets" (Sauvant 2005) which are source of efficiency and consequently, competitiveness. It is well known that EMNCs often lack of strategic resources, especially the intangible ones, which, on the other hand, are the strong point of developed economies' multinationals. For this reason, they utilize mergers and acquisitions in developed country markets to gain access to resources, both tangible and

intangible ones (Uray *et al.* 2010). Evidence is also given to the fact that MNCs from emerging economies often prefer joint-ventures with minority shares in equity as mode of market entry (Yeung 1999). This and other types of contractual arrangements are chosen to maximize learning and access benefits. Later, other investment modes are developed and sharpened (Yaprak and Karademir 2011).

As to industrial categorization, literature shows that multi-industry conglomerates account for a large proportion of EMNCs. Subsequently, mining and petroleum sectors represent an important cluster, followed by a third sector comprising construction, public utilities and transport services. Finally, the fourth one groups "manufacturing firms producing both capital-intensive industrial commodities and food and beverages." A few EMNCs from Asia also operate in electronics (Goldstein 2007). Another common element of emerging economies is that they often give birth to state-owned oil companies. These are becoming important FDI players and are to be analyzed by taking into account a complexity of economic, political and diplomatic factors. Although the productivity gap between developed and developing markets remains wide, emerging economies' FDI in the services sector is also rising and specializing. Initially limited to trade and finance, it has later moved to public utilities and business services as well.

A general trend that can be highlighted is that emerging economies' firms tend to start investing in their own region, before expanding to the rest of the world (Aykut and Goldstein 2006). This tendency is not unique to EMNCs. Indeed, it is a characteristic of most of the world's multinational companies, that is why a debate on whether it should be more appropriate to speak about "regionalization" rather than globalization is going on among some scholars (Sethi 2009). Long-established and successful regional groups, such as the European Union and the North-American Free Trade Agreement (NAFTA), are important pull factors for other areas of the world. They demonstrate that "regional economic integration provides a strong boost to intraregional cross-border investment linkages" (UNCTAD WIR 2012). Attempts of this kind are common among developing countries, even though they often lack the basic and necessary forms of regional cooperation or efficient institutions to support them.

Despite this, successful realities are spreading among emerging economies, especially in Asia and Latin America. In fact, regional trade agreements (RTAs), regional economic integration organizations (REIOs), and South-South investment agreements (SSIAs) are growing in number, geographical coverage, and policy width. (UNCTAD WIR 2012). Literature on EMNCs argues that their motivation to expand regionally at first reflects their tendency to remain in a familiar environment, both for cultural or ethnic ties, and for well-established trade relations. Given the strong presence of its multinationals in West and Central Asia, Turkey is a clear example of this trend (Aykut and Goldstein 2006).

South-South investment is thus a well-known and well-established pattern, favored by recent privatization waves in developing countries. Despite being at lower levels, South-North investment is also rising, as EMNCs try to expand their markets globally (Aykut and Goldstein 2006). Among mature markets, the main destination of this type of investment is the EU-15, followed by Australia and Canada, during 1999-2008 (Bower 2009).

Sauvant (2005) argues that the primary motives behind investment choices of these enterprises are supporting trade and breaking into new markets. They try to achieve these goals through production, distribution and service-related investment. In fact, differently from developed countries, emerging markets are more likely to concentrate their foreign direct investment on the services sector and to "keep their manufacturing investments onshore, where wages are lower" (Economist 2012). Access to natural resources is another important FDI motivation, as well as cheap labor and the desire to diversify risks and profits. A very specific motive of emerging economies' firms is the need to strengthen their technological capacity, "traditionally one of the firm-specific advantage that actually lead firms to invest abroad" (Sauvant 2005).

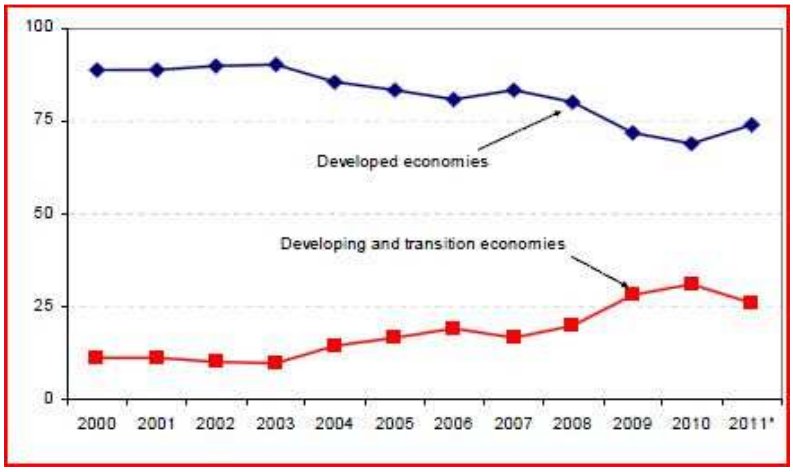
In his study, Deng (2012) argues that EMNCs often adopt a dual expansion path, that is entering both developing and developed markets, in order to build and strengthen their own capabilities on the one hand, and gaining global reach on the other. Investing in emerging markets helps EMNCs to "gain size and generate huge, instant efficiency gains from exploiting the technologies, business models, and practices that they have

managed to hone in their home markets", thus more successfully realizing economies of scale and scope (Deng 2012). Moreover, these firms likely have competitive advantages in emerging economies because of their "capability to manage in less munificent resource environments", which, on the contrary, developed markets' enterprises lack.

On the other hand, the capability building process is said to be the main motivation pushing EMNCs to invest in developed markets. Through overseas acquisitions in these countries, they aim at attaining external know-how, at gaining more direct access to strategic resources, and at "exposing themselves to sophisticated and cutting-edge demand" (Deng 2012). Expanding market power and distribution channels, as well as acquiring well-known brand names is also argued to be a significant pull factor, especially in the case of China. In their firm-level mergers and acquisitions study on outward FDI from emerging markets, Bower *et al.* (2009) found out that the bulk of M&A in advanced economies is conducted in basic materials and utilities sectors, in particular in mining, energy and steel.

Outward FDI by emerging markets' firms have been rising sharply in recent years, even though the recent global crisis had its negative repercussions, by giving it a slowdown, which started in 2010 and is still going on. The effects of the crisis have been registered in developed economies first, with a decline in outward FDI since 2007. Nonetheless, investment outflows started to rise again in 2010 and are continuing to do so, by reaching US$ 1.23 trillion in 2011, thus approaching the pre-crisis average. Emerging markets are not experiencing the same trends, because of the different and delayed impact the crisis had on them. In particular, Latin America and the Caribbean are witnessing a significant decrease in outward FDI since 2010, followed by developing Asia, which is also experiencing a slowdown. West Asia is now living a positive phase, after a severe decrease of outflows in 2010. In particular, Turkey registered a 68% increase, reaching US$ 2.5 billion, the level of the 2008 record (UNCTAD Investment Trends Monitor 2012).

Figure 13. FDI outflows shares by major economic groupings, 2000-2011
(percent)



Source : UNCTAD Global investment trends monitor n. 9, 12 April 2012

Asian countries are, among emerging economies, the largest source investors, especially in Greenfield investment projects (Aykut and Goldstein 2006). In particular, the so called Asian Tigers (Singapore, Hong Kong, South Korea and Taiwan) plus China reached extremely high levels of outward FDI, compared to both developed and developing economies (Sauvant 2005). There follow the BRICs, Mexico and Malaysia.

Both in the cases of South-South and South-North investment, FDI is strongly connected and depends on the business environment of host countries and regions, and on the industrial and development policies adopted there. Increasing liberalization in developing economies favors South-South investment, as do bilateral and regional trade and investment agreements (Aykut and Goldstein 2006).

From the side of source countries, government policies also play an important role. Given the relatively recent nature of outward FDI from emerging markets, the latter do not always have a well thought-through policy in this area. However, following the trend rising among developed economies, governments of emerging markets are losing reticence in “regulating and steering the economy” (UNCTAD WIR 2012). This is also happening because global competition causes a change in the relationship between governments and enterprises, their destinies being more and more related to each other.

In some cases, governments enact restrictive policies towards OFDI, because of the perception that outflows of capital affect their domestic productive capacity and employment. In fact, emerging countries often perceive themselves, (and many times actually are) as capital importing, rather than capital exporting, and they face the dilemma between supporting their firms' competitiveness through internationalization or having a more critical approach, in order to manage the public reaction to outward FDI (Sauvant 2008).

Many countries, on the other hand, strongly believe in the importance of overseas investment and its capacity to bring technology home, thus positively impacting the country's economic performance and competitiveness. This is why they provide clear regulations and supportive policies. The most mentioned example is the "Go Global" Chinese policy, which appears to have had a significant role on the expansion of OFDI from China. The Chinese government made changes including : 1- the creation of incentives for OFDI, 2- streamlining administrative procedures (including decentralization of authority to local levels of government), 3- easing capital controls, 4- the provision of information and guidance on investment opportunities, and 5- reducing political and investment risks (Luo *et al.* 2010). Beside this kind of provisions, governments can offer grants, loans, tax incentives and equity financing, as Singapore, for instance. Moreover, they can allow firms to realize overseas investments without the prior approval of the Reserve Bank, like in India. Or they can grant tax exemptions on remittances from income earned overseas, like in Malaysia.

The entrance of emerging economies' MNCs in the economic world order does represent a challenge, both for the former business champions, who fear growing competition, and for the new born multinationals, who have to integrate themselves in an already established order. As we mentioned before, these transformations of investment patterns are causing reactions both in source and host economies, and, if not properly managed, they could provoke the rise of feelings of opposition against FDI all around the world. Indeed, two main questions are raised by Sauvant (2005) about : "the appropriate policy regime for OFDI from emerging markets and the challenge of managing the public reaction to such investment".

2.4 – Outward FDI from Turkey : strategies and trends

Turkey's involvement in the world economy can be traced back to the 1980s, when the country decided to embrace a more open economy, replacing its economic strategy based on import-substitution with a new one based on export-orientation. Construction companies can be considered as the "pioneers" of international expansion, as they paved the way for the rest of the Turkish private sector during the 1970s (Erdilek 2005). Following the logic of the Washington consensus, Turkey decided to adopt neoliberal policies and to liberalize key sectors of the economy in the 1980s (Öniş 2010). Indeed, the opening up of the economy was followed by a wave of deregulation, trade liberalization and privatizations. In those years, Turkish firms started to expand in such markets as the EU, the Middle East and North Africa. They continued to grow internationally during the 1990s, in relation to Free Trade Agreements and development of regional unions (Erdil 2012). International trade was encouraged and it grew both in volume and value, also boosted by the Customs Union with the European Union in 1996 (Aybar *et al.* 2011).

This led to a slow growth of inward foreign direct investment as well, though not comparable to the performance of other emerging economies, that have been more successful than Turkey in attracting FDI, as we explained in the previous chapter (Erdilek 2003). Despite this, increasing FDI to Turkey had some positive effects to the outward FDI trend, for example, "by making Turkish firms more competitive through knowledge spillovers", and by pushing them to explore new markets, given the growing competition they were facing at home (Aybar *et al.* 2011).

Another reason for this growth is that the 1990s were characterized by an unstable economic environment in Turkey, "particularly due to high taxes, rising unit labor costs, and robust bureaucracy" (Uray *et al.* 2010). Moreover, the severe economic crises that Turkey experienced in 1994 and later in 2000/2001 are recognized to have had an important role in MNEs' investment decisions. As a consequence of the crises, purchasing power started to decrease, while at the same time production and labor costs were increasing, thus pushing Turkish enterprises to look for better opportunities in foreign markets. The International Monetary Fund played a key role in those times of

crisis, by imposing liberal reforms in exchange of its funding assistance. In order to fight and survive to these crises, Turkey had to become more competitive at the international level. It learned how to do so by "utilizing international markets much more efficiently while making use of domestic market characteristics to its own advantage" (Uray *et al.* 2010).

As we stated before, the growth of trade and inward FDI made the domestic market much more crowded in the late 1990s, thus contributing to push big businesses to internationalize. Turkish outward foreign direct investment started to rise, following a more general trend, which saw a growing number of emerging country multinationals engage in outward FDI (Uray *et al.* 2010). This is defined by some authors as the "Second Wave" of outward FDI by MNCs from emerging economies, coming after the first wave, which occurred during the 1970s and '80s (Yeung, Erdilek, Bonaglia).

The main difference between the two is that firms involved in the earlier wave of OFDI, which were relatively small in number and mostly situated in Asia and South America, were characterized by multinational ownership aimed at internationalize their domestic operations. On the other hand, "Second Wave" MNCs "appear to be driven directly by firm-to-firm contracting in a global setting" (Bonaglia *et al*. 2006), as they aim at globalizing their operations in order to compete successfully in the world economy.

Differently from developed markets' multinationals, those from emerging markets do not globalize because of cost factors *per se*, but rather to search for new markets and technological information (Yeung 1999). This is also the case of Turkish MNEs, trying to integrate in markets such as the EU, the United States, the Middle East, West Asia, the Balkans, the Russian Federation and the Turkic Republics in Central Asia (Erdilek 2003).

Investing in developed markets favors the access to advanced technologies and skills, while directing FDI to other emerging and developing countries, like the ones cited above, allows Turkish firms to enter into markets free of competition (Anıl *et al.* 2011). These firms look for natural resources in the Turkic Republics of Central Asia and the

Balkans, and for low-cost labor in Africa and Asia (Aybar *et al.* 2011). As for Europe, the first joint ventures and distribution channels networks have been established in countries where exporting activities have been built before, such as Germany, the Netherlands, and England (Erdil 2012).

In order to give a clear picture of Turkish outward FDI trends, we will now enter into detailed data information. The compilation of the balance of payments (BOP) and international investment position (IIP) data are governed by the Article 43 of 1970 Central Bank Law 1211, as amended by Law number 4651 of April 25, 2001. The Central Bank of Turkey (CBRT) collects all statistical information relating to financial system and other information considered necessary for the control of developments in the economy and the balance of payments. Inward and outward FDI stock data are disseminated after six months since the end of the reference year. FDI flow data consist of equity capital, other capital and real estate. Since 2010, the Undersecretariat of Turkish Treasury started to collect and disseminate data about direct investment abroad through an annual survey, which also covers 2009 and 2008 data (UNCTAD Investment Country Profile 2012).

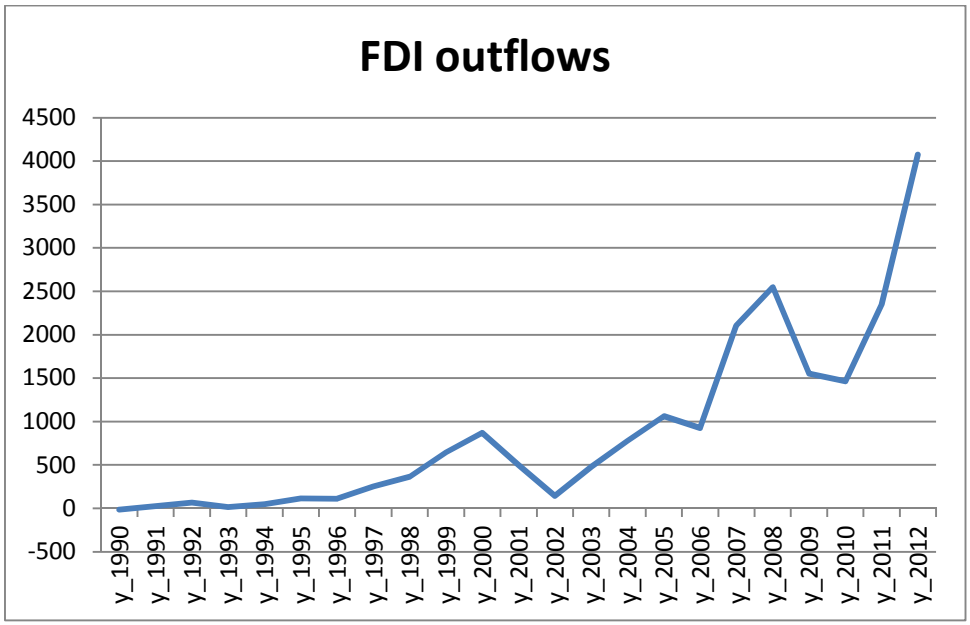
Despite progress reached in the field of data collection, and just like in many other emerging countries, it is fair to state that Turkish official FDI statistics do not reflect the true picture yet. This statement is verified by the incongruities showed by different data collectors. Indeed, depending on the source, and thus, on the way data are collected, figures can vary extensively. Many reasons can be found behind this phenomenon. The first relates to the full deregulation of the Turkish foreign exchange market in 1989, which made it very difficult for Turkish official agencies to monitor the type and entity of capital movements between Turkey and other countries. Another reason is the common practice of Turkish firms to invest abroad through firms registered in other jurisdictions, such as Germany, Switzerland, Luxembourg, or the Netherlands. “Through this mechanism, Turkish firms can access to developed countries’ insurance schemes and financing, which are scarce or difficult to secure in Turkey” (Trifonova and Alexandrov, 2003). This is why we can argue that official statistics underestimate

real amounts of investment. However, they are the only tool we are able to utilize in this context, and therefore, the only one we will report.

Table 4 and figure 14. FDI outflows from Turkey 1990 – 2012

(US$ million)

Year	OFDI amount	Year	OFDI amount
1990	-16	**2002**	143
1991	27	**2003**	480
1992	65	**2004**	780
1993	14	**2005**	1.064
1994	49	**2006**	924
1995	113	**2007**	2.105
1996	110	**2008**	2.549
1997	251	**2008**	1.553
1998	367	**2010**	1.464
1999	645	**2011**	2.349
2000	870	**2012**	4.073
2001	497		



Source : UNCTAD

As shown by the chart, at the end of the 1990s, we witness a peak in Turkish outflows, although from very low levels, that confirms the historical analysis. There follows a sharp decline caused by the severe economic crisis of November 2000 and February 2001. After this first phase of downturn, along with the recovery from crisis, outflows started to rise again in 2003, reaching the pre-crisis level in 2005 (UNCTAD Investment Country Profile 2012). Between 1992 and 2004, Turkey's growth rate of outward FDI rose an annual average of 26%, surpassed only by India (UNCTAD WIR 2006). After 2005, it accelerated again and reached a peak in 2008, in line with more general tendencies. Later, The global financial and economic crisis severely hit FDI outflows from Turkey, which fell dramatically in 2009 and 2010, even though the total stock maintained a positive trend. The downturn did not last long, and starting from 2011, outflows recovered to positive values.

Table 5. Turkey's OFDI stock 1990-2012

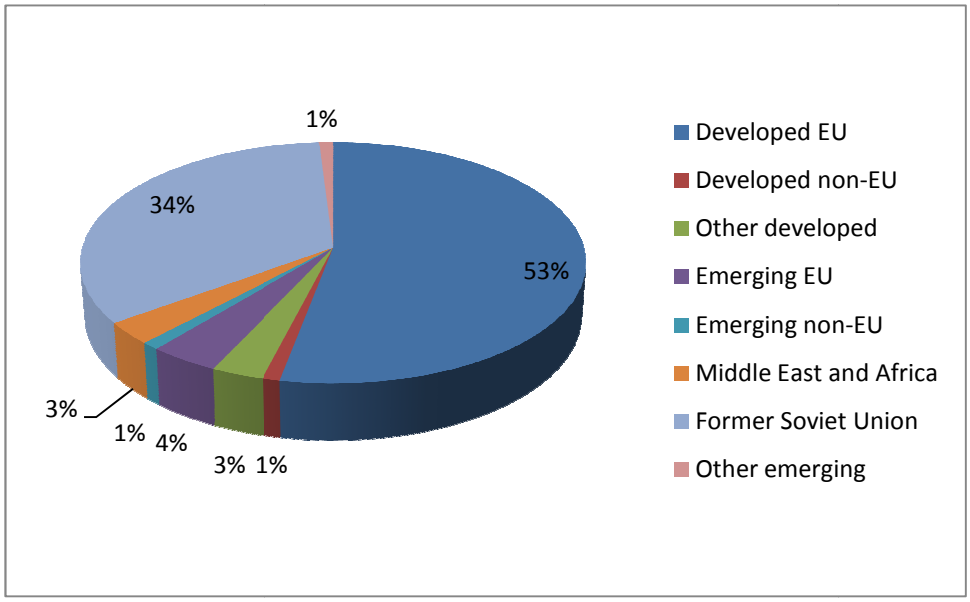
(US$ million)

year	OFDI stock	Year	OFDI stock
1990	1.150	**2002**	5.847
1991	1.177	**2003**	6.138
1992	1.242	**2004**	7.060
1993	1.256	**2005**	8.315
1994	1.305	**2006**	8.866
1995	1.418	**2007**	12.210
1996	1.528	**2008**	17.846
1997	1.779	**2009**	22.250
1998	2.146	**2010**	22.509
1999	2.791	**2011**	26.398
2000	3.668	**2012**	30.471
2001	4.581		

Source : UNCTAD

Figure 15. Geographical breakdown of Turkish OFDI, 2007

(percent)



Source : Demirbağ *et al.* 2010

Table 6. FDI outflows by main geographical destinations, 2007-2012
(US$ million)

region/economy	2007	2008	2009	2010	2011	2012
World	2.275	2.604	2.040	1.823	2.542	4.333
EU	1.621	1.370	1.537	1.254	1.879	3.501
Netherlands	310	369	279	699	526	2.764
Germany	42	143	82	68	90	61
Luxembourg	16	1	451	46	103	21
United Kingdom	15	57	72	25	20	84
Romania	16	24	20	20	27	32
Italy	6	7	7	14	45	23
Other Europe	9	332	32	42	30	70
Switzerland	4	332	32	37	28	66
North America	83	533	73	58	54	176
USA	82	532	55	57	43	150
North Africa	81	189	36	35	32	43
Egypt	26	17	20	18	22	20
Libya	3	3	9	10	1	2
West Asia	35	32	65	165	99	72

Bahrain	5	/	/	116	35	7
Lebanon	1	/	/	15	1	/
Iraq	9	/	35	11	28	20
Other Asia	24	144	51	63	66	85
India	3	14	25	24	14	25
China	9	1	5	19	9	18
Iran	/	128	3	13	4	2
SEECs and CIS	543	447	527	521	503	752
Azerbaijan	337	273	239	216	297	373
Belarus	/	/	100	100	/	/
Russian Federation	50	77	101	74	88	163
Georgia	11	6	3	6	25	12
BIH	7	10	21	61	22	7
Ukraine	18	15	9	24	25	12
Kazakhstan	75	29	33	13	78	56
FYR of Macedonia	11	1	/	8	71	12
Serbia	4	22	3	3	/	7

Source : Central Bank of Turkey

By 2011, 4339 Turkish firms have invested about 26 billion dollars abroad. Most of these investments were directed to the European Union, in particular to the Netherlands. However, part of the investment to this country was transferred from the Netherlands to a third country. At the base of this preference there are benefits of favorable taxes and the double taxation treaty concluded in 1986. The cumulative stock of OFDI from Turkey to the Netherlands was almost 8 billion dollars by 2011, with 220 Turkish enterprises investing in this country. The second European country preferred by Turkish investors is Germany, with a total stock of almost 600 million dollars and 335 Turkish firms (data from the Turkish Undersecretariat of Treasury).

Out of Europe, Azerbaijan is the most favored destination, with a total stock of 4.75 billion dollars and 152 Turkish firms investing there in 2011 (cumulative). During the 1990s, investment to Azerbaijan has been led by the Turkish Petroleum Corporation (TPAO), a state-owned petroleum enterprise. TPAO has a lot of interest in the Azeri energy sector, and also in other countries of the Caucasus, Central Asia, the Middle East and North Africa. Through the Turkish Petroleum International Company ltd. (TPIC), a

TPAO subsidiary, the Turkish Petroleum Corporation aims at participating in oil and natural gas exploration, in order to provide access to natural resources to Turkey (UNCTAD 2007).

Another significant destination of Turkish outward direct investment is the Russian Federation, with 288 Turkish enterprises operating there by 2011 and a cumulative stock of about 800 million dollars. The main sectors involved are retail services, durable and non-durable consumer goods, real estate and property development activities; market access and geographical diversification are the two main motivations (UNCTAD 2007). In 2012 the FDI stock reduced significantly, because of large disinvestments amounting to almost 2 million US$.

Despite the importance of Russia for Turkish outward FDI, when calculated on GDP, its impact reaches only 0,031 percent. On the other hand, OFDI stock to Romania has an impact of 0,125 percent on its GDP, thus making it the most attracting economy among Central and East European countries (data from the Turkish Undersecretariat of Treasury and UNCTAD). Because of this reason, chapter 4 will be fully dedicated to Turkish foreign direct investment to Romania.

The Undersecretariat of Treasury disseminates the sectoral breakdown of Turkey's outward FDI stock as well. By the end of 2011, "activities of holding companies" accounted for the bulk of investments, with a total amount of about 7.2 billion dollars out of about 26.3 of total stock. After, there come "financial and insurance activities", which contribute with about 6.5 billion dollars, followed by "mining and quarrying" with 4.7 billion dollars of investment. Other very important industries are "manufacturing" (2.9 billion), information and communication (1.2 billion), and "construction" (1 billion). According to official figures, financial services are concentrated in the Netherlands, as well as manufacturing and the communication sector. Germany accounted for the most of banking OFDI activities, followed by the Netherlands. About the energy sector, Azerbaijan receives the great majority of Turkish investment.

Table 7. Sectoral breakdown of Turkish outward FDI stock

(US$ million)

	2009	2010	2011	2012
AGRICULTURE SECTOR, *of which*	5	8	9	6
Agriculture, Forestry and Fishing	5	8	9	6
INDUSTRIAL SECTOR, *of which*	6.563	7.261	7.459	7.854
Mining and Quarrying	3.860	4.490	4.718	4.859
Manufacturing, *of which*	2.680	2.653	2.623	2.682
Food products, beverages and tobacco products	n.a	845	871	1.077
Textiles and wearing apparel	n.a	503	601	714
Leather and related products	n.a	0	0	0
Wood and products of wood	n.a	101	130	0
Paper and paper products; printing and reproduction of recorded media	n.a	158	168	115
Coke and refined petroleum products	n.a	2	2	3
Chemicals, chemical products, basic pharmaceutical products and pharmaceutical preparations	n.a	304	317	335
Rubber and plastic products	n.a	23	63	50
Other non-metallic mineral products	n.a	401	0	2
Fabricated metal products, except machinery and equipment	n.a	93	134	62
Machinery and equipment	n.a	9	7	1
Computer, electronic and optical products	n.a	107	217	108
Other transport equipment	n.a	20	25	22
Furniture and unclassified manufacturing	n.a	87	88	193
Electricity, Gas, Steam and Air Conditioning Supply and Distribution	23	107	108	299
Water Supply; Sewerage; Waste Management and Remediation Activities	0	11	10	14
SERVICE SECTOR, *of which*	13.356	13.492	16.429	19.330
Construction	194	233	453	426
Wholesale and Retail Trade; Repair of Motor Vehicles and Motorcycles	593	661	600	621
Transportation and Storage	393	263	280	1.702

Accomodation and Food Service Activities	134	152	43	144
Information and Communication	955	875	807	946
Financial and Insurance Activities, *of which*	10.656	10.547	12.411	14.138
Monetary intermediation activities	4545	3.901	4.843	4.518
Insurance, reinsurance and pension funding, except compulsory social security	1	4	5	2
Holding company activities	6082	6.469	7.420	9.116
Other financial service activities	28	173	143	502
Real Estate Activities	110	303	456	509
Professional, Scientific and Technical Activities	n.a.	16	343	14
Administrative and Support Service Activities	n.a.	5	433	546
Public Administration and Defense; Compulsory Social Security	0	0	0	0
Education	3	6	9	2
Human Health and Social Work Activities	0	19	171	190
Arts, Entertainment and Recreation	n.a.	25	26	25
Other Service Activities	317	387	397	67
TOTAL	**19.923**	**20.761**	**23.897**	**27.190**

Source : Turkish Undersecretariat of Treasury

According to Erdilek (2005), both large enterprises and small and medium-sized ones carried out their internationalization process through mergers and acquisitions, confirming more general tendencies. For example, two of the largest conglomerates, Koç Holding and Sabancı Holding, have pursued aggressive acquisitions both in developed and developing countries. On the other hand, a number of Turkish SMEs have invested in the neighboring countries of the Balkans and Central Asia to take advantage of investment opportunities given by large privatizations of previously state-owned enterprises.

In this regard, Erdilek (2005) states that most of Turkish firms investing in neighboring countries are SMEs, even though large enterprises account for the bulk of the total OFDI value. Moreover, the analysis of his case studies, especially those of SMEs, highlighted the trend that "Turkish firms prefer majority-owned joint-venture with local partners initially in order to minimize uncertainty and start up costs, cope with host country bureaucratic obstacles, and to gain access to superior technology." Once they have depleted the needed benefits from joint-ventures, they acquire full ownership and control of their affiliates.

Arçelik, an example of latecomer firm

Arçelik was founded in 1955 by Vehbi Koç, founder of the Koç Group, the largest industrial and services group of Turkey. Originally producing metal office furniture, Arçelik moved quickly into home appliances (Bonaglia 2006). The first Turkish washing machine was produced in 1959, using a Belgian license, and the first refrigerator in 1960, assembling the parts supplied by an Israeli company.

Today, Arçelik A.Ş. is the second largest member of the Koç Group, and Turkey's leader in consumer durables. It operates fourteen manufacturing plants in five countries (Turkey, Romania, Russia, China and South Africa) to produce the whole range of home appliances. It has 22,000 employees and comprises ten different brands, the major and original ones being Arçelik and Beko. Koç Holdings owns 57 per cent of its shares, the Burla Group controls 17.5 per cent, and the remaining 25 is publicly traded on the Istanbul Stock Exchange (Godstein and Bonaglia 2005 - Arçelik annual report 2011).

Arçelik started international expansion during the 1980s, by exporting to Turkey's neighboring countries, especially to Libya, Iraq and the Turkish Republic of Northern Cyprus. A number of reasons may be at the basis of this early export strategy: logistics, higher market standards in the West, government initiatives directed to Middle East countries, and finally, the relevance of psychic distance. With the fall of the Soviet Union and the regime changes in other Turkey's neighbors, demand for home appliances rose, and exports from Turkey boomed. The Customs Union with Europe in 1996 marked another turning point for Turkish trade, thus also for Arçelik, since it contributed to the opening of the Turkish market to foreign competition (Gülsoy *et al.* 2011).

Arçelik's internationalization process followed a "two-pronged strategy, fostering exports and acquiring new companies to enter or consolidate the company's position in foreign markets and complete its product range" (Goldstein and Bonaglia 2005). Starting from 1988, trade relations with Europe increased, thanks to a schedule of phased tariff reductions that Turkey agreed with the European Community. Arçelik started to sign several Original Equipment Manufacturer (OEM) contracts with home appliances firms in the United States and Europe. These contracts imposed to the Turkish firm a few restrictions, like the commitment not to sell similar products in Europe under own brands. In 1996, 50 per cent of washing machines' exports and 30 per cent of refrigerators were under OEM contracts (Bonaglia *et al.* 2006).

In order to elude contractual restrictions and to reinforce its technological and productive capabilities, Arçelik started a series of targeted acquisitions of foreign competitors. During the 1990s, the company invested significantly in R&D and started developing its own technology and brand. However, it is in the 2000s that it concentrates its internationalization efforts on aggressive acquisitions, also fostered by the 2001 economic crisis. Indeed, in this year, Arçelik made its first bid in Europe, trying to purchase Brandt, a French company bankruptcy, which, however, was sold to an Israeli competitor.

Building on this experience, Arçelik made major acquisitions the following year : Blomberg in Germany, Elektra Bregenz and Tirolia in Austria, Leisure and Flavel in Britain, and Arctic in Romania. With the British Alba Plc, it acquired the German brand Gründig in 2004, buying the remaining shares in 2007. After having acquired these well-known brands, Arçelik made further investments in them, by increasing production capacity of existing plants and by opening new ones (Gülsoy *et al.* 2011). In 2006, for example, it opened two new production plants, one in Romania and one in Russia, and a design centre in Italy.

Over the years 2000s, Arçelik A.Ş. has doubled its turnover, which in 2011 reached the record net amount of 8,437 million Turkish lira (around 4,669 million US dollars). A significant element is that international revenues account for 51 per cent of the total turnover. The company conquered important markets : it is the leader of home appliances sector in Turkey, Romania and South Africa, the second largest player in the UK market, and one of the top five players in Western and Eastern Europe (Arçelik annual report).

In his empirical study for UNCTAD (2005), Erdilek highlights the conditions thanks to which Turkish firms started to invest abroad, and the main drivers and motivations at the basis of this decision. These factors differ according to size of enterprises and country of destination. As we have already illustrated before, the Turkish economy have opened to international markets since the 1980s. Therefore, the government started to liberalize the country's OFDI regulatory environment, thus spurring Turkish firms' internationalization.

The first significant regulatory reform was the liberalization of the foreign exchange regime, which had been regulated since 1930 by Law 1567 for the Protection and the Value of Turkish Currency. This law, which severely restricted Turkish foreign exchange transactions and capital movements, was amended several times during the decades. The most important liberalizing reform, however, was Decree 32, issued by the Council of Ministers in 1989. "Under this Decree, Turkish residents are allowed to transfer, without seeking permission, up to 5 million dollars, in either currency or in kind, such as machinery, for OFDI purposes. Transactions exceeding 5 million dollars

would require the permission of the Undersecretariat of Treasury's Banking and Exchange General Directorate" (Erdilek 2005).

As a consequence of both the Uruguay Round of 1994, where the World Trade Organization (WTO) came into existence, and the Customs Union with the EU of 1996, Turkish foreign trade regime has also been progressively liberalized. The inward FDI regime followed this development as well, thus contributing to increase competitive pressure in the local market. As we stated before, these factors pushed domestic enterprises to seek foreign markets through both export and outward FDI.

Another significant motivation for Turkish firms to invest abroad was "their desire to escape from the constraints of home economic environment" (Erdilek 2005). Indeed, between mid 1980s and early 2000s, Turkish businessmen faced several difficulties under various aspects, in a dissatisfying business environment. Significant elements affecting good performance of firms were the high costs of labor (including social security premium and employment tax), of utilities (energy and water), of finance and credit, and of raw material and semi-finished goods (Kaya 2009).

In that period, the general Turkish economic environment was suffering major difficulties, as we mentioned before. High inflation rates and an increasing public sector debt brought to declining confidence, to a series of financial crises, a sharp rise in real interest rates, and a significant depreciation of the Turkish Lira. GDP rates were strongly fluctuating and hit by recessions. Its average growth was very modest compared to its potential and needs (OECD 2004). We can easily affirm that this unfavorable home country environment represented a strong push factor for Turkish firms' internationalization via FDI (Kaya 2009).

Indeed, one central element that influenced the birth and growth of Turkish multinational corporations (MNCs) has been "the chronic macroeconomic and political instability over more than three decades to which especially the large Turkish companies have adapted remarkably well" (Erdilek 2005). In this context, they were able to develop ownership specific assets and to internalize them through OFDI as a reaction to the eroding location-specific advantage of their home country.

Small and medium-sized enterprises were pushed abroad by difficult domestic conditions as well. Even though the Turkish business environment have improved considerably since 2003 (with lower inflation and higher real economic growth), SMEs who were suffering instability and heavy difficulties are still fighting for survival. Fiscal motives were recognized to impact firms' decision to invest abroad in a significant way. An example is the high exit costs that unsuccessful companies had to confront. Another, high corporate and personal income tax rates, which changed frequently and unpredictably over the decades (Erdilek 2005).

Regarding the so-called pull factors of OFDI, the fall of the Soviet Union and the restoration of capitalist regimes in numerous countries surrounding Turkey is a significant turning point for the international expansion of Turkish multinational companies. In fact, the latter gained the possibility to enter into new virgin markets, characterized by a relatively large and consumption-prone population (Demirbağ *et al.* 2010). The Turkic republics of Central Asia and the Caucasus are close to Turkey either in terms of psychic or physical distance and they have thus become among the most important countries (after Europe) where Turkish companies directed their foreign businesses during the 1990s and the 2000s. The privatization of state-owned enterprises in these countries enabled Turkish firms to increase their presence there even more. Other significant motives are : access to natural resources, access to markets, access to technologies, and access to brand names (Erdilek 2005).

Like other emerging countries' firms, a number of Turkish companies can be classified as "international born firms", that is "those firms whose first foundation took place abroad without any ownership advantage" (Anıl *et al.* 2011). Many of these firms have been established in the post-Soviet countries, where companies from developed economies did not invest easily. The perception of risk discouraged them, thus leaving large opportunities to Turkish firms, which could operate in a market free of competition. In order to benefit from the opportunities presented by those markets, Turkish companies have been established in such countries, without taking into consideration their level of technological development, nor the risks given by high costs of contract implementation.

This idea is verified by Anıl *et al.* (2011) in their study about the determinants of Turkish outward FDI in Romania, Bulgaria, Uzbekistan, Kazakhstan, Turkmenistan, Kyrgyzstan, and Russia. They identified 107 firms with wholly owned subsidiaries and 169 facilities in 129 sectors to which they submitted the questionnaire developed by Tatoglu and Glaister (1998). The majority of the companies consists of small-scale businesses, the average investment amount being 1,704,241 US dollars. 64 of the 107 firms were market seeking, and 43 were resource seeking. The analysis classifies the main motivations behind the firms' choice of host country. The most important pull factor appears to be the "Advantage of being the first to enter the market", demonstrating the validity of the point proposed before. The second one is "Purchasing power of customers", the third, "Level of competition in industry", the fourth, "Growth rate of the country's economy", the fifth, "Market size", the sixth, "Possibility of obtaining low cost inputs", the seventh, "Easy access to markets in neighboring countries", and the eighth, "Return to profit to the country of origin".

The authors analyze investing firms by dividing them into market-seeking and resource-seeking. The first group of companies, moved by the advantage of being the first to enter into those markets and willing to expand there, possesses considerable starting ownership advantages. They base their performance on cheap and qualified inputs, as well as on the size of the market and the purchasing power of the customer. On the other hand, resource-seeking companies aim at minimizing costs and directing their exports towards external markets. They invest in those transition economies in order to exploit cheap and quality inputs, low business taxes, and subvention advantages. "Attaching no importance to the domestic market, these firms create a positive externality in the countries in which they invest, by supporting the development of industry and exports" (Anıl *et al.* 2011).

Beside these findings, the authors reveal that almost all Turkish firms surveyed made their investments without considering the risk aspect, as we stated before. They also argue that companies did not invest in that region in order to seek strategic resources, because the material conditions of the region were not optimal for such kind of investment. Despite the limited research area, this study can be useful to understand

how Turkish newly globalized firms behave in a business environment free of competition, but also not very developed.

Another study releasing detailed information about Turkish investment abroad is the annual survey on Turkish multinational enterprises supported by Kadir Has University (KHU), KPMG Turkey (KPMG-T), the Foreign Economic Relations Board (DEİK), and the Vale Columbia Centre on Sustainable International Investment (VCC). This research has been conducted by a team of experts led by Professor Sedat Aybar, first in 2009, and later in 2010. It analyses the top 19 Turkish multinational firms on the basis of their foreign assets and highlights their characteristics, industry composition, strategies, and market and investment choices.

Table 8. Top 19 Turkish non-financial multinationals, 2009
(US$ million)

Rank	Company	Industry	Foreign assets
1	Sabancı Holding	conglomerate	8.051
2	Doğuş Group	conglomerate	6.357
3	Enka Construction	infrastructure	3.195
4	Turkcell	communication	2.996
5	Çalık Holding	conglomerate	2.633
6	Turkish Petroleum Corp.	oil & gas operations	1.254
7	Koç Holding	conglomerate	1.160
8	Şişecam A.Ş.	glass manufacturing	1.129
9	Tekfen Holding	conglomerate	1.003
10	Doğan Holding	conglomerate	801
11	Alarko Group	conglomerate	636
12	TAV Holding	conglomerate	571
13	Zorlu Enerji Group	energy	459
14	Orhan Holding	conglomerate	293
15	Eczacıbaşı Holding	conglomerate	262
16	Borusan Holding	conglomerate	235
17	Yıldız Holding (Ülker)	food and beverage	165
18	Eroğlu Holding	textiles	106
19	Çelebi Holding	conglomerate	95

Source : KHU−KPMG-T−DEIK−VCC survey of Turkish multinationals, 2010

By the end of 2009, these companies had 396 foreign affiliates : 70 per cent of the total number of affiliates was in Europe, 17 per cent in the Middle East and Africa, about 6 per cent in Asia and Oceania and another 6 per cent in the Americas. Of those 19 companies, only one is state-owned, the TPAO, and 15 are listed on at least one stock exchange.

The global economic and financial crisis heavily impacted Turkish outflows of FDI, by giving them a slowdown starting in 2009 and continuing in 2010. Many firms decided to adopt a "wait-and-see policy", while others were able to exploit the slowdown as an "opportunity to acquire new partners abroad and to update and reequip their workforce for the new economic environment". Turkish conglomerates responded to the crisis "mainly by drawing down their stocks and slowing down their production" (Aybar *et al.* 2011). Another strategy was product and regional diversification, which also helped companies to turn the crisis into opportunity.

Those firms responding to Aybar's survey declared that they intend to strengthen their presence in foreign markets, particularly in the Balkans, the Middle East and Africa. To enact their investments, most of them use a mixture of external funding and own capital. They declared to be unsatisfied with the availability of credit for foreign investment projects. Indeed, it is recognized that the Turkish government and the Ankara and Istanbul Chambers of Industry do not give proactive support for OFDI, at least until very recent years (Erdilek 2005).

Regarding the services sector, financing comes from own capital and long-term project financing. The main constraint to the initial stages of investment is recognized to be technical support, while shortage of workforce skills both at home and in host countries affects later stages. The construction sector proved to be the "locomotive of OFDI", even though it has been heavily affected by the global crisis (Aybar *et al.* 2011). Also the textile sector has been negatively impacted by the crisis, especially on the production side. The main cause was the shrinking of the credit markets on which textile firms were heavily dependent.

As we mentioned before, Turkish FDI outflows recovered in 2011 and are following a positive trend since then. The country emerged as one of the most significant investors in West Asia, even though the Gulf countries continue to account for most of the region's outward FDI flows. Turkey's outward investment amount increased by 73 percent in 2012 compared to 2011, mainly thanks to the $2 billion acquisition by Anadolu Efes of the Russian and Ukrainian SABMiller (UNCTAD WIR 2013).

Once again, large Turkish companies prove to be true international actors. Beside them, a lot of small and medium-sized enterprises have the same outward oriented look. The Commonwealth of Independent States (CIS), Central and East Europe, and South Eastern European countries are all privileged hosts of this investment from Turkey. The upcoming chapter intends to provide the general framework to understand these countries' economic situation and their potential as hosts of investment. Romania will be the main focus of this analysis.

CHAPTER 3

ROMANIAN ECONOMIC TRANSITION AND FDI PERFORMANCE

3.1 – Introduction to the chapter

After the collapse of the Soviet Union, the newly independent countries of Eastern Europe and Central Asia experienced major changes in their political, economic, social, and cultural structure, with a heavy impact on the lives of millions of people. The main economic revolution was the transformation from an economy based on state ownership and central planning to a market economy with a predominance of private ownership. By doing this, those states opened their economies to international integration and became part of the world economic system, with all its pros and cons. Romania was one of them.

All these so-called transition economies, went through common experiences during their transformation from central planning towards market economy. At the very beginning of transition, they experienced a severe economic shock, that some analysts attribute to the consequences of the Washington Consensus strategy, while others to other factors linked to the capability to reform of single countries. All these elements will be investigated below in the chapter.

Albeit transition economies shared the experience of shock, the depth, timing, and causes of this so-called "transformational depression" (Myant & Drahokoupil 2011) clearly varied between countries. After a few years of depression, most economies went through recovery and then reached sustained levels of growth, though with different forms and strength.

International integration played a key role in sustaining recovery from transformational depression in all countries. It developed in four main dimensions, as stated by Myant and Drahokoupil (2011) : trade in goods and services, movement of money and capital, movement of labor, and official financing from international agencies and through international aid. All these international aspects were considered

necessary to achieve overall external balance, and to import all sorts of goods that were severely needed at that time.

One way to be integrated in the international environment is through FDI. For instance, inflows of foreign direct investment are less volatile than other forms of capital flows, and they can be an important source of export, once investment projects are operating and directed to external markets. FDI came to transition economies first with privatization of state-owned enterprises and then, especially from the late 1990s, with Greenfield projects. Hungary was the leading country in attracting FDI, quickly followed by other CEEs and the Baltic republics, and then, with a significant lag, by Bulgaria and Romania.

Indeed, because of the reluctance of its early governments to implement deep restructuring and reforms, Romania followed a belated transition path. It opened its economy later compared to other countries, but this did not prevent it to reach high levels of international integration during more recent years.

Recovery brought to rapid growth in all CEE economies from the late 1990s and throughout the 2000s. Nonetheless, the global crisis of 2008 severely hit all those countries, thus revealing the limitations, both quantitative and qualitative, of that growth. With differences between countries, wrong policy choices and an "excessive faith in, and reliance on, free markets" prevented those economies to fully exploit their potential and to create a solid economic development (Myant & Drahokoupil 2011).

This chapter will first discuss the transition process in general terms, by presenting its main phases and by focusing on growth. There will follow an analysis of the Romanian transition and of the country's more recent economic performance. Then, foreign direct investment in Romania will be studied, by highlighting its composition, its main features and trends. A brief overview of the Romanian legal framework on FDI will be also presented at the end of the chapter.

3.2 – The transition process - general overview

The economic system of the Communist period was characterized by encouraging successes and disastrous failures. It succeeded in "achieving economic growth and

development, in securing, at least formally, full employment and a high degree of social protection" (Myant and Drahokoupil 2011), and in fighting inequalities, that reached very low levels, compared to market economies. However, it was not able to catch up with most advanced economies, and it lagged behind concerning technology and production of modern goods. It also failed to provide adequate supplies of basic consumer goods, thus undermining trade balance.

Indeed, after a few years of relatively good economic performance, with an annual growth rate of per capita GDP by 4.5 percent in the 1950s, Soviet countries and their affiliates were unable to keep pace with the fast changing world economy. The rigidities of their system frustrated invention, innovation and efficient allocation of resources. Therefore, these countries experienced an economic slowdown which started in the 1960s and continued during the following decades (Svejnar 2002). There emerged clear signs of declining dynamism and, especially by the 1970s, of stagnation. Despite the attempts during the final years of USSR to implement substantial reform, the old economic system was inevitably collapsing. The political change gave to state Socialism the final hit.

The collapse of the Soviet Union and its economic system based on central planning represented a major change in the world economy and international relations at the end of the 20th century. The fall of communism created large expectations about rapid recovery and growth, to be sustained by the new market-based economic system. But transition revealed itself to be more challenging than expected. The outburst of inflation, the fall of output and the rapid decline in GDP rates are only a few of the main difficulties that transition economies had to face. Despite numerous elements in common, these states have experienced their transition process in different ways and times. A brief overview of the main steps of transition process will be now presented, mostly referring to the IMF perspective published in 2000, though integrated with the contribution of authors from different theory groups. There will follow an in-depth analysis on reform and growth.

The economic transition process began fairly early after the collapse of the socialist regimes. It was composed by four main "ingredients", mainly based on the Washington

Consensus strategy, and identified by the IMF as : liberalization, macroeconomic stabilization, restructuring and privatization, and legal and institutional reforms.

First, liberalization refers to “the process of allowing most prices to be determined in free markets and lowering trade barriers”. This came after a long period when transition countries have been excluded from the price structure of the world's market economies.

Second, macroeconomic stabilization is “the process through which inflation is brought under control and lowered over time, after the initial burst of high inflation that follows from liberalization and the release of pent-up demand”. To reach this objective, discipline in fiscal and monetary policy needs to be imposed, and progress toward sustainable balance of payments supported.

Third, restructuring refers to the process of creating a dynamic financial sector and reforming the enterprises to render them able to operate in free markets. Privatization is the main tool for transferring their ownership from the state into “private hands”.

Final, legal and institutional reforms are those reforms needed to redefine the role of the state in these newly liberalized economies, establish the rule of law, and introduce appropriate competition policies (IMF 2000).

At the time of transition there rose a debate between two different approaches to the implementation of those measures, characterized as shock therapy, or “big bang”, and gradualism. The first and dominant one, at least during the early years, was centered on achieving the most rapid changes that were possible in the direction of a market system. The advocates of this view believed that it would be more effective to the purpose of making market price mechanisms working, and of liberalization and macroeconomic stabilization to introduce these measures quickly at the start of transition. (IMF 2000) They referred to the theory that a market system is essentially simple and can be created quickly. A political reason lied behind this choice as well, namely the fear that opposition would soon mobilize against reform (Myant and Drahokoupil 2011). Economists knew that this strategy was imposing severe economic hardship to those countries, but they also predicted it to be temporary and less burdensome than if the process was extended over time.

On the other hand, supporters of a more gradual approach were looking with more caution to the effects of reform and were fearing the political and economic consequences of shock therapy. They put emphasis on the role of the state and the institutional framework, by underlining the importance they had in the historical process of development of capitalism elsewhere in the world (Myant and Drahokoupil 2011). In absence of efficient institutions, too rapid liberalization and privatization would prove counterproductive.

A certain degree of flexibility did exist between the two views, even though the main consensus agreed on the need of rapid and decisive change. The package of reform measures was in perfect line with the dominant economic and political view of that time, the neoliberal thinking, supported by international agencies and propagated by teams of foreign advisers. The main elements constituting this economic theory were deregulation, privatization, great emphasis on use of the market, minimization of the role of state, reduction in the level of taxation. It became known as Washington Consensus, after the IMF adapted it to Latin American countries suffering from internal and external imbalances.

In the context of transition, differences between countries were recognized, which implied that the recommended policy packages were not completely inflexible. However, international agencies, namely the IMF and the World Bank, were imposing their strategy unilaterally, with little consultation with local economists (Myant and Drahokoupil 2011). During the years following 1989, all transition countries received financial assistance from the IMF, which was giving conditional support in exchange to some basic policy requirements. In this way, it had formal power over policy making on a number of economies, with stronger impact on those with large inherited debts, like Poland and Russia.

Two main shocks occurred as a consequence of the newly introduced liberalizing measures. First, an immediate burst of corrective inflation followed the liberation of prices from artificially low levels. Inflation was sustained by the pent-up demand that had built up during the period of central planning. At the start of transition, inflation reached the average level of 450 per cent a year in CEE, nearly 900 per cent in the

Baltics, and over 1000 per cent in the CIS. Nonetheless, in 1998 these levels have lowered significantly (data from IMF). Second, a heavy fall of output characterized all three groups of economies, clearly with differences in pattern between different countries. At the beginning of transition, output fell on average by 40 per cent, before it bottomed out, “far more than was expected”. However, this is likely to be a faulty estimation, based on probably over-estimated pre-transition levels of output. (IMF 2000) Anyway, by 1996, official GDP had dropped to well below 1988 levels throughout transition economies (Dunford and Smith 2000). Then, in 1995, a weak recovery started in all groups.

Much econometric research has been made to understand the patterns and causes of the severe fall of output occurring in transition economies. Myant and Drahokoupil (2011) recognize two main factors causing it : the policies of stabilization and liberalization following the advices of the IMF (“Washington Consensus depression”), and the disorganization associated with shocks such as the collapse of the Council for Mutual Economic Assistance (CMEA).

The Washington Consensus depression occurred in its purist form in Poland in 1990. The circular flow of income explains this phenomenon in a basic way : enterprises paid less wages, when measured in real terms. Consumers then spent less, and enterprises reduced their level of output. A divergence between enterprise behavior and that predicted by Poland’s policymakers also contributed to rapid decline. In fact, they were expecting lower demand to lead quickly to an end of price increases, while enterprises were passing on higher input prices following the freeing of trade and currency devaluation.

Disorganization refers mainly to the disruption in the production network, “particularly in the provision of materials and intermediate inputs, resulting from the collapse of central planning and the dismantling of vertically integrated conglomerates that operated under the old system” (IMF 2000). Being the most dependent on the CMEA market, Czechoslovakia was affected much more than other countries.

Table 9. GDP growth rates of transition economies at constant prices, 1989-2012 (percent)

country	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Albania	9,8	-10,0	-28,0	-7,2	9,6	8,3	13,3	9,1	-10,9	8,6	13,2	6,5
Armenia	14,2	-7,4	-11,7	-41,8	-8,8	5,4	6,9	5,9	3,3	7,3	3,3	5,9
Azerbaijan	-	-	-0,7	-22,6	-23,1	-19,6	-11,8	1,3	5,8	10,0	7,4	11,0
Belarus	8,0	-3,0	-1,2	-9,6	-7,6	-11,7	-10,4	2,8	11,4	8,4	3,3	5,8
Bosnia-Herzegovina	-	-23,2	-12,1	-50,0	-60,0	0,0	20,8	68,0	37,0	15,6	9,6	5,5
Bulgaria	0,5	-9,1	-11,7	-7,3	-1,5	1,8	2,9	-9,4	-5,6	4,0	2,3	5,4
Croatia	-1,6	-7,1	-21,1	-11,7	-8,0	5,9	6,8	5,9	6,8	2,5	-0,9	2,9
Czech Republic	1,4	-1,2	-11,6	-0,5	0,1	2,2	5,9	4,2	-0,7	-0,8	1,3	3,6
Estonia	8,1	-6,5	-13,6	-14,2	-8,8	1,6	5,0	5,0	10,8	5,4	-0,1	9,6
Georgia	-4,8	-12,4	-20,6	-44,8	-25,4	-11,4	2,4	10,5	10,6	2,9	3,0	1,9
Hungary	0,7	-3,5	-11,9	-3,1	-0,6	2,9	1,5	1,3	4,6	4,8	4,2	5,2
Kazakhstan	-0,4	-0,4	-11,0	-5,3	-9,2	-12,6	-8,2	0,5	1,7	-1,9	2,7	9,8
Kyrgyzstan	2,8	5,7	-7,9	-13,9	-15,5	-20,1	-5,4	7,1	9,9	2,1	3,7	5,4
Latvia	6,8	2,9	-10,4	-34,9	-14,9	2,2	-0,9	3,9	8,4	4,7	3,3	6,9
Lithuania	1,5	-5,0	-5,7	-21,3	-16,2	-9,8	1,2	5,1	8,5	7,5	-1,5	4,1
Macedonia, FYR	0,9	-9,9	-6,2	-6,6	-7,5	-1,8	-1,1	1,2	1,4	3,4	4,3	4,5
Moldova	8,5	-2,4	-17,5	-29,1	-1,2	-30,9	-1,4	-5,9	1,6	-6,5	-3,4	2,1
Mongolia	4,2	-2,5	-9,2	-9,5	-2,9	2,3	6,3	2,4	4,0	3,5	3,2	1,1
Montenegro	1,3	-7,9	-10,8	-21,0	-24,9	0,7	6,2	13,9	4,2	4,0	-6,7	3,1
Poland	0,2	-11,6	-7,0	2,6	3,8	5,2	7,0	6,2	7,1	5,0	4,5	4,3
Romania	-5,8	-5,7	-12,9	-8,8	1,5	3,9	7,1	3,9	-6,1	-4,8	-1,1	2,1
Russia	1,6	-3,0	-5,0	-14,8	-8,7	-12,7	-4,0	-3,6	1,4	-5,3	6,4	10,0
Serbia	1,3	-7,9	-11,6	-27,9	-30,8	2,5	6,1	7,8	10,1	1,9	-18,0	5,2
Slovakia	1,4	-0,4	-15,9	-6,7	-3,7	6,2	5,8	6,1	4,6	4,2	1,5	2,0
Slovenia	-1,8	-7,5	-8,9	-5,5	2,8	5,3	4,1	3,7	4,8	3,9	5,4	4,1
Tajikistan	3,0	-32,6	-7,1	-28,9	-11,1	-21,4	-12,5	-4,4	1,7	5,3	3,7	8,3
Turkmenistan	-6,9	2,0	-4,7	-5,3	-10,0	-17,3	-7,2	-6,7	-11,3	6,7	16,5	18,6
Ukraine	4,0	-4,0	-10,6	-9,7	-14,2	-22,9	-12,2	-10,0	-3,0	-1,9	-0,2	5,9
Uzbekistan	3,7	1,6	-0,5	-11,1	-2,3	-4,2	-0,9	1,6	2,5	4,3	4,3	3,8

country	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Albania	7,1	4,2	5,8	5,7	5,7	5,5	6,0	7,0	2,8	3,9	2,0	1,2
Armenia	9,6	13,2	13,9	10,1	14,0	13,2	13,8	6,8	-14,2	2,2	4,7	7,1
Azerbaijan	9,9	10,6	11,2	10,1	26,5	34,5	25,1	10,8	9,3	5,0	0,1	2,2
Belarus	4,7	5,0	7,0	11,4	9,4	9,9	8,2	10,0	0,2	7,7	5,3	1,5
Bosnia-Herzegovina	4,3	5,5	3,0	6,3	3,9	6,7	6,8	5,4	-3,4	0,7	1,7	0,2
Bulgaria	4,1	4,5	5,0	6,6	6,2	6,3	6,2	6,0	-5,0	0,4	1,7	0,8
Croatia	4,4	5,6	5,3	4,3	4,3	4,8	5,5	2,4	-5,8	-1,4	0,0	-2,0
Czech Republic	2,5	1,9	3,6	4,5	6,3	6,8	6,1	2,5	-4,2	2,5	1,9	-1,3
Estonia	7,7	7,8	7,1	7,5	9,2	10,4	7,2	-3,6	-14,1	3,3	8,3	3,2
Georgia	4,7	5,5	11,1	5,9	9,6	9,4	12,4	2,1	-3,9	6,3	7,0	6,1
Hungary	4,1	4,1	4,2	4,8	4,0	4,1	1,2	0,6	-6,3	1,3	1,7	-1,7
Kazakhstan	13,5	9,8	9,3	9,6	9,7	10,7	8,9	3,2	1,2	7,3	7,5	5,0
Kyrgyzstan	5,3	0,0	7,0	7,0	-0,2	3,1	8,2	7,6	2,3	-0,5	5,7	-0,9
Latvia	8,0	6,5	7,2	8,7	10,6	12,2	10,0	-4,6	-18,0	-0,9	5,5	5,6
Lithuania	6,6	6,9	10,3	7,3	7,9	7,7	9,8	2,8	-15,2	1,5	5,9	3,6
Macedonia, FYR	-4,5	0,9	2,8	4,1	4,1	3,7	5,9	4,8	-0,7	1,8	3,0	-0,3
Moldova	6,1	7,8	6,6	7,4	7,5	4,8	3,0	7,2	-6,7	7,1	6,4	0,6
Mongolia	1,0	4,0	5,9	10,1	7,3	8,6	10,2	8,9	-1,6	6,4	17,3	12,5
Montenegro	1,1	1,9	2,5	4,4	4,2	8,6	10,7	7,0	-5,3	2,5	2,5	0,3
Poland	1,2	1,4	3,9	5,3	3,6	6,2	6,8	5,0	1,7	3,9	4,3	2,0
Romania	5,7	5,1	5,2	8,5	4,2	7,9	6,0	7,1	-7,1	-1,7	2,5	0,3
Russia	5,1	4,7	7,3	7,1	6,4	7,4	8,1	5,6	-7,9	4,3	4,3	3,4
Serbia	5,1	4,5	2,4	9,3	6,3	5,5	6,9	5,5	-3,0	1,4	2,2	-0,9
Slovakia	3,4	4,8	4,8	5,2	6,6	8,5	10,4	6,2	-4,7	4,2	3,4	2,0
Slovenia	3,1	4,0	2,8	4,3	4,3	5,9	6,8	3,5	-7,8	1,2	0,6	-2,3
Tajikistan	10,2	9,1	10,2	10,6	6,7	7,0	7,8	7,9	3,4	6,5	7,4	7,5
Turkmenistan	20,4	15,8	17,1	14,7	13,0	11,4	11,6	10,5	6,0	9,2	14,7	11,1
Ukraine	9,2	5,2	9,6	12,1	2,7	7,3	7,9	2,2	-15,1	4,2	5,2	0,2
Uzbekistan	4,1	4,0	4,2	7,7	7,0	7,3	9,5	9,0	7,0	8,5	8,3	8,2

Source : EBRD; UNCTAD for 2010-2011-2012; World Bank for Azerbaijan

Depending on different initial and pre-transition conditions, the fall of output followed diverse patterns in different countries. The main differences impacting economic performance in transition, as highlighted by the IMF, were : “the ability to reorient trade toward the advanced market economies”; degree of industrialization; the share of agriculture in the economy; enrollment in secondary school, which impacted skill levels; the number of years passed under communism.

However, when considering distinct groups of countries, more specific differences emerge. CIS countries are the best example showing that the economic downturn was affected by a wide range of factors, not only economic. Indeed, these countries suffered of a much deeper “institutional collapse” (Myant and Drahokoupil 2011), that other economies did not went through. The collapse of the state, legal, and enforcement apparatuses became not only an obstacle for the development of a functioning market system, but even the catalyst for ethnic tensions which, in a few cases, brought to civil war, like in Tajikistan and Georgia. Another factor harming the economy of CIS was the breakdown of the financial and currency systems. The total loss of public confidence in the existing currencies brought to hyperinflation, that means an inflation level above 50 per cent per month. Besides, CIS countries were severely it by the breaking of links between the Soviet Republics, which contributed to the economic isolation of these new independent countries.

After the early decline, transition economies experienced a new phase of recovery in output, with clear national variations. In order to tame inflation, governments adopted an explicit or implicit exchange rate peg, linking their currency to an internationally held currency with relatively stable value. To maintain the peg, the state had to follow tight macroeconomic policies and reduce government spending. These policies, together with tight monetary policies introduced by more independent central banks, or the enforcement of the IMF discipline, contributed to bring inflation down. In particular, some studies proved that “countries that tamed inflation quickly and sustained the gains experienced a speedier and stronger recovery in output.” Indeed, “they were better able to maintain economic activity than countries where inflation was unchecked” (IMF 2000).

Nevertheless, the lowering of inflation was not sufficient for the revival of growth. Structural reforms facilitating the birth and growth of the private sector were needed. Studies made by the IMF and the European Bank for Reconstruction and Development (EBRD) reveal that, where structural reforms were implemented early and firmly, new production networks developed quickly. Among these were the CEE and the Baltic countries. On the other hand, countries that did not put in place sharp structural reforms suffered of output losses. However, this approach does not take into account the before mentioned, non-economic factors impacting output performances.

As privatization of large enterprises is concerned, the debate about the time of action comes into light again. Indeed, there was no complete agreement about whether it was more advantageous and effective to transfer assets from the state to the private sector in a rapid way, or to adopt a more gradual approach.

On the one hand, economists supporting rapid privatization were said to be motivated by "considerations of fairness, a desire to give ordinary people a stake in the economy". Moreover, they desired to take advantage of privatizations before the state bureaucracies could reorganize and resist the process. Some specific cases, such as Czech Republic and Russia, highlight the weak points and traps of this approach. In Czech Republic, state assets were transferred to millions of ordinary citizens, which subsequently sold them, thus contributing to the creation of investment funds. However, these measures did not help to restructure enterprises, either because of the lack of assets by those funds, or because they were controlled by state-owned banks, that did not impose hard budget constraints.

Even in Russia rapid privatization did not match expectations. On the contrary, it had disastrous economic effects. In order to support "self-induced restructuring of firms", economists were hoping to involve outsider ownership through secondary trading and to introduce transparent methods in the second wave of privatization of those firms still under state control. Despite this, inside workers and managers feared foreign ownership. In particular, managers "found it easier to keep enterprises alive by lobbying the state for subsidies than to foster competitive performance through involvement of outsiders." Moreover, the second wave of privatizations, in particular the so-called loans-for-share

regime, was non-transparent and it systematically favored investors and banks with ties to government interests (IMF 2000).

On the other hand, the choice of a more gradual scaling back of state enterprises proved to be more effective for the restructuring of enterprises. Those advocating this type of privatization meant to sale state assets to those likely to work on improving the performance of companies. Hard budget constraints were considered fundamental in order to force out chronic loss makers and thus facilitating investment to the more profitable enterprises. Hungary is a successful example of this gradual and pondered approach to privatization.

"With the death of faith in mass privatization into domestic ownership, the new panacea became foreign MNCs. Enterprises inherited from the past were either improved under foreign ownership, or their place in the economy was taken by new investment" (Myant and Drahokoupil 2011). Therefore, foreign ownership became determinant for growth in all transition economies, though especially in Central and Eastern Europe. Indeed, private capital flows, in the form of foreign direct investment, are considered helpful for economies in transition to grow and to enhance human development. Usually, governments respond to flows of foreign capital and investment with liberalizing policies, such as liberalization of capital, incentives, a conducive industrial policy, the implementation of pragmatic technology and labor policies. In transition economies, these policies need to be implemented in a comprehensive and thus more efficient way, avoiding short-term, ad hoc measures (UNDP 2002).

Depending on the thinking of MNCs and on political and economic situations in individual countries, different patterns of foreign participation took place. As FDI is concerned, the first acquisitions were directed to the manufacturing export-oriented sector, followed by public utilities in a second moment, especially telecommunications. Estonia and a group of CEE countries were leading the way and have recorded the highest figures until today. At the end of the 1990s, the FDI figure rose in all CEE and Baltic republics, both because foreign investors were directing their capital to a wider range of sectors, and because early opposition started to fade with the approach of EU accession. Moreover, governments were increasingly following Western European

models of financial and other incentives to foreign firms (Myant and Drahokoupil 2011).

The whole process of transition required a large amount of capital to realize it in a complete and coherent way. Some of the most important reforms to be made were the reallocation of investment into productive sectors, the modernization of antiquated machinery, the improvement of public infrastructure, and the allocation of financing for emerging firms. Given the general conditions, countries did not have the required capital available in the first years of transition. This is why international financial institutions, the European Union, and individual countries provided external assistance, even if on a limited scale.

The flight of capital from the uncertain initial circumstances in post-Soviet countries at the start of transition is another factor influencing capital scarcity. However, once the reform plan was clearly defined in many CEE and Baltic countries, private capital started to return. In particular, the reversal of capital flows did benefit these countries, where it favored a decline in inflation and improvements in the quality of structural reforms. In this respect, Russia had a different experience, as private capital massively flew away and did not return for many years after the start of transition. This explains why inflation has been brought under control, while implementation of structural reforms lagged behind (IMF 2000).

The transition period of post-Soviet countries was also characterized by the rise in income inequalities. The Gini coefficient measures the income inequality level of countries : it ranges from 0 to 1, where a value of 0 would indicate perfect equality, while a value of 1, the concentration of income in only one person. Pre-transition Gini coefficients were around 0.25, close to those of Scandinavian countries and far below that of the United States (0.4). During and after transition, Gini coefficients have increased, reaching peak values of 0.5, in Ukraine, for example. It is recognized that countries with better growth performance, such as with higher cumulative GDP growth in the first years of transition, experienced a smaller increase in inequality.

A dramatic consequence of the rise of inequality was the deterioration of social indicators in a number of countries. An example was the decline in the relative position

of retirees. The demographic pressure represented a problem which affected heavily the existing pay-as-you go pension system. Pension reforms were needed, even if it was already too late to remedy the damages on that generation of retirees.

If it is true that inequality reached different levels in different countries during the transition process, it generated "winners and losers" in all economies. (Keane and Prasad 2000) An example is given by Poland. In their study about inequality during transition in Poland, Keane and Prasad (2000) analyze the correlation between inequality, transfers and growth in that country. In particular, they aim at challenging the traditional wisdom that Polish income and consumption inequality increased in the first years of transition. Their estimates reveal that the Gini coefficient for overall individual income distribution declined from 0.256 in 1988, to 0.230 in 1992. Subsequently, it began a gradual increase, reaching pre-transition levels, and up to the value of 0.276 in 1997. On the other hand, "inequality in labor earnings increased steadily and substantially during the transition period of 1989-1997".

Another important point of their study is the analysis of social transfers in Poland. They claim that social transfers played a key role in mitigating the increase in income inequality during the early phase of transition. Different kinds of social transfers were directed, from 1989 to 1992, mainly towards the middle class and, through the increased generosity of pensions, to older workers, who were more likely to be affected by transition in terms of employment and earning prospects. These transfers had the political objective to create support for the "big bang" reform strategy. In fact, from 1993 onward, transfers were reduced and overall inequality began to rise. Even though social transfers did not entirely prevent poverty from increasing, Keane and Prasad highlight their significant role in "ensuring social stability and setting the stage for rapid reforms, including enterprise restructuring".

By extending the analysis to all transition countries whose data were available, the study deepens the search for correlation between equality and growth. The main results show the negative relationship between cumulative GDP growth and the change on the Gini coefficient in the first eight years of transition. At the same time, the positive relation between government transfers as a percentage of GDP and growth is

demonstrated. After including the EBRD transition indicator, that is the extent of liberalization, and the MDGT initial conditions measure in the analysis, further results are obtained. Initial conditions are said not to affect growth directly, once subsequent policy choices (the transition indicators) are controlled for. On the other hand, market liberalization is positively associated with growth. More precisely, growth is fostered by greater progress toward a market economy framework but, "conditional on the degree of liberalization, policy that maintains a greater degree of equality is more conducive to growth". Nonetheless, initial conditions are said to matter through their effects on policy. In fact, countries with better initial conditions tended to pursue policies that have resulted in rapid progress toward liberalization and smaller increases in inequality. This could lead to enhanced growth. (Keane and Prasad 2000)

The determinants of growth are a key issue in a number of studies about transition economies. In particular, the relationship between macroeconomic policies and reforms, and sustained growth is studied in literature. The main focus of the still ongoing debate is "whether progress in transition enables a country to grow faster, and if it does, whether the benefits are large and durable and outweigh the short-term costs often associated with transition". (Falcetti *et al*. 2005)

In their study, Falcetti *et al.* (2005) review the empirical literature on reforms and growth in transition, by comparing the early studies to more recent ones. Around 1996-97, economists started to analyze the short-term dynamic interactions among reforms and output variations and the impact of different kinds of policies on them. Three variables were recognized to be fundamental : a country's starting point, the implementation of sound macroeconomic policies, and reforms.

First, initial conditions are important for economic performance, and a good starting point is still today considered to be positive for overall economic growth, while this effect is also said to decline over time. In fact, it is demonstrated that countries with weak initial conditions can catch up after a delayed recovery. Nonetheless, a good starting point can have indirect effects on growth through its impact on reforms. (Falcetti *et al*. 2005) More specifically, Havrylyshyn *et al*. (1998) distinguish between initial structural conditions, including level of per capita income, over-industrialization

and urbanization and initial macroeconomic conditions, arguing that the first ones have a stronger negative effect on growth. Confirmed by later evidence, the study presumed that adverse initial conditions would diminish over time.

Second, early literature entirely agreed on the positive correlation between a credible macroeconomic stabilization program and growth. The annual inflation rate and the size of the fiscal balance relative to GDP were the main indicators of the effectiveness of stabilization measures. Most studies argued that lower inflation rates and smaller budget deficits are associated with economic recovery and higher growth rates. The empirical study conducted by Havrylyshyn *et al*. in 1998, for example, reveals that inflation levels higher than the range of 20-30 per cent significantly hurt growth. Simply by pushing inflation from very high levels to well below 100 per cent, a successful stabilization and reform program may induce growth. In order to maintain its positive effects on growth, this trend needs to continue.

Third, reforms were generally said to be beneficial for growth. In order to measure reforms in an effective way, they can be divided between initial-phase reforms, such as price and trade liberalization and small-scale privatization, and second-phase reforms, which affect corporate governance, competition policy and reform of financial institutions. Common results affirmed that early-stage, liberalization measures have a positive impact on economic performance in the first period of transition, while the improved quality of the institutional environment shows its benefits over time. (Falcetti *et al.* 2005) This is confirmed by Havrylyshyn *et al*. (1998), which states that "growth appears to be negatively affected by early reforms, but it is quickly compensated if reforms continue, and on balance growth is affected positively by the accumulated stock of reforms".

Recent literature proposes a more flexible approach to the question. Indeed, the causal link between reforms and growth in transition, has become more controversial. In particular, a few studies affirm that "there is no clear evidence that the net effect of reforms on growth is positive". (Falcetti *et al.* 2005) If it is true that the initial-phase reforms firstly have a negative effect on growth, but after one year they have a positive influence, the hypothesis that the sum of the two coefficients is zero cannot be rejected.

This is why we cannot conclude that the positive effect of initial reforms on growth is out of doubt.

Together with stabilization and macroeconomic reforms, Havrylyshyn *et al*. (1998) analyses another "policy variable", namely the impact of the size of government on growth. Even if it does not have the same importance as the previous factors, the size of the government does also affect economic performance in transition countries. It is argued that large governments have negative effects on growth, because of five main reasons. First, expenditures are directed heavily on unproductive sectors, such as subsidies to enterprises, a large bureaucracy, and an untargeted social safety net. Second, the continued interference of the government in many aspects of economic life, as well as deficiencies in the institutional framework represent an "obstacle to the development of a favorable business climate and the realization of the country's economic potential". Third, a heavy tax burden is also a deterrent for the development of the enterprise sector, and it has the side effect of encouraging the shadow economy. Corruption in the government is another factor weighing on enterprises, and finally, the inability to reduce government expenditures contributes to maintain budget deficits relatively high.

The same study tries to assess the relative importance of policies versus initial conditions, as a way to explain differences in growth performance between countries. Results show that macroeconomic and structural policies, and the size of the government have a much stronger impact on total variation than initial conditions. In fact, even if countries found themselves at an unfavorable starting point, it is relatively easy for structural policies to compensate for it.

Besides the three main drivers of growth discussed until here – initial conditions, stabilization policies, and reforms – Falcetti *et al*. (2005) highlight other factors potentially influencing growth in transition, that are : recovery, oil prices, and trade dependence. Regarding recovery, it can be argued that "other things being equal, the harder the fall, the greater the potential for a period of rapid growth once the recovery starts". Average growth rates in the years after decline were higher in those countries that suffered a long and deep recession, than countries where recession have been

relatively milder. The price of oil is also said to affect growth. Indeed, the surge in commodity prices, in particular that of oil, fostered the growth of oil exporting countries, thanks to improved terms-of-trade as well. In particular, the CIS indirectly benefited through trade and other linkages. On the other hand, oil importing transition economies suffered a significant constraint of growth. External demand is the third factor influencing growth, considering the growing impact that integration into the world economy has on transition countries. A greater dependence on international trade can bring short-run benefits if the main trade partners are booming, while it can generate costs if they are stagnating or in recession.

Another focus of the study is the "feedback effect of growth to reforms". In fact, final econometric results reveal that along with the strong influence that reforms in one period have on subsequent growth, the opposite correlation is also true. Higher growth is associated with further reform efforts, thus creating a "virtuous circle of reforms and growth proceeding in tandem". (IMF 2000)

The world financial and economic crisis of 2008 had a strong impact on all transition countries, and its effects are still very visible, though with different patterns in each country. By bringing an end to the period of recovery and the rapid growth of the immediately preceding years, the crisis highlighted the weaknesses of transition and its illusionary successes. The benefits of transition are not neglected here, but it is fair to recognize that it has not been able to bring post-Soviet populations to the well-being levels it promised. It did not create robust and secure economies, and none of those countries had been able to join world leaders in key areas of modern technology. FDI-based economies experienced the best performance, though highly dependent on developments in more wealthy economies.

The interpretation of Myant and Drahokoupil (2011) presents this outcome as a matter of missed chances. Indeed, numerous alternatives to the implemented economic measures and reform strategies did exist, but they were not taken into account. The study makes the comparison with China, for example, which succeeded in creating a stronger economy, and today is able to export modern manufactured goods. Post-Soviet economies, on the other hand, became "outposts for foreign MNCs", which did not

bring much of their high-value activities. No high-tech activities have been developed under domestic ownership, thus delivering the future of these economies into foreign hands.

According to the same study, the main mistakes causing transition countries' bad performances have been extreme liberalization, state breakdown, giving wealth to owners without the interest or ability to develop enterprises, and covering up for their economies' weaknesses with financial inflows. Where the openness to free markets was accompanied by the development of stable state structures and the regulations of market processes, like in many CEECs, the transformation depression was shorter and recovery more persistent.

3.3 – Romania's economic performance (1989 – today)

Depending on the source, Romania is considered as part of different groups of countries. In some cases, it is included among South East European countries (SEECs) (Myant and Drahokoupil 2011, Hunya 2004, EBRD), while in others among Central and Eastern European economies (CEE) (IMF). More comprehensively, it is simply considered one of transition economies. The IMF divides this group of countries into three geographical subgroups, that are : CEE, comprising Albania, Bulgaria, Croatia, Czech Republic, FYR Macedonia, Hungary, Poland, Romania, Slovak Republic, and Slovenia; the Baltics, namely Estonia, Latvia and Lithuania, and the Commonwealth of Independent States (CIS), consisting of Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyz Republic, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine, and Uzbekistan. In this paper, we will use the above-written categorization.

Romania is today a member of the European Union and the second largest consumer market in Central and Eastern Europe, with a population of 21,33 million people (data from the World Bank). In the last twenty years, it experienced hard transition times, recovery, growth, and then, hit by the global economic crisis, a declining phase again. Per capita GDP amounts at euro 5,800, against an EU average of euro 24,500. It ranks penultimate before Bulgaria. Its GDP of euro 136.5 billion in 2011, was mainly composed by the service sector with 45.4 percent. Then there came industry with 26.3 percent, and then agriculture with 9.8 percent. It has a large potential based on several

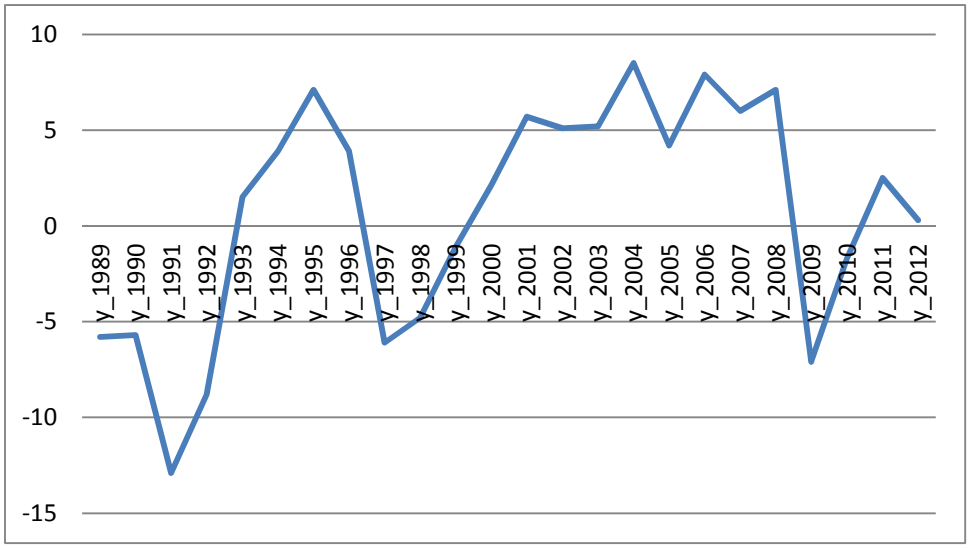
elements, among which : natural resources, market dimension, predisposition of its population to consuming, strategic geographical position, an educated but still competitive workforce, and the EU membership with its structural funds. Despite all these strong points, the economy of Romania is still very weak and it heavily relies on foreign investments and international markets' trends (ICE, Bucharest Office). We will now study the historical evolution of the Romanian economy, by analyzing its transition process and by focusing on FDI.

Mostly like other transition countries, during the Soviet time, Romania's economy was dominated by a massive industrialization led by the state. The main objectives of this policy were to develop economic sectors with the highest added value and to create new jobs to ensure full employment of labor source. By the 1980s, the industrial sector generated over 60 per cent of the total output of the economy (UNDP 2002). However, investment in industrial objectives did not include modernization of existing technologies, nor even technology imports. This, along with the concentration on obsolete intermediate goods and the involvement of big infrastructure and inefficient projects, represented a huge deficiency at the starting of transition. The economy of Romania was one of the most controlled and centralized of Central and Eastern Europe and the public sector was totally dominant in both industry and agriculture.

At the same time Romania had the peculiar advantage of lack of external debts, as a consequence of Ceausescu's obsession to pay them to prove Romania's independence in foreign relations. Another advantage was the enthusiastic wave for change rising in the Romanian society after the collapse of communism. Nonetheless, the governments in charge at the initial years of transition were not able to interpret and exploit these advantages in order to enhance progress. (Constantin *et al.* 2011) Therefore, like in all other economies, the conversion to a market-driven economy started with a dramatic fall in GDP in the early 1990s.

Figure 16. Romania GDP growth rate at constant prices, 1989-2012

(percent)



Source : EBRD; UNCTAD for 2010-2011-2012

Transition in Romania has been particularly slow and painful, due to its lower starting position compared to other economies, but, according to some opinions, mostly because of the gradual transformation process that was implemented, instead of applying "an effective shock therapy" (Constantin *et al.* 2011). The transformation of the economic system required numerous adaptations. Re-industrialization was considered a pillar, as industry was the central and most productive sector. The country needed a robust and dynamic industrial sector, one being able to act in an often irrational market environment. UNDP identifies three types of economic measures characterizing the Romanian transition : stabilization, liberalization, and structure or institutional measures. More specifically, the evolution of economic reforms can be divided into two main periods : from 1990/1992 to 1996, and to 1996 to 2000. Different political agendas and governing coalitions did mark these periods, as well as different conditions imposed on Romania by its agreements with the international financial institutions.

The first period was mainly characterized by programs aiming at restructuring the economic framework, including the legal status of State-Owned Enterprises (SOEs). Important legislative provisions of this period concerned Romanian enterprises. Law 15/1990 aimed at dividing enterprises into "autonomous and trading companies".

Autonomous Companies included state and defense monopolies, and public companies. Moreover, Law 84/1992 was integrated in the first privatization program; it created the State Ownership Fund and five Private Ownership Funds. Three programs were at the basis of this privatization effort : 1- the MEBO method; 2- the mass privatization program; 3- the capital market privatization, facilitated by means of tenders and public offers. Initially, these privatization measures created much confusion, particularly as the property structure was concerned. Law 18/1991, named “of the Land Fund”, was promulgated (and then modified until 1997) in order to reduce this confusion.

At the macroeconomic level, the 1990-1993 period was characterized by the implementation of monetary and fiscal policy measures, which had immediate negative effects. The total inflation rate reached a level of 300 in 1994, purchasing power declined and unemployment increased from 3 percent to 10 percent. (data from UNDP 2002) Other sharp macroeconomic measures were launched, following the agreement that the Romanian government signed with the IMF in 1991. It included a stabilization plan, a devaluation of the national currency, and the introduction of a new currency exchange structure.

In the first years, these measures did not prevent inflation from increasing, and the government had to extend its actions towards a tight inflation control and the reduction of the fiscal deficit. Moreover, it was forced to reduce subsidies for key sectors of the economy, such as agriculture, industry, and mining, thus causing an rapid decrease in real wages. Privatization advanced at a slow pace, growth did not rise significantly, while debt and budget deficit continuously showed increasing rates. Capital flows did not accelerate, although the net foreign direct investment significantly increased throughout the decade.

Liberalization and privatization measures were not properly synchronized with the development of those institutions that were needed for a well-functioning market economy. In some cases, inadequate institutional arrangements had negative repercussions at the economical, political, social, and even environmental level. These contributed to enlarge poverty and inequality, which in turn provoked “disappointment with market reform, and further weakened the authority of government to establish

effective institutions". (Constantin *et al.* 2011) All these difficulties made real advance of reform very difficult. The EU and the international financial institutions criticized Romania for its incapacity of restructuring and privatizing in an efficient way, of eliminating losses within the economy and of reforming the public administration significantly.

The year 2000 represents a turning point for Romania, both because it was the year of the beginning of a slow economic recovery, and also because there started the negotiations for the accession to the European Union. From this moment onward, the Copenhagen accession criteria dominated the political and economic discourse. The economic criteria were based on two mains dimensions : the existence of a functioning market economy and the capacity to face the pressure of competition and market forces within the EU. But Romania was coming out of ten difficult years of transition, and the previous delays and failures made the efforts to meet the EU criteria even harder. (Constantin *et al.* 2011) After years of successes and failures in building up a functioning market economy, Romania finally became member of the EU on January 1st, 2007.

The years immediately before and after the adhesion to the EU were characterized by significant growth in the Romanian economy, bolstered by increased foreign investment and export-oriented production, labor productivity growth, and increasing domestic demand for consumption. Romania's good performance was also supported by an improved European economic climate and a "favorable international economic juncture, with a robust growth of world economy, effervescent international trade, high prices of goods, and international financing with relatively low costs" (Zamfir 2010).

The growing process of globalization, with its extremely high levels of economic and financial interconnectedness represented for Romania a source of development opportunities and vulnerabilities at the same time. The global financial crisis found Romania highly unprepared, thus pushing it into a severe economic crisis, marked by a strong reduction of economic activity in all sectors and a rapid deterioration of all economic indicators (Zamfir 2010). A sharp decline in GDP growth was registered since 2009, when it reached the negative value of -7.7 (the EU-27 average being -4).

The weak reaction of the government also impacted unemployment, which reached a much higher rate compared to the EU average. The private sector, in particular the manufacturing industry, construction, retail trade, and transportation, did collective layoffs and started to reduce personnel already in 2008. The number of employees in public sector started to decline in the first quarter of 2009. The contraction of employment was also deepened by a large number of SMEs closing down or narrowing their activity. However, the registered unemployment rate started to decline in the second quarter of 2010, falling from 8.4 per cent, to 6.9 per cent, much lower than the EU average of 9.6 per cent (Stanculescu and Marin 2011).

Much like other newcomers to the European Union which kept their own currency, Romania is taking good advantage of this fact. Indeed, it has the flexibility to set interest rates, control liquidity, and allow the currency to depreciate to help rein in the deficit. On the other hand, euro zone weak countries like Greece, Ireland or Spain cannot control monetary policy and they have to rely primarily on fiscal policy. By maintaining its cheaper currency, the lei, Romania has made exports more competitive and the living cost lower, thus starting to attract highly qualified workers from "struggling euro zone countries" (Bilefsky 2012). To help the country cope with crisis, but in exchange for severe spending cuts, the International Monetary Fund, the European Union, and the World Bank allocated a $26 billion rescue package. This allowed Romania to prevent budgetary shortfalls, but imposed a decrease by 25 per cent in public sector wages, and the rise of value-added tax to 24 percent from 19 percent.

Romania's political situation is not one of stability and transparency. Indeed, recent political turmoil shook investors' confidence, though not impacting the business environment in a severe way. Romania attracts a high number of enterprises willing to build strong and durable links there. It offers a "talented pool of engineers, relatively low wages, and a strategic location between east and west" (Bilefsky 2012).

3.4 – FDI in Romania : main trends and recent developments

In the last years, Central and Eastern European countries have become very attractive destinations for foreign direct investment. Especially for Poland, the Czech Republic, and Hungary, the first years of transition have been characterized by a significant surge

in FDI, in line with the global growth of direct investment operations. Political stability and macroeconomic stabilization, including institutional development, were important premises for an attractive business environment (Birsan and Buiga 2008). The increase in FDI inflows was also sustained by the European Union strategy of strengthening and intensifying the economic relations with its neighbors (Altomonte and Guagliano 2003).

These countries generally offer attractive conditions for investors, both domestic and foreign. The main determinant factors are the relative high growth rates and growing market potential. Moreover, labor costs are comparatively lower, labor force is skilled and educated, and the fiscal regimes have become very encouraging in a number of these countries.

Compared to FDI to CEE, capital inflows to South East European countries are very low. Indeed, these economies have been less successful in attracting investment because of several reasons. The most significant ones are identified in : political instability, low intra-regional trade, and the small size of national markets. Despite this, Balkan countries recognize the importance of attracting FDI to foster economic growth, and for this purpose, they have created a favorable legal framework helping to improve their comparative performance (Slaveski and Nedanovski 2002).

FDI had an important role in assisting rapid restructuring and economic development in all CEE countries, although they attracted foreign investors to a very different extent. In particular, MNCs were attracted to countries “with which they had been in contact in the past, which had heritages of reasonably modern industry, good physical infrastructure, and links to Western Europe” (Myant and Drahokoupil 2011). Moreover, political stability was important for companies undertaking long-term investment, and the likelihood of EU accession also served as attractive factor. MNCs looked for a secure legal and business environment, that could guarantee that contracts would be honored. Specific policies aiming at attracting FDI, such as the offer of infrastructure development, subsidies, and other concessions, had a significant role as well.

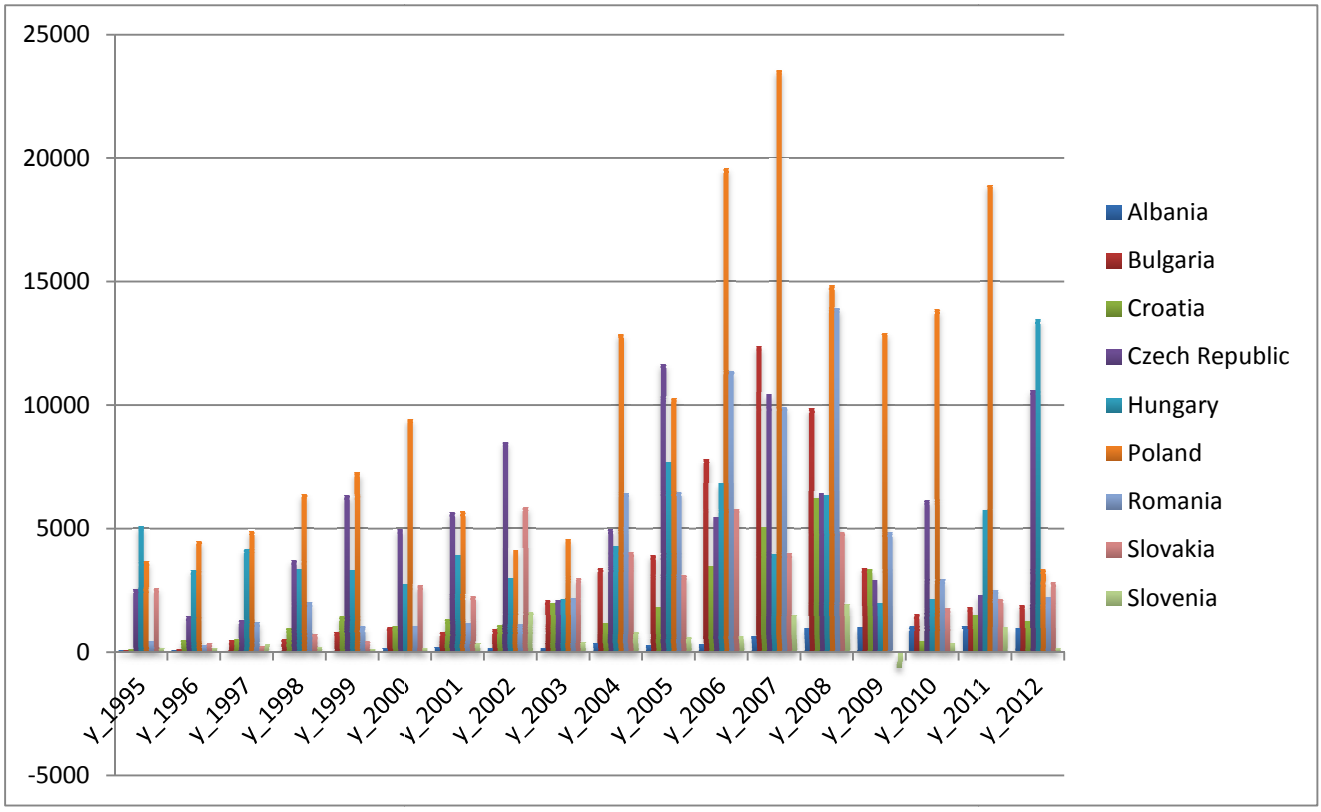
Privatization of formally state-owned enterprises has been an important determinant of inflows of FDI into CEEs, especially during the early years of transition. However, it was a lumpy and time-bound phenomenon, the privatization process being essentially

completed in all economies today (Demekas *et al.* 2007). Besides the opportunities given by privatizations, FDI inflows were also depending on investors' current perceptions about the attractiveness of the host economy and future expectations about profitability (Stephan 2006).

The main strategies that investors follow to penetrate these markets are : Greenfield investment, participation in the privatization process (Brownfield) and mergers and acquisitions of already existing private or state owned enterprises. (Birsan and Buiga 2008) CEE countries experienced an impressive increase in FDI inflows on the eve of EU accession and immediately afterwards (Savoiu and Popa 2012).

Figure 17. FDI flows to CEE countries 1995-2012

(US$ million)



Source : UNCTAD

As we stated before, Romania started its economic reform after other transition economies, due to the fact that implementation of reforms had been slow and hesitant.

As a consequence, foreign direct investment also started to arrive later. Indeed, the government did not implement favorable policies toward FDI, and the type of mass privatization it followed did not support it either. Nonetheless, the situation started to change in 1998, when the stock and flows of direct investment in Romania started to increase. This was mainly due to large scale privatizations, positive changes in the business climate and the progress in fulfilling the criteria of adhesion to the EU.

At the end of the 1990s and the first 2000s, EU candidates were recording increasing growth rates, declining levels of unemployment and relatively stable short and medium-term prospects for growth. Moreover, they were managing to normalize their foreign debts and to enter private financial markets. All these factors were highly encouraging FDI (Hunya 2004). From 2004 onward, FDI flows to Romania accelerated, "with net inward FDI flows as a share of GDP exceeding the inflows recorded in both the eight Central and Eastern European countries which joined the EU in 2004 and the EU-15" (Pauwels and Ionita 2008). Some of the FDI related to privatizations attracted more investment in those years, thus contributing to enlarge the export base (Hunya 2004). In 2006 Romania overtook the Czech Republic as the third largest destination of FDI flows among newly entered Member States, after Hungary and Poland. 80 per cent of total FDI stock of Romania comes from the EU. Austria, the Netherlands and Germany are the most investing countries (50 per cent of total stock in 2011).

Table 10. FDI stock in Romania by country of origin, December 2011
(EUR million)

Country	FDI stock
TOTAL, *of which*	55.139
1- Netherlands	11.982
2- Austria	9.667
3- Germany	6.272
4- France	5.042
5- Italy	3.341
6- Greece	2.934
7- Cyprus	2.536
8- Switzerland	1.839
9- USA	1.420
10- Luxembourg	1.274
11- Belgium	1.116
12- Spain	958
13- Czech Republic	816
14- United Kingdom	719
15- Turkey	622
16- Hungary	611
17- Sweden	402
18- Lebanon	330
19- Canada	256
20- Denmark	241
21- Norway	209
22- Poland	198
23- Portugal	194
24- Ireland	193
25- Gibraltar	193
26- British Virgin Islands	190
27- Japan	183
28- Finland	170
29- Israel	166
30- EBRD (European Bank for Reconstruction and Development)	162
Other	903

Source : National Bank of Romania

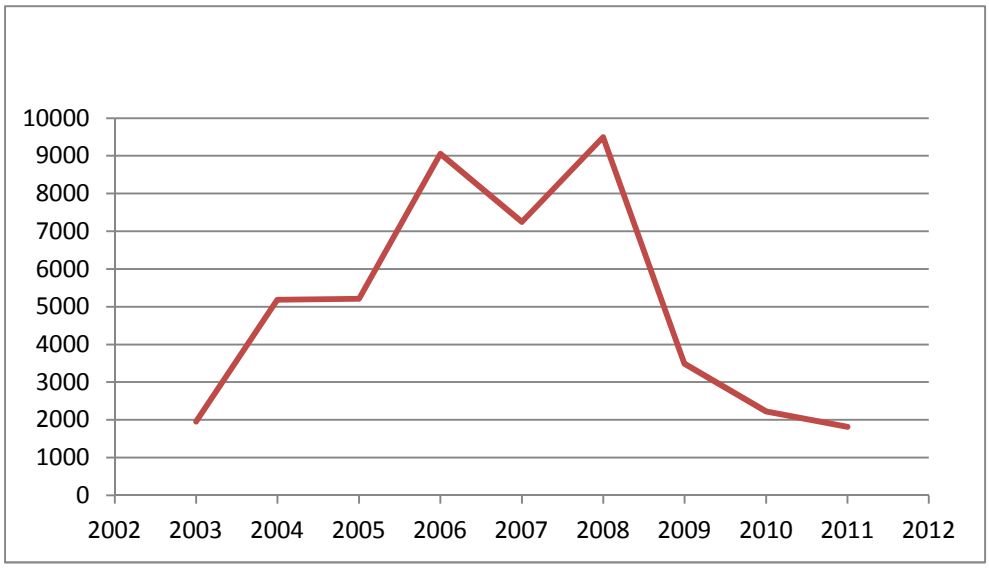
Despite good general performance in the last two decades, FDI flows to Romania show a high degree of fluctuation. As we mentioned before, in 2004 we witness a "multiplication of total volume of FDI over two hundred times, much higher than the average European or global evolution", when analyzed as a share of gross fixed capital formation (Savoiu and Popa 2012). Another peak was registered in 2006, mainly due to the privatization of Banca Comerciala Romana (BCR). Indeed, thanks to the acquisition of 61.88 percent of its shares by Erste Bank, the Romanian state gained 2.2 billion euro.

Subsequently, a decrease in inflows was registered in 2007, as a consequence of the declining importance of privatization-related FDI. The main sectors involved in FDI were public utilities, banking and construction, and they represented nearly half of total FDI stock. With the completion of the privatization program, this type of FDI lost its significance (Pauwels and Ionita 2008). A subsequent increase was registered in 2008, when the total stock of inward FDI reached 48,798 million Euros. In that year, Romania hosted 145 new FDI projects, which created in total 11,403 new jobs.

Following the general trend, the global economic crisis affected FDI in Romania as well. A sharp decline in inflows was registered since 2009, when, according to a study released by Ernst and Young, the country recorded 48 per cent reduction in the number of FDI projects and 44 per cent in the creation of jobs, compared to the previous year. Relative to other countries in the region, the crisis hit Romania and its capacity to attract investment in a more violent way. From figure n. 17 we clearly witness this fact : from the second position as hosts of FDI in 2008, it went down to the fifth in 2012.

After two disappointing years, Central Eastern European countries have regained traction as FDI destination in 2012. Though investment projects diminished by 4.8 percent in that year, the region registered an increase in job creating by 26.1 percent, thus overtaking Western Europe as the leading recipient of FDI jobs in Europe (E&Y Investment Monitor 2013).

Figure 18 and table 11. FDI flows to Romania, 2003 – 2011*
(EUR million)



year	FDI flows	% change on previous year
2003	1.946	60,6
2004	5.183	166,3
2005	5.213	0,6
2006	9.059	73,8
2007	7.250	-20
2008	9.496	31
2009	3.488	-63,3
2010	2.220	-36,4
2011	1.815	-18,2

Source : National Bank of Romania
*equity stakes plus credit

The sectoral composition and the main motivations of FDI flows to Romania have been changing over time. During the last two decades, investment in Romania was mainly driven by low-cost motivations, especially as the manufacturing sector was concerned. Unskilled labor-intensive activities were the solid basis of the industrial

sector. Access to the domestic market was not the main driver of FDI, since production was mainly directed towards external markets (Birsan and Buiga 2008).

In more recent years, this pattern has been changing. While hourly labor costs remain low (Romania is overcome only by Bulgaria in Europe), “a tightening labor market and skill shortages, partly due to large outward migration, have contributed to significant increases in private sector wages”, which until 2008 were growing by about 20 per cent annually (Pauwles and Ionita 2008). This is why global low-cost investment flows are moving towards the East and South Asian markets. Therefore, much like other Central and Eastern European countries, foreign investment in Romania is progressively being directed towards value-added production, with a stronger emphasis on the growing domestic market. FDI itself represented a significant instrument facilitating this transformation. In fact, those “countries which have experienced the largest FDI inflows have also witnessed the largest increase in skilled-labor and capital-intensive exports” (Pauwels and Ionita 2008).

The huge increase in the share of FDI to the services sector and the transformations undergone by manufacturing demonstrate this evolution. Most CEE countries shared this trend in changing FDI distribution by sector (Stephan 2006). In Romanian services, financial intermediation and insurance have quadrupled their shares of total FDI between 2003 and 2006, becoming the second largest beneficiary after manufacturing. It has maintained this position until today. The main motivations behind this rise are the growing population and rising living standards. Other services like wholesale and retail trade, real estate and business activities have doubled their FDI share as a percentage of GDP during the same period (Pauwels and Ionita 2008).

Nonetheless, manufacturing remains the most important sector for FDI, even though it is undergoing major transformations. For instance, FDI in clothing and wearing apparel sector decreased, while investment towards the furniture sector and transport equipment rose. Thanks to its well-trained labor force, companies from all over the world are today coming to Romania to produce transport equipment, in particular the sub-sectors of motor vehicles and shipping.

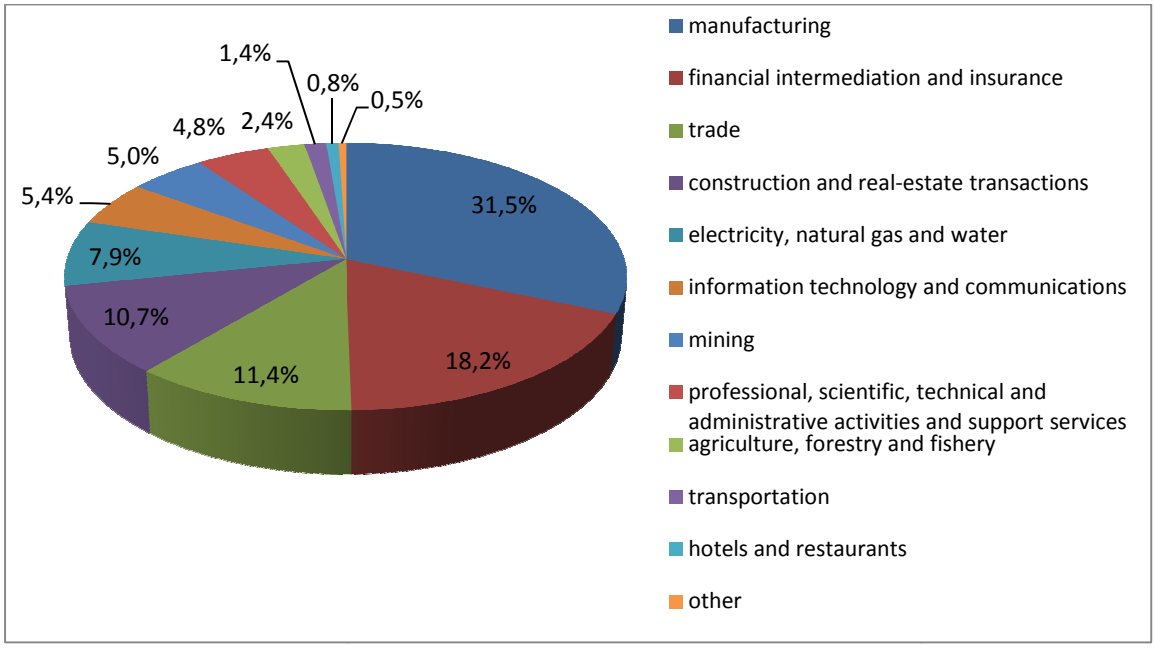
Table 12. FDI in Romania by main economic sector, December 2011

(EUR million)

Sector	FDI stock
TOTAL stock, *of which*	55.139
Industry, *of which*	24.487
Mining	2.753
Manufacturing, *of which*	17.372
food, beverages and tobacco	2.251
cement, glassware, ceramics	1.768
wood products, including furniture	1.029
computers, other electronic, optical and electrical equipment	1.062
machinery and equipment	995
metallurgy	2.695
transport means	2.840
crude oil processing, chemicals, rubber and plastic products	3.468
textiles, wearing apparel and leather goods	798
other manufacturing sub-sectors	466
Electricity, natural gas and water	4.362
Professional, scientific, technical and administrative activities and support services	2.679
Agriculture, forestry and fishery	1.316
Trade	6.282
Construction and real-estate transactions	5.897
Hotels and restaurants	431
Financial intermediation and insurance	10.026
Information technology and communications	2.967
Transportation	787
Other	267

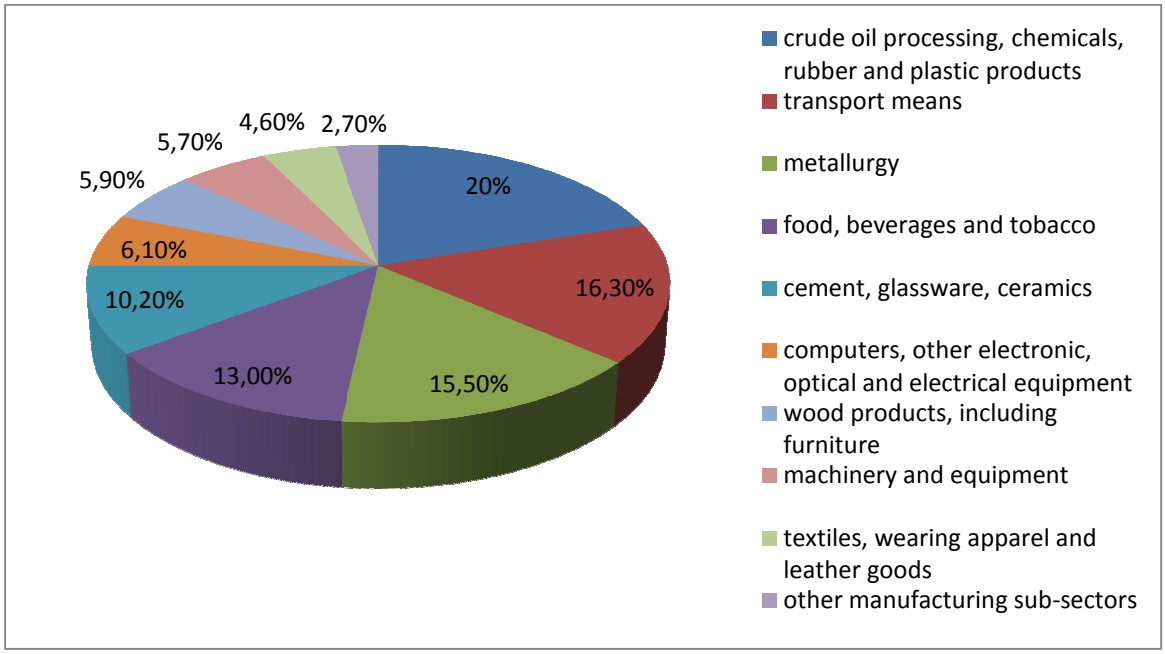
Source : National Bank of Romania

Figure 19. Sectoral breakdown of FDI stock by December 2011
(percent)



Source : National Bank of Romania

Figure 20. Manufacturing
(percent)



Source : National Bank of Romania

Of the total FDI stock, EUR 26,254 million are invested in Greenfield projects (47.6%), the main source countries being the Netherlands, Germany, Austria and Italy. Not surprisingly, the sectoral distribution of Greenfield projects does not differ significantly from the general one. Limiting the analysis to 2011 (the last available year as to official statistics), the partition of FDI flows changes significantly. Indeed, 97.2 percent went to corporate development, 2.1 percent to mergers and acquisitions, and only 0.7 percent to Greenfield investment. This means that very few new plants have been built in 2011.

Despite the crisis and recent political instability, a number of large foreign investors still count a lot on Romania and plan to remain there for the longer term. Competitive costs of doing business here are said to offset the "punishing downturn". Moreover, the country maintains its strong points, such as the "talented pool of engineers, relatively low wages, and a strategic location between East and West" (Bilefsky 2012).

FDI in Romania have an important impact on national trade as well. Indeed, most of Romania's foreign trade is composed by export and import activities of FDI enterprises; more specifically, 71.4 percent of total exports and 62.6 percent of total imports by 2011. The main sub-sector involved is manufacturing, in particular transport means, machinery and equipment, metallurgy, chemical products, and textiles for both exports and imports, yet with different percentages on total. Transport means, metallurgy, and machinery and equipment are also the main contributors to the trade surplus of manufacturing (EUR 4,015 million by 2011). Despite a relatively low FDI level, agriculture, forestry and fishery is the other sub-sector recording an aggregate surplus. FDI enterprises in all other sub-sectors reported and aggregate trade deficit. (National Bank of Romania)

Regarding the territorial distribution of FDI, the Bucharest-Ilfov region is the main investment recipient, with a percentage of 61.7 of the total amount in 2011. This area offers better infrastructure, more abundant labor supply and higher quality of labor. Other development regions attracting FDI were : the Central region (7.6 per cent), the South-Muntenia region (7.4 per cent), the Western region (7.2 per cent), and the South-Eastern region (5.4 per cent). (data from the National Bank of Romania)

3.5 – FDI legal framework in Romania

Starting from 1991, Romania adopted a legal framework aiming at attracting foreign capital to its economy. In order to provide the most suitable and efficient incentives to be granted to investors, the legislation has been revised several times, adapting to the market demands and to the changes and needs of a dynamic business environment (Pirciog 2004). The establishment of the Romanian Agency for Foreign Investment (ARIS) is a fundamental measure in order to improve the relations between foreign investors and the local business environment. Its main objectives are : increasing the investment volume in Romania; promoting investment opportunities; and offering professional services for foreign investors, all along the investment cycle (Vasilescu 2007).

Foreign and domestic investors are offered equal opportunities to invest in Romania. They obey the same national rules, have the same rights, and are granted the same legal and financial incentives. The main reason behind providing incentives to FDI is its capacity to "boost the economic development of the country, particularly the acceleration of industrialization in disfavored zones, as well as the development of small and medium-sized enterprises (SMEs), and micro enterprises" (Platis 2012). There is no limit to the foreign share in companies; foreign capital can take various forms, including foreign currency, equipment, services, rights of intellectual property, know-how and management expertise, and the proceeds and profits resulting from other businesses in Romania.

Romania's general legal framework concerning investment, both foreign and domestic, was adopted by means of Government Emergency Ordinance no. 85/2008 (the so-called "GEO"), subsequently amended and completed, which abrogated almost entirely Law 332/2001, previously regulating investment. The new law aims at creating a suitable and transparent framework for the promotion of investments (the Romanian Digest 2008).

GEO 85/2008 provides supporting measures for investment promotion, oriented through priority fields, that are, according to governmental policies : development and regional cohesion; protection and rehabilitation of environment; increase of energy

efficiency and/or production and use of renewable energy; research, development, and innovation; employment and training of labor force; development of fields of activities, which are priorities, according to governmental social-economic policies (Government of Romania, National Reform Program – Implementation Report 2008).

According to provisions in the GEO, incentives for investment are available under the form of grants conferred for tangible and/or intangible assets acquisitions; financial support from the state budget for newly created jobs; interest bonuses for credit contracting, and other incentives regulated by special laws. The Romanian government provided large amounts of state aid, which can be granted to large, small and medium-sized enterprises (including microenterprises), depending on the type of investment, the field in which the investment is to be implemented, and the provisions of the state aid scheme applied for (website of the Embassy of Romania in India).

While Law 332/2001 referred only to direct investment having a "significant economic impact", the GEO enlarges its applicability, by eliminating the requirement to be "significant". The former threshold of US$ 1 million has been removed, thus allowing investment of any size to benefit from the law's provisions.

The main principles of Government Emergency Ordinance no. 85/2008 are presented in Article 2. They include : 1) The principle of equal treatment of all investors, in line with the relevant European Legislation and in contrast with Law 332/2001, which favored foreign investors over domestic ones. 2) The principle of transparency, requiring that the grant of incentives should be easily available to all interested parties. 3) The principle of the efficient use of incentives, meaning that, in granting the incentives, the authorities have to apply certain criteria for granting them and follow their implementation. 4) The principle of confidentiality, requiring the protection of intellectual property rights of investors which are granted incentives and of all data that could jeopardize their interests (the Romanian Digest 2008). 5) The principle of eligibility of the source of funds for financing.

Other general principles of investment rules include : freedom of decision for the investment forms and methods; possibility to invest in any sector and under any juridical form provided by law; guarantees against ownership appropriation by the state,

expropriation or other similar measures; right to be assisted in filing administrative formalities; the right to own fixed and current assets (land can be owned by EU nationals and entities, as well as stateless persons domiciled in any EU state, provided they reside in Romania); the right to elect the competent court or arbitration authorities to settle potential investment-related disputes (Pirciog 2004).

The first step for a foreign company setting up a business in Romania is to choose a form of company, as provided by Romanian legislation. A study released by Ernst & Young provides detailed information about the forms of companies chosen by foreign investors. The most frequently used are : A) Limited liability company (Romanian : Societati cu Raspundere Limitata - SRL), having the status of a separate and distinct legal entity and where the shareholder's liability is limited to the amount subscribed as participation to the company's shared capital. B) Joint-stock company (Romanian : Societati pa Actiuni - SA), where ownership interests are represented by shares of stock and the shareholder's liability is limited to the amount subscribed in the company's share capital. C) Representative office, usually set up by foreign companies in Romania in order to carry out non-commercial activities, such as advertising and market research on behalf of the parent company. D) Branch of foreign company, which does not have its own legal personality or share capital. E) Consortium, such as a joint venture agreement. F) Societas Europaea (SE), which may be created on registration in any of the EU member states in accordance with the EC Regulation 2157/2001.

The most popular form of enterprise among local and foreign investors is the limited liability company, because it has fewer administrative requirements, greater flexibility in operations and low initial capital requirement, compared to other types of companies. At the same time, the number of joint-stock companies in Romania is increasing, thanks to their attractiveness to investors interested in equity investment. All other forms of business are not very common among foreign investors in Romania (Romanian Ministry of Foreign Affairs). Procedures for setting up trading companies are regulated by Law 31/1990 (the Romanian Companies Law), as amended and republished.

After having established a Romanian legal entity, "foreign investors may, during the course of business, restructure their activities through mergers and acquisitions as

stipulated by Romanian law" (Platis 2012). Mergers are regulated by the Romanian Companies Law, and the methodological norms approved under Order 1376/2004. The law regulates both mergers by absorption, and mergers by fusion, as well as spin-offs. Government Emergency Ordinance 52/2008, which amends the Romanian Companies Law, regulates both cross border mergers and Societas Europaea. The cross border merger procedure does not show major differences from the procedure concerning local mergers.

Acquisitions in any type of company are also regulated by the Romanian Companies Law. Acquisition procedures are different in case of limited liability companies or joint-stock companies, because, differently from shares in a joint-stock company, those in a SRL are not freely transferable to third parties. "Mergers and acquisitions involving at least one public company must be done in accordance with Capital Market Law 297/2004 and by observing the regulations issued by the National Securities and Exchange Commission (CNVM) (Platis 2012).

Law 346/2004 regulates incentives for those investors who want to set up or run small and medium-sized enterprises. An SME is defined by Romanian legislation as a company that has an annual average number of employees below 250 and whose net annual turnover does not exceed EUR 50 million, or whose total asset value does not exceed EUR 43 million. Financing incentives to SMEs include state assistance and loans guaranteed by the state.

In January 2011, the microenterprises taxation regime was reintroduced by the Fiscal Code. It can be applied by those companies fulfilling the following criteria, as presented by Platis for Ernest & Young (2012) : A) not to perform activities in the field of banking, insurance and reinsurance, capital markets (except for intermediation companies of these fields), gambling, consulting, and management; B) not to have their share capital owned by a shareholder or associate-legal entity with more than 250 employees; C) to have at least one employee, but not more than nine; D) to register an annual income less than the RON equivalent of EUR 100,000; E) share capital owned by natural or legal persons other than the state and local authorities. According to this

taxation regime, microenterprises are required to pay 3 per cent tax on income from any source, except certain categories.

According to Law 20/1999 on the approval of the Government Emergency Ordinance 24/1998 on the regime of deprived country zones, investment made in these areas can benefit from specific incentives, such as several exemptions on customs and profit, incentives for exports, and financing of special programs and investment projects. Disadvantaged or deprived zones are determined as such by government decision for a period of at least three years, but not more than ten, with the possibility of extension. Today most of these areas have ceased to be valid. There remain three disfavored zones in the mining areas of the country, in accordance with Annex 4A to the National Rural Development Program 2007-2013.

Industrial parks are regulated by Government Ordinance 65/2001, as further amended. According to the Ordinance, an industrial park is “delimited areas where commercial activities, scientific research, industrial production and services, use of scientific research and/or technological development are carried out within a regime of specific facilities, with the purpose of best using the area’s potential”.

The founder of an industrial park is granted free choice for the duration of investment, although it cannot be less than fifteen years. The so-called administrator-company, a Romanian legal entity, administrates the industrial park. No shareholder company using facilities and/or infrastructure of the industrial park can hold direct or indirect control over the administrator-company. The setting-up and development of industrial parks are granted the following incentives : exemption from taxes due on the conversion of agricultural land into industrial parks; buildings, constructions, and land located inside industrial parks are exempt from local property tax; other incentives granted in compliance with the local administrative law.

Free trade zones are administered by Law 84/1992, as further amended. These areas are regulated by a specific custom regime, under which the custom supervision is limited to the borders of such areas. Means of transport, products and other goods are admitted into free trade zones, regardless of their country of origin or destination.

However, the import of goods prohibited by domestic law or by international agreements to which Romania is a party, is forbidden.

Specific laws regulate mining and oil extraction activities in Romania. In fact, the country is rich in mineral resources, most of all oil, gas, salt gold and silver ore, and non-ferrous metals. New mineral deposits have been discovered by recent geological and geophysical studies, with considerable potential for exploitation and thus, investment (Platis 2012).

Mining activities are regulated by Mining Law 85/2003, as further amended. Its defined scope is to ensure maximum transparency and fair competition in mining activities, without discrimination between operators, depending on the property type and the origin of the capital. Subterranean and aboveground mineral resources located in Romanian territory are exclusive public property of the state. Private operators can be granted a mining license by the National Agency for Mineral Resources for a maximum period of twenty years, with the possibility to extend it for other five years. Foreign investors need to set up a permanent subsidiary in Romania within ninety days of obtaining the mining license.

All operations involving oil and gas in Romanian were regulated by Petroleum Law 134/1995, abolished and replaced by Law 238/2004, as further amended by Government Emergency Ordinance and approved by Law 262/2009. Oil resources in Romanian territory are part of the state's public property. The National Agency for Mineral Resources can grant a Romanian or foreign legal entity an oil concession to perform oil operations. The concession cannot exceed thirty years duration, with the right to extend it for other fifteen years and it can be applied as exploitation license or exploration permit. Foreign operators should create a permanent establishment in Romania within ninety days of obtaining the oil and gas license. However, Law 238/2004 does not grant any incentives to the holders of an oil license.

CHAPTER 4

TRENDS AND PATTERNS OF TURKISH FDI IN ROMANIA

4.1 – Introduction to the chapter

Starting from 1990, Romania opened its doors to foreign capital, yet through a slower process compared to its neighboring transition countries, as we explained in the previous chapter. Indeed, the early transition entrepreneurial environment was dominated by large state-owned, government-subsidized firms, heavily discouraging investments from abroad. However, after a few years the government realized the importance of FDI for the development of the Romanian economy and started to improve the business environment (DEIK 2005). Following widespread trends, Turkish entrepreneurs exploited this opportunity and started to enter the Romanian market in a consistent way.

In line with the Turkish firms' tendency to expand into neighboring countries, Romania became one of the most attracting countries for Turkish outward FDI. Indeed, among the EU countries, it ranks sixth by the 2012 FDI stock, second compared to South East European countries (Bosnia and Herzegovina being the first), and first in Central and Eastern Europe. With a total amount of 2.9 billion euro in mid-2012, trade relations are also well developed.

Turkish enterprises are active in several sectors of the Romanian economy, ranging from real-estate to breeding, but they are mainly concentrated on service and manufacturing activities. The Turkish business community in Romania is well integrated and dynamic, yet the same cannot be said about Romanian entrepreneurs in Turkey. Although different historic paths created distinct economic environments and structures, these two countries share common characteristics and are tied by strong links at several levels.

The main concern of the upcoming chapter is to introduce the economic relationship between Romania and Turkey, by focusing in particular on the investments flowing from the latter to the former.

4.2 – Turkey and Romania : a consolidated economic relation

Turkey and Romania share good diplomatic and economic ties since a long time. During the last few years the diplomatic relationship has been intense, with several visits between the Turkish President, Prime Minister, Minister of Foreign Affairs, and the Romanian President and Minister of Foreign Affairs. In particular, in December 2011, representatives of both countries signed the Strategic Partnership Declaration, which aims at "enhancing bilateral relations in every field, particularly in the political and economic domains" (Turkish Ministry of Foreign Affairs). After less than two years, the two countries signed off on an action plan to enhance strategic cooperation in numerous fields of activity at the bilateral, regional, and international level in March 2013. This "broad-based action plan" aims at integrating the strategic partnership agreement with concrete proposals on politics, economy, security, the environment and more (Tokyay and Ciocoiu 2013).

Besides their bilateral relationship, Romania and Turkey cooperate in different regional and international institutions and work together to strengthen stability and security in their neighborhood and regional environment. Indeed, they are part of various regional economic, political, and security organizations, such as : the Stability Pact for Southeastern Europe, the South East European Cooperation Process (SEECP), the South East European Cooperative Initiative, the Black Sea Naval Cooperation Task Group (BLACKSEAFOR), and the Black Sea Economic Cooperation (BSEC).

At the international level, they are both members of the Organization for Security and Cooperation in Europe (OSCE) since its establishment, and have been involved in dialogue and cooperation before and after the Cold War. Romania is a strong supporter of Turkey's adhesion to the EU, while Turkey historically supports Romania's entry to NATO. The current security partnership is based on the construction of anti-missile defense shields in both countries. Turkey is already hosting an early warning radar system near Malatya under NATO's Smart Defense Initiative and Ballistic Missile defense system, and "officials affirm that anti-ballistic missiles interceptors are planned to be placed in Romania by 2018" (Tokyay and Ciocoiu 2013).

Due to their shared past, the two countries are united by historical and cultural ties as well. Indeed, as vassal states, the ancient Romanian provinces of Transylvania, Moldavia and Walachia had long been in a tight relationship with the Ottoman Empire. Moldavia and Walachia in particular lived under Ottoman suzerainty from the 16th to the 19th century. Under this kind of relation, the vassal states could enjoy some internal autonomy, in exchange of conspicuous tributes paid to the Empire. As a result, today Turkish traces can be found in several areas of the Romanian society and culture, ranging from the language to the cuisine, and from architecture to tourism.

Moreover, Romania historically hosts the Turkish community of the so-called Romanian Turks. Coherent data about the dimension of the community are not available, because, depending on the source, the figure ranges from around 28,000 people (2011 official census) to around 80,000 (Constantin *et al.* 2010). These Turks are all of Muslim religion, but they are not an homogenous group. On the one hand, we find the historical community which settled in the country, in particular in the Dobrogea region, during the XIII century, and is perfectly integrated into the Romanian society. It is composed by two minorities, the Tatars and the Turkish, both organized in specific ethnic and cultural organizations, and represented in Parliament by their own political party. On the other hand, the other part of the group is composed by those Turkish immigrants who started to enter Romania since 1990, and which created a new distinguished community. "Mainly attracted by the already existing Turkish community, geographical proximity, and the new business opportunities, a number of them engaged in entrepreneurial activities" (Constantin *et al.* 2010).

From an economic perspective, the relation between the two countries is constantly increasing over time, with high levels of bilateral trade and investment. Indeed, Romania is one of the strongest economic and commercial partners of Turkey in the South Eastern European region, and Turkey is Romania's number one trading partner among non-EU countries. However, this is mainly a one-way relationship, as the Turkish economic presence in Romania is much more significant than the opposite one (Phinnemore 2006). In fact, by 2013, about 13,000 companies with Turkish shares were registered in Romania, employing more than 150,000 people, and with a total stock of investment amounting at nearly 1 billion euro, Fatih Karamancı, head of the Turkish-

Romanian Business Council at the Foreign Economic Relations Board, declares to Southeast European Times (Tokyay and Ciocoiu 2013).

Phinnemore (2006) attributes the success of bilateral economic relations between Turkey and Romania to three main factors : 1- geographical proximity, excellent political relations, and bilateral cooperation; 2- the fact that Turkish entrepreneurs wishing to invest abroad are attracted by stability and predictability, fostered by progress towards adopting the *acquis communautaire*; 3- the numerous economic agreements encouraging trade and investment.

Indeed, since 1989, a Double Tax Treaty signed in 1986 is in force between Turkey and Romania, with the dual purpose of avoiding double taxation on the movement of capital and other factors, and preventing tax evasion. On the other hand, the Free Trade Agreement in force since 1998 was terminated in 2007, when Romania entered the EU and became part of the Customs Union. A first agreement between the two governments on the reciprocal promotion and protection of investments was signed in 1991 and enforced in 1996. However, it has been replaced by the new Bilateral Investment Treaty signed in 2008 and ratified in 2010.

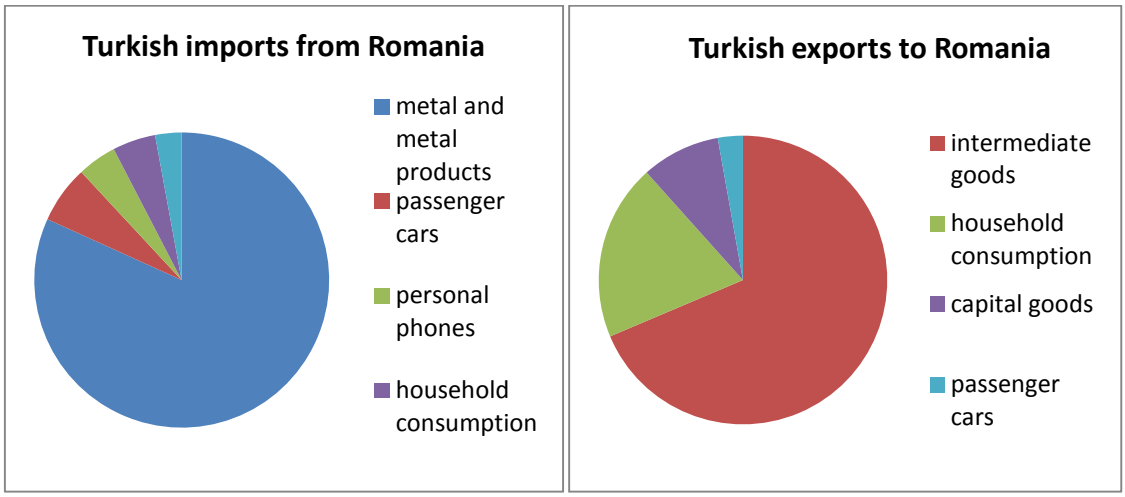
The economic relations between Romania and Turkey are bolstered by private sector organizations as well. Indeed, the Turkish Industrialists' and Businessmen's Association (in Turkish : *Türk Sanayicileri ve İşadamları Derneği*, TÜSİAD), the Union of Chambers and Commodity Exchanges in Turkey (in Turkish : *Türkiye Odalar ve Borsalar Birliği*, TOBB), the Turkish Businessmen's Association in Romania (in Turkish : *Türk İş Adamları Derneği,* TİAD), and the Turkish-Romanian Chamber of Commerce founded in Bucharest in 1995, are playing an active role in facilitating the bilateral relationship at several levels.

Trade relations between Turkey and Romania are good and rise over time. Since 1990, Romania reported a surplus in its trade with Turkey, and exports growth rate has been much faster than imports. Indeed, data released by the Turkish Statistical Institute reveal that total Turkish exports to Romania in 2012 amounted to 2.495.427.000 dollars, while imports amounted to 3.236.425.000 dollars.

By 2011, Turkey's imports from Romania mainly consisted of intermediate goods, in particular metals and metal products, which accounted for 81.6 percent of total imports. There followed end-use goods with a percentage of 10.7 percent, comprising passenger cars (6.3 percent), personal phones (4.3 percent), and packed medicines (0.1 percent). Then we find household consumption (4.7 percent) and capital goods (2.9 percent). Concerning exports, the main industry is again intermediate goods (68.5 percent), followed by household consumption (19.7 percent), capital goods (8.8 percent), and finally end-use goods, in particular passenger cars (2.8 percent) and packed medicines (0.1 percent).

Figures 21 and 22. Turkish-Romanian trade by main products, 2011

(percent)



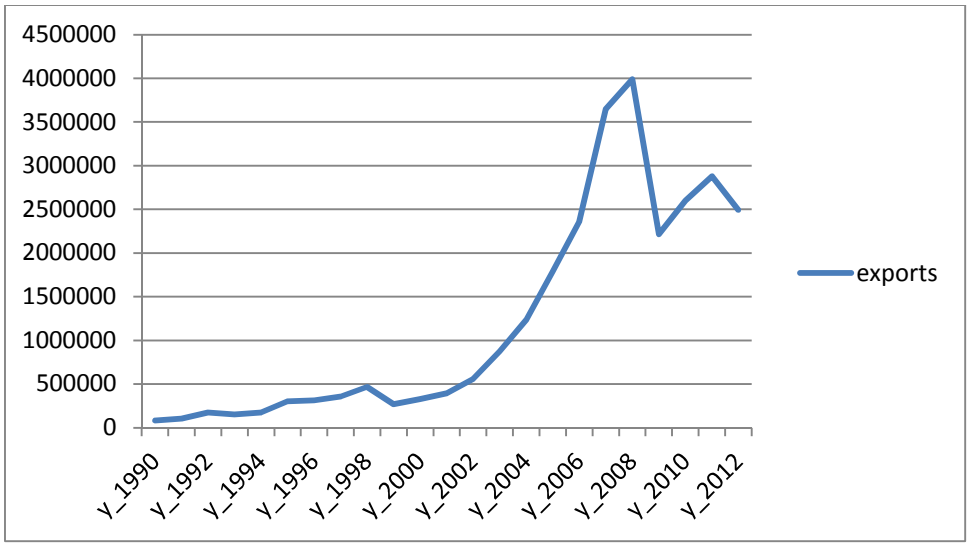
Source : OECD statistics

According to data presented by TİAD, Turkey absorbed in 2010 almost 25 percent of Romanian exports outside the EU, and was the source of around 13 percent of Romania's imports from outside the EU. The main domains of cooperation highlighted by TİAD were : energy, tourism, transportation, industry, and software (Cojocaru 2010). The 2008 global economic crisis heavily impacted trade relations between Turkey and Romania as well. Indeed, bilateral trade dropped by nearly 40 percent in 2009, compared to 2008. We see in the graph how exports slightly recovered in 2010, but follow a fluctuating trend since then. Imports recovered a little more, but did not

find stability either. However, the evaluation made by the National Bank of Turkey about the first half of 2013 reveals an encouraging upward trend.

Figure 23 and table 13. Turkish exports to Romania 1990-2012

(US$ thousands)

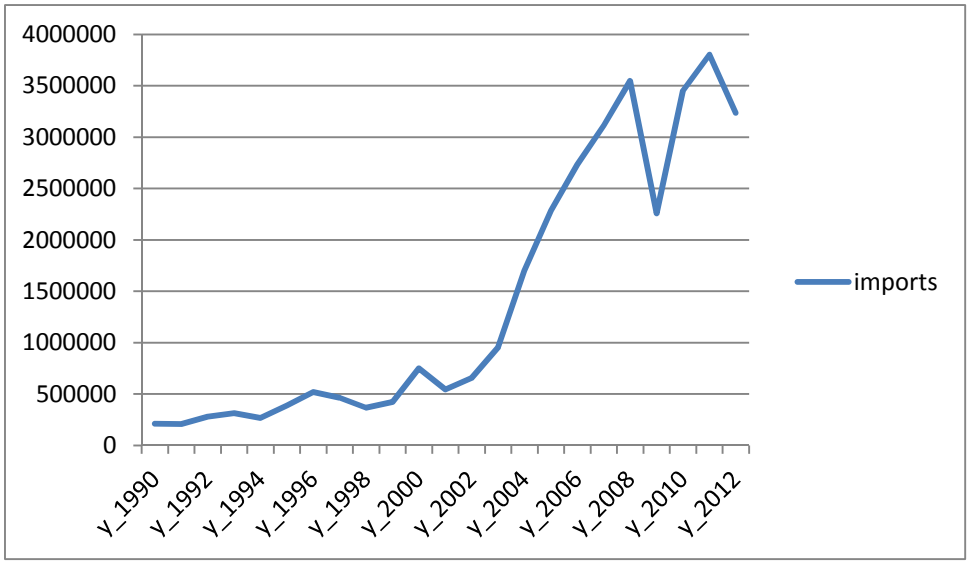


year	exports	year	exports
1990	83.165	**2002**	560.431
1991	105.158	**2003**	873.347
1992	173.168	**2004**	1.235.165
1993	151.653	**2995**	1.785.409
1994	175.449	**2006**	2.358.558
1995	302.062	**2007**	3.646.925
1996	314.127	**2008**	3.987.344
1997	358.826	**2009**	2.215.162
1998	468.343	**2010**	2.599.020
1999	268.293	**2011**	2.878.840
2000	326.718	**2012**	2.495.427
2001	392.417		

Source : OECD statistics and National Bank of Turkey

Figure 24 and table 14. Turkish imports from Romania 1990-2012

(US$ thousands)



year	imports	year	imports
1990	210.424	**2002**	656.561
1991	206.668	**2003**	955.971
1992	278.172	**2004**	1.699.436
1993	313.473	**2005**	2.285.592
1994	267.709	**2006**	2.729.366
1995	390.130	**2007**	3.113.783
1996	520.294	**2008**	3.547.820
1997	462.181	**2009**	2.258.183
1998	366.746	**2010**	3.449.179
1999	423.168	**2011**	3.801.245
2000	748.675	**2012**	3.236.425
2001	544.431		

Source : OECD statistics and National Bank of Turkey

From 1989 onward, also small retailers have benefited from the increasing relationship between Turkey and Romania. The Istanbul Gran Bazaar became an important base for Romanian merchants who, due to the economic difficulties they were experiencing at home, started to import cheap products, mostly clothing, to Romania.

Corruption at the customs helped them to introduce the Turkish goods to their country, and falsification of brands to keep prices low. This commercial pattern has been maintained until recent years, and clothes *Made in Turkey* still have relevance in the Romanian market (Iordache 2005).

4.3 – Turkish enterprises in Romania : a significant presence

As we mentioned before, Turkish economic presence in Romania is highly based on FDI. But this is not a Romanian prerogative. Indeed, Turkey has been very active at the investment level in all transition economies, because of different reasons. Both in the area of South East Europe and CIS countries attract high Turkish FDI flows mainly because of historical and cultural ties, while Central and Eastern Europe economies are important for their large markets and their proximity to Europe. In fact, market access and productivity are two of the primary motives behind Turkish firms' FDI in this area.

Concerning entry modes of Turkish firms into CEE and CIS countries, Trifonova and Marinov (2003) highlight the main strategies they pursued at the beginning of the 2000s. According to them, Turkish enterprises generally preferred to establish wholly-owned subsidiaries in the host market, but occasionally opted for joint ventures and consortiums with Western groups. They relied heavily on internal resources (such as technology) to control supplies and conditions of sale of inputs. At the same time, they established very good relationships with host governments, in order to avoid "broken contracts and ensuing litigation".

Turkish FDI in the region have been sustained both by home country conditions and location specific advantages. Concerning the internal economic conditions of Turkey, the main determinants have been the radical liberalization of the foreign exchange regulations, the economic slowdown that the country experienced throughout the 1990s and in the early 2000s, and the Customs Union with the EU. On the other hand, location specific advantages include economic liberalization in transition countries, and the emerging consumer demand for quality goods and services (besides all other factors attracting FDI we mentioned in the previous chapter) (Trifonova and Marinov 2003).

Among CEE countries, Romania is the one attracting the highest amount of investment by Turkish enterprises. Collecting coherent data about Turkish investment in Romania can present difficulties, because figures are released by different sources, which use diverse criteria to collect them. Indeed, besides usual obstacles of dealing with emerging or transition economies' institutions and economic reports (lack of cooperation between institutions, large portions of unofficial economy and so on), Romanian and Turkish dedicated agencies do not always release complete and coherent data sets. For instance, we presume that, when reporting about the number of Turkish companies operating in the Romanian market, certain sources, such as the National Trade Register Office of Romania and the Turkish-Romanian Business Council at the Foreign Economic Relations Board, report as "Companies by Turkish foreign investment" the ensemble of enterprises with Turkish shares, regardless of the magnitude of these shares. On the other hand, the Turkish Undersecretariat of Treasury, the institution dedicated to Turkish outward FDI data release, indicates as "Turkish enterprises abroad", only those firms with Turkish majority shares.

In any case, mostly since 1990, many enterprises with Turkish shares operate in the Romanian market, and it is arguable that Turkey ranks among the first countries by number of firms. Official Turkish data (Undersecretariat of Treasury) report that 274 branches of Turkish firms were operating in Romania by 2012. This figure increased by 76.76% compared to 2000, when 99 Turkish activities were registered. The total capital stock corresponding to these firms amounted to 219,601,673 US$ by 2012, with a disinvestment of 26% compared to 2011.

On the other hand, the Romanian National Trade Register Office registered 12.726 enterprises with Turkish capital in July 2013, thus positioning Turkey at the third place among investing countries by number of firms. By recorded subscribed capital Turkey ranks 16th with 619,433.7 US$ thousands (figure confirmed by the Romania National Bank, see chap. 3).

Table 15. Classification of investing country by number of companies, July 2013

country	companies by foreign investment	
	number	%
total Romania	189.912	100
1. Italy	35.976	19,23
2. Germany	19.904	10,64
3. Turkey	13.256	7,08
4. Hungary	12.099	6,47
5. China	10.797	5,77
6. France	7.450	3,98
7. USA	6.672	3,57
8. Austria	6.588	3,52
9. Israel	6.524	3,49
10. Iraq	5.819	3,11

Source : National Trade Register Office of Romania

The first economic activities were run by those Turkish entrepreneurs migrating to Romania soon after 1990. Encouraged by a favorable legal and institutional environment for the business sector, they arrived with modest capital and started small ventures, like bakeries and textile boutiques, "mainly financed by informal sources, such as personal savings, loans from family and friends, and home equity loans" (Constantin *et al.* 2010). A few years later, their success attracted a second, more consistent wave of Turkish businessmen, who were highly motivated and had better experience in running business. Involved in a large variety of economic sectors, this second group contributed to improve the business environment of the Turkish in Romania in a significant way. They founded activities in all regions of the country, yet the highest concentration was registered in Bucharest.

Other entrepreneurs of Turkish nationality did not arrive from Turkey, but rather from the EU, in particular those countries with a high Turkish presence, such as Germany, the Netherlands, and Luxembourg. Having "high financial potential and important

managerial experience", but also capital availability, they join already settled businesses, usually for important projects, such as the establishment or purchase of major companies (Constantin *et al.* 2010). Because of its internal unity and its integration with the local environment, the community of Turkish businessmen in Romania is considered under the umbrella of ethnic entrepreneurship.

After its adhesion to the EU, Romania attracted even more investment from Turkish entrepreneurs, who began to expand their business in almost every sector of the economy. In fact, now Romania can access European funds, which become available to foreign businesses operating there. As a result, today Romania is one of the most preferred destinations of Turkish investment in the EU, and the main one in the region. Referring to data released by the Turkish Undersecretariat of Treasury, among CEE and SEE countries, Romania ranked first as to FDI stock in 2011, while it has been surpassed by Bosnia and Herzegovina in 2012. As to number of companies, it still is the main recipient.

Table 16. Turkish OFDI stock by country and year (US$)

country	2008	2009	2010	2011	2012	% on GDP
Romania	16.558.262	381.000.150	372.997.759	297.420.125	219.601.673	0,12%
Albania	5.858.455	137.152.237	149.477.969	20.727.621	11.637.112	0,09%
Bosnia and Herzegovina	3.286.039	191.565.183	250.740.839	263.408.391	233.600.977	1,40%
Bulgaria	8.207.264	137.490.310	105.289.987	87.100.696	89.568.358	0,17%
Croatia	/	89.033	10.416.937	8.713.704	22.142.745	0,04%
Czech Rep.	/	0	0	310.536	26.400	0,00%
Montenegro	7.952.609	15.802.316	18.657.222	20.173.507	22.271.938	0,51%
Kosovo	8.867.450	82.394.624	62.270.031	33.900.639	104.384.267	1,67%
Hungary	262.244	28.623.005	21.248.552	19.898.676	26.663.771	0,02%
Macedonia	340.001	25.012.012	32.973.310	131.107.818	126.112.796	1,34%
Moldova	29.000	628.229	5.535.606	15.367.104	11.607.610	0,15%
Poland	/	108.551	21.944.698	24.526.762	20.765.186	0,00%
Serbia	0	327.774	2.276	2.164	1.569.629	0,00%
Slovakia	/	6.838.591	7.611.021	8.560.963	9.239.604	0,01%
Slovenia	576.922	0	301.436	790.750	332.494	0,00%

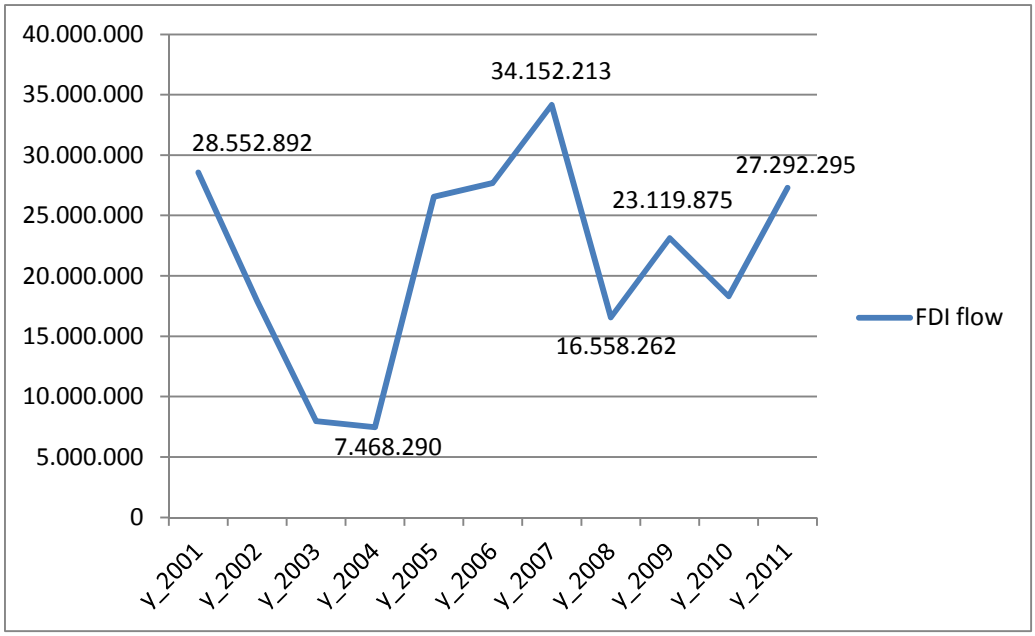
Source : Turkish Undersecretariat of Treasury and UNCTAD for GDP

The trend of Turkish investments to Romania shown in figure n. 25 reflects the economic phases that Turkey went through during recent years. Before 2001, the amount of capital flowing to the European country was significant, compared to other countries of the area. Indeed, the total FDI stock to Romania amounted to 62,294,479 US$ in 2000, while that to Bulgaria, the second most important recipient at the time, amounted to 41,248,125 US$. Other important FDI destinations, such as Bosnia and Herzegovina and Macedonia recorded less significant figures (US$ 15,327,223 and 13,209,824 respectively), because their economies were highly unstable and non attractive for foreign investors.

The Turkish economic crisis of 2000-2001 caused a severe breakdown of FDI outflows, not only to Romania, but to all recipient countries of Turkish foreign direct investment. The annual flows fell by around 74 percent in three years, reaching the negative record of 7,468,290 US$ in 2004. Nevertheless, they recovered very rapidly, and in other three years they attained the positive peak of 34,152,213 US$, which is still to be overtaken. Indeed, the 2008 global financial and economic crisis provoked another slowdown in Turkish outflows, yet not as violent as the 2001 one. FDI flows to Romania fell by 52 percent in 2008, and later took a recovery path, which, despite being not linear, appears encouraging (data from Turkish Undersecretariat of Treasury).

Figure 25. Turkish FDI flows to Romania, 2000-2011

(US$)



Source : Turkish Undersecretariat of Treasury

Turkish companies are deeply integrated into the Romanian economy, thus contributing to the development of the country and benefiting from its dynamic market at the same time. They sell their products to Romanians and also hire local workers. "Experienced immigrant entrepreneurs also provided role models for the local population where they settled their businesses" (Constantin *et al.* 2010). Moreover, the integration of Turkish businessmen in civil society in made smooth by complex networks of several professional associations, and ethnic and religion-based organizations with strong connections at the national and international levels.

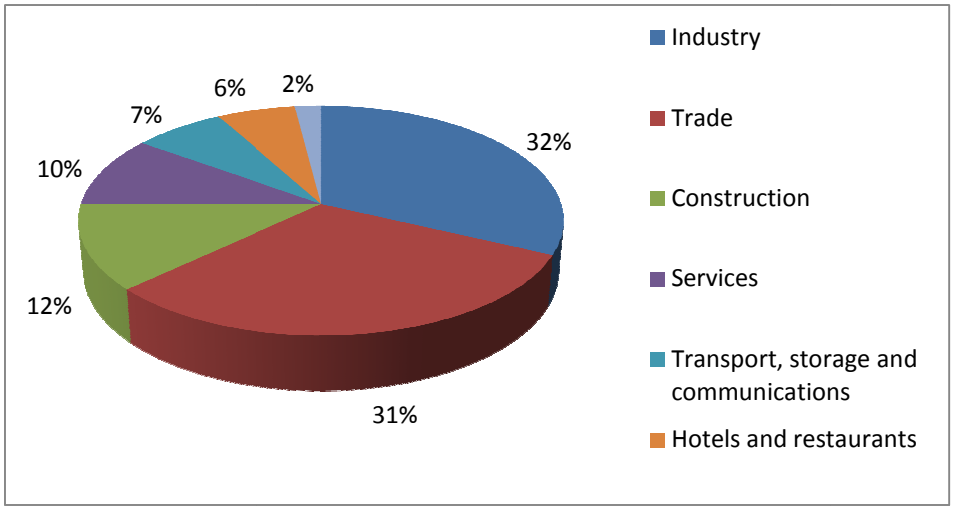
The Turkish Businessmen Association (TİAD) is very active in supporting the economic activities of its members. Founded in 1993, today it has around 130 members, covering almost all industrial sectors. In order to support social, religious, and cultural projects involving the whole Turkish community in Romania, TİAD established an intense cooperation with the two leading minority organizations, namely the Democratic Union of Turkish-Muslim Tartars in Romania, and the Turks' Democratic Union in Romania.

The Romanian industry sectors involved in FDI have been changing over time. At the beginning, the concentration was on small food business, like bakeries and restaurants, import and distribution. Then, thanks to the completion of the legal and regulatory framework at the intergovernmental level, larger companies started to invest, and production moved towards industry and trade, in particular to real-estate, construction equipment, the automotive industry, home appliances, the textile, and food and beverages (DEİK 2005). In more recent years, new industry sectors gained importance : the banking, insurance services, and residential and hotel sectors among the others (Turkish Ministry of Economy).

The chart below illustrates the division into the main economic sectors of Turkish entrepreneurs' activities by 2007. It has been proposed by Constantin *et al.* (2010) on the base of TİAD's "Romania. Businessmen and Investors Guide, 2007-2008" (Bucharest: TIAD-YAYINIDIR, 2007), pp.190-202. According to the figure, industry and trade (wholesale and retail sale of food and non-food production) accounted for the bulk of the investments, with almost one third of the total amount each. They were followed by the construction sector and services, in particular real estate investment and transactions, banking, and business consultancy.

Figure 26. Sectoral distribution of Turkish capital in Romania, 2007

(percent)



Source : Constantin *et al.* 2010

Concerning the banking sector, two Turkish banks are active in Romania today : Garanti Bank and Credit Europe bank. The sector is in good health today and accounts for the largest part of total investments, when concerning the capital invested. However, it has not always been so. Indeed, the deep financial crisis impacting Turkey in 2000 had heavy consequences in Romania as well. The image of Turkish banks were severely damaged, and the Banca Turco Romana, owned by Bayındır Holding was closed by the National Bank of Romania in 2002. Eventually, the performance of Turkish economy improved, and so did the banking sector.

The table below lists the enterprises operating in Romania with Turkish capital and it is taken from the data sets released by the Office of the Commercial Counsellor at the Turkish Embassy in Bucharest. Clear indications about company information are not released; therefore, we presume that they take into account all enterprises with Turkish shares operating in the Romanian territory. Moreover, a precise definition of “capital of Turkish companies” is not given; therefore, on the base of data comparisons with other sources, we suppose it refers to the total capital owned by those firms, not only the one invested in Romania. We report here the first 50 investing firms out of the 799 companies taken as a sample by the Office.

Table 17. Top 50 Turkish investing societies in Romania by capital, 2011

rank	company	capital (EUR)	%	sector (NACE classification)
1	GARANTIBANK INTERNATIONAL N.V.	202.996.873	20,16	monetary intermediation
2	CREDIT EUROPE BANK SA	156.260.852	15,52	monetary intermediation
3	DOGAN MEDIA INTERNATIONAL SA	61.688.634	6,13	television programming and broadcasting activities
4	KASTAMONU ROMANIA SA / PROLEMN SA	54.614.937	5,42	sawmilling and planing of wood
5	D YAPI REAL ESTATE INVESTMENT AND CONSTRUCTION SA	53.084.830	5,27	development of building projects
6	AGRAFOOD SRL	31.827.016	3,16	raising of poultry
7	RULMENTI SA	23.215.552	2,31	manufacture of bearings, gears, gearing and driving elements
8	ERDEMIR ROMANIA SRL	18.867.410	1,87	manufacture of basic iron and steel and ferro-alloys
9	CREDIT EUROPE LEASING IFN SA	16.792.241	1,67	financial leasing
10	GIMROM HOLDING SA	16.532.028	1,64	retail sale in non-specialized stores with food, beverages, or tobacco predominating
11	BANVIT FOODS SRL	14.022.121	1,39	processing and preserving of poultry meat
12	ENKA CONSTRUCTION AND DEVELOPMENT BV AMSTERDAM SUCURSALA CLUJ	13.683.028	1,36	construction of road and motorways
13	DAMBOVITA CENTER SRL	13.596.741	1,35	development of building projects
14	AZOMURES SA	12.177.527	1,21	manufacture of fertilisers and nitrogen compounds
15	ARCTIC SA	11.120.927	1,10	manufacture of electric domestic appliances
16	DENTAS ROMANIA SRL	10.906.885	1,08	manufacture of articles of paper and paperboard
17	VICTORY REAL ESTATE DEVELOPMENT SRL	10.638.306	1,06	development of building projects
18	ADYA METAL SRL	8.927.943	0,89	manufacture of metal structures and parts of structures
19	UNYE CEM SRL	7.945.806	0,79	wholesale of wood, construction materials ans sanitary equipment
20	EUREX ALIMENTARE SA	7.556.080	0,75	manufacture of rusks and biscuits; manufacture of preserved pastry goods and cakes
21	DURAL SRL	6.774.588	0,67	copper production
22	CHIMPEX SA	6.521.165	0,65	cargo handling
23	PLUS DEVELOPMENT SRL	6.517.447	0,65	business and other management consultancy activities
24	SUPERLIT ROMANIA SA	6.389.333	0,63	manufacture of plastic plates, sheets, tubes and profiles
25	IROMET SRL	5.820.402	0,58	wholesale of waste and scrap

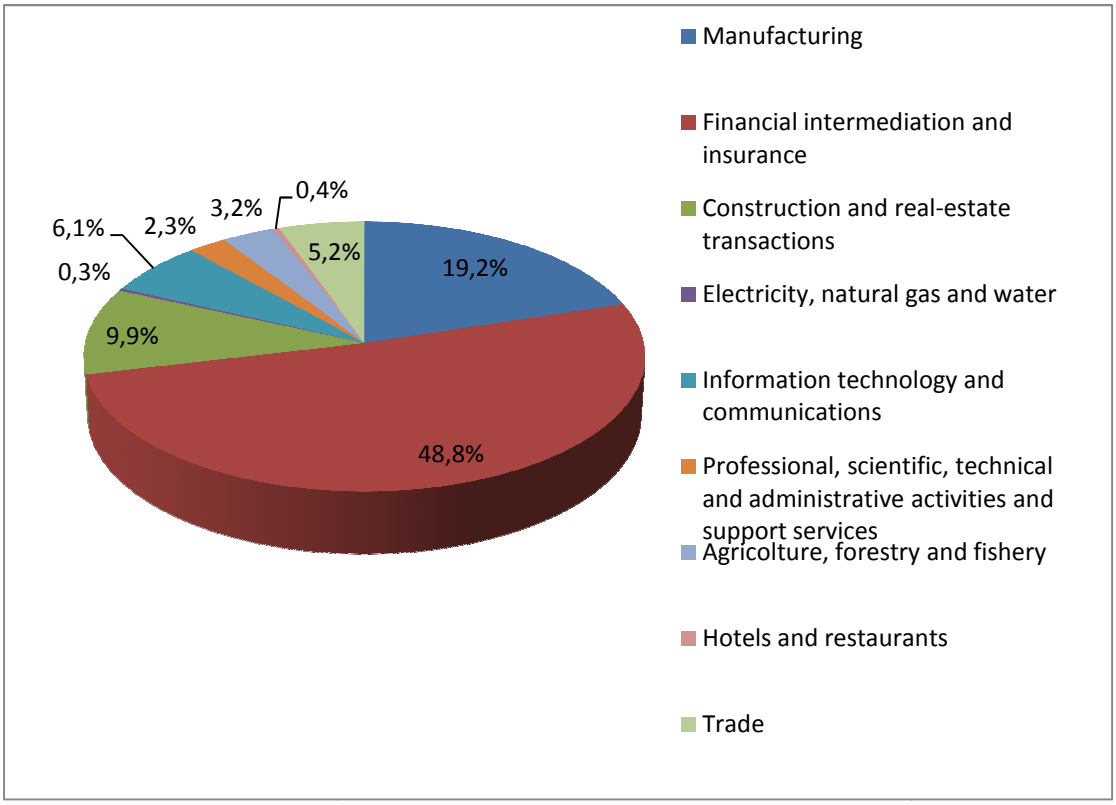
rank	company	capital (EUR)	%	sector (NACE classification)
26	ASAS SRL	4.945.436	0,49	printing (other than newspapers)
27	M.R. INVESTITII INDUSTRIALE SA	4.335.972	0,43	buying and selling of own real estate
28	KOTON SRL	4.131.884	0,41	agents involved in the sale of textiles, clothing, fur, footwear and leather goods
29	BH INVESTMENTS LAND DEVELOPMENT SRL	3.863.132	0,38	agents involved in the sale of timber and building materials
30	PRESTIGE MOB SRL	3.758.180	0,37	manufacture of furniture
31	SISTEM YAPI INSAAT VE TICARET A.S. ISTANBUL TURCIA	3.738.163	0,37	engineering activities and related technical consultancy
32	UNICOM OIL TERMINAL SA	3.718.060	0,37	cargo handling
33	MAJESTIC TOURISM SA	3.592.594	0,36	hotels and similar accommodation
34	ACCESS FINANCIAL SERVICES IFN SA	3.481.793	0,35	other financial service activities, except insurance and pension funding n.e.c.
35	CREDIT EUROPE IPOTECAR IFN SA	3.472.463	0,34	other credit granting
36	BIWATER INTERNATIONAL LIMITED REGATUL UNIT	3.222.048	0,32	construction of water projects
37	DYO BALKAN SRL	3.064.589	0,30	manufacture of paints, varnishes and similar coatings, printing ink and mastics
38	CREDIT EUROPE ASIGURARI REASIGURARI SA	3.048.432	0,30	non-life insurance
39	DSM NUTRITIONAL PRODUCTS ROMANIA SRL	2.870.801	0,29	manufacture of prepared feeds for farm animals
40	GOLD & PLATIN SRL	2.722.581	0,27	sale of cars and light motor vehicles
41	TEKZEN ROMANIA SRL	2.495.058	0,25	other retail sale of new goods in specialised stores
42	ROMPAK SRL	2.410.121	0,24	manufacture of other food products n.e.c.
43	INTER DOGA SRL	2.378.174	0,24	construction of residential and non-residential buildings
44	ASTROM UNITED SA	2.339.805	0,23	renting and operating of own or leased real estate
45	TEMA RETAIL RO SRL	2.318.566	0,23	retail sale via stalls and markets of textiles, clothing and footwear
46	ALIX AVIEN COSMETICS SRL	2.243.735	0,22	wholesale of perfume and cosmetics
47	PIM MUHENDISLIK SANAYI VE TICARET LIMITED SIRKETI	2.206.819	0,22	plumbing, heat and air-conditioning installation
48	COBAN IMPORT EXPORT SRL	2.074.012	0,21	agents involved in the sale of timber and building materials
49	MALVINA COM IMPEX SRL	2.042.966	0,20	manufacture of plastic packing goods
50	GOLD & PLATIN DANUBIUS SRL	2.038.248	0,20	sale of cars and light motor vehicles

Source: Turkish Embassy in Bucharest, Office of the Commercial Counsellor

Relying on the present list, we elaborated the following chart about the sectoral distribution of the top 50 enterprises. Due to the large capital owned by the two major Turkish banks with branches in Romania, the percentage of the financial sector amounts at nearly half of the total stock. There follows the manufacturing sector, to which belongs the majority of Turkish enterprises (17 out of 50), yet with a much smaller amount of capital. Then we find construction and real estate, another lucrative sector in the Romanian environment.

Figure 27. Sectoral breakdown of top 50 firms by capital, 2011

(percent)



Source : Turkish Embassy in Bucharest, Office of the Commercial Counsellor, processed by the author

Table 18. Geographical distribution of Turkish firms by county, 2011

county	companies	capital (EUR)	sales (EUR)
ALBA	4	764.150	3.798.606
ARAD	1	943.629	1.866.874
ARGES	18	4.872.007	40.478.008
BACAU	3	359.697	3.932.461
BIHOR	1	46	14.801.874
BISTRITA-NASAUD	3	414.560	26.943
BOTOŞANI	1	50.177	2.334.160
BRAILA	11	3.157.419	29.701.279
BRAŞOV	29	5.064.528	25.224.917
BUCURESTI	280	610.959.150	2.166.268.504
BUZAU	5	7.517.034	55.468.375
CALARAŞI	2	5.051.314	11.386.861
CARAŞ-SEVERIN	2	1.354	1.066.924
CLUJ	9	14.988.972	71.379.816
CONSTANTA	96	31.710.359	355.268.803
DIMBOVITA	11	42.567.243	339.707.135
DOLJ	4	563.829	9.961.969
GALATI	9	6.424.263	30.406.545
GIURGIU	12	3.614.394	32.731.621
GORJ	1	46.300	1.357.312
HARGHİTA	2	787.231	4.325.538
HUNEDOARA	3	1.236.484	1.989.779
IALOMITA	5	1.378.377	26.904.424
IAŞI	17	11.819.584	54.486.381
ILFOV	190	121.533.726	805.099.006
MARAMUREŞ	1	1.332.816	3.777.873
MEHEDINTI	1	46	104.530
MUREŞ	8	67.296.744	444.778.541
NEAMT	2	1.267.655	732.887
OLT	11	890.241	25.624.769
OLTENITA	1	3.064.589	1.070.034
PRAHOVA	25	21.939.178	56.693.146
SIBIU	5	267.852	9.273.929
SUCEAVA	5	4.139.271	4.224.003
TELEORMAN	2	869.227	228.787
TIMIŞ	8	450.591	9.844.946
TULCEA	2	5.877.800	160.637
VALCEA	3	666.528	3.104.839
VASLUI	2	23215598	60.778.046
VRANCEA	4	155.922	3.963.890
Totale	**799**	**1.006.759.884**	**4.714.334.972**

Source : Turkish Embassy in Bucharest, Office of the Commercial Counsellor

Table n. 18 shows the geographical distribution of all 799 firms considered by the survey of Office of the Commercial Counsellor in the Romanian counties. The geographical distribution of Turkish businesses has changed over time. Indeed, after the initial concentration in the Dobrogea region, which still hosts several Turkish businesses mainly in its county of Constanta, more developed industrial activities started to be built in the area of Bucharest and the surrounding Ilfov department, the major industrial area of the country. Later on, they spread all over the country, though with less dense concentration.

CONCLUSIONS

Principal objective of this study was to analyze the expansion of Turkish firms abroad, in particular to Romania. It was our interest to investigate how, if so, the recent political change of orientation of the Turkish government was reflected on the economic sphere. Given the growing success of Turkish businesses both at home and abroad, we tried to analyze their behavior and strategies in the penetration of foreign markets, in particular those transition economies that are increasingly becoming attractive hosts of FDI.

Turkish MNCs are studied in the context of emerging economies' multinational companies (EMNCs), a branch of the enterprise studies that still has to be analyzed with in-depth theories. In this work we tried to present this topic, by referring especially to EMNCs' motivations to invest, their entry modes and destination choices. The leading emerging sources of FDI today are China, Russia, and Taiwan. However, other economies, including Brazil, Malaysia, Mexico, South Korea, India, and Turkey are also becoming "important players in outward FDI" (Demirbağ *et al.* 2010).

Similarly to other emerging markets' MNCs, Turkish companies usually prefer to start their businesses in closer countries, both physically and psychologically. Indeed, the former Soviet Turkic Republic of Central Asia, the Middle East, and South and Eastern European countries are the most favored destinations for initial FDI flows. In a second moment, large firms move their activities further, especially to Europe, where they adopt aggressive strategies, mainly through mergers and acquisitions. This is clearly not a universal pattern, and large well-established groups often start their internationalization directly in Europe, which remains the most attractive region for Turkish MNCs.

The historical analysis of the economic performances of Turkey and Romania have been useful to understand the background on which they operate as national states and which creates opportunities or obstacles to the enterprises operating there.

The economic history of the Republic of Turkey has been very turbulent. A new political and economic system had to be created on challenging foundations. Indeed, the War of Independence left heavy traces of the society, and the early 20th century world

stage was chaotic and unstable. We analyzed all different phases up to the present day by focusing on the macroeconomic level, thus giving an idea of what Turkey went through before reaching the growth level everybody witnesses today.

The current economic performance of Turkey has been analyzed, with a focus on its FDI environment. Despite recent improvements in its capacity to attract foreign direct investment, Turkey still lags behind other emerging economies, because of several obstacles, real or supposed, that foreign capitals find on their way. The same can be said about outward flows of investment, although they have a longer tradition than IFDI. Indeed, due to deep economic instability during the 1990s, Turkish enterprises started to look for more opportunities abroad, and established their businesses in more profitable markets, as we stated before.

Romania is one of these countries, whose large and not too crowded market attracted numerous firms. Interest of this study was also to investigate the process that brought Romania to its current economic situation and to understand how, together with a very large group of countries, it was able to transform from a socialist to a market-based country. This process has been long and traumatic for all transition economies, though with different modes and timing.

In Romania its traces can still be found in the difficulties it has in the attempt to gain stability and its incapacity to cope with the present global crisis in a firm way. A political class not always prepared and short-sighted state institutions have weighed on its economic performance. Despite this, Romania has always been an attractive destination of FDI compared to its neighboring countries, but the recent global crisis had a heavy impact on it. Indeed, FDI flows decreased sharply in 2009 and are not yet recovered.

Romania is today a member of the EU, and this status improved its attractiveness for foreign investors, the Turkish included. However, Turkish entrepreneurs were active in the country long before its adhesion to the EU, and in fact, they have created a well established business community. Because of its history and characteristics, this community can be included in the context of ethnic entrepreneurship. The strong point of ethnic entrepreneurship is the positive impact they have, especially in urban areas,

through “social bonds in a cultural network”. These can make it easier to attract personnel and capital, can help integrate two cultures, and generate “market niches for specific cultural goods” (Constantin *et al*. 2010).

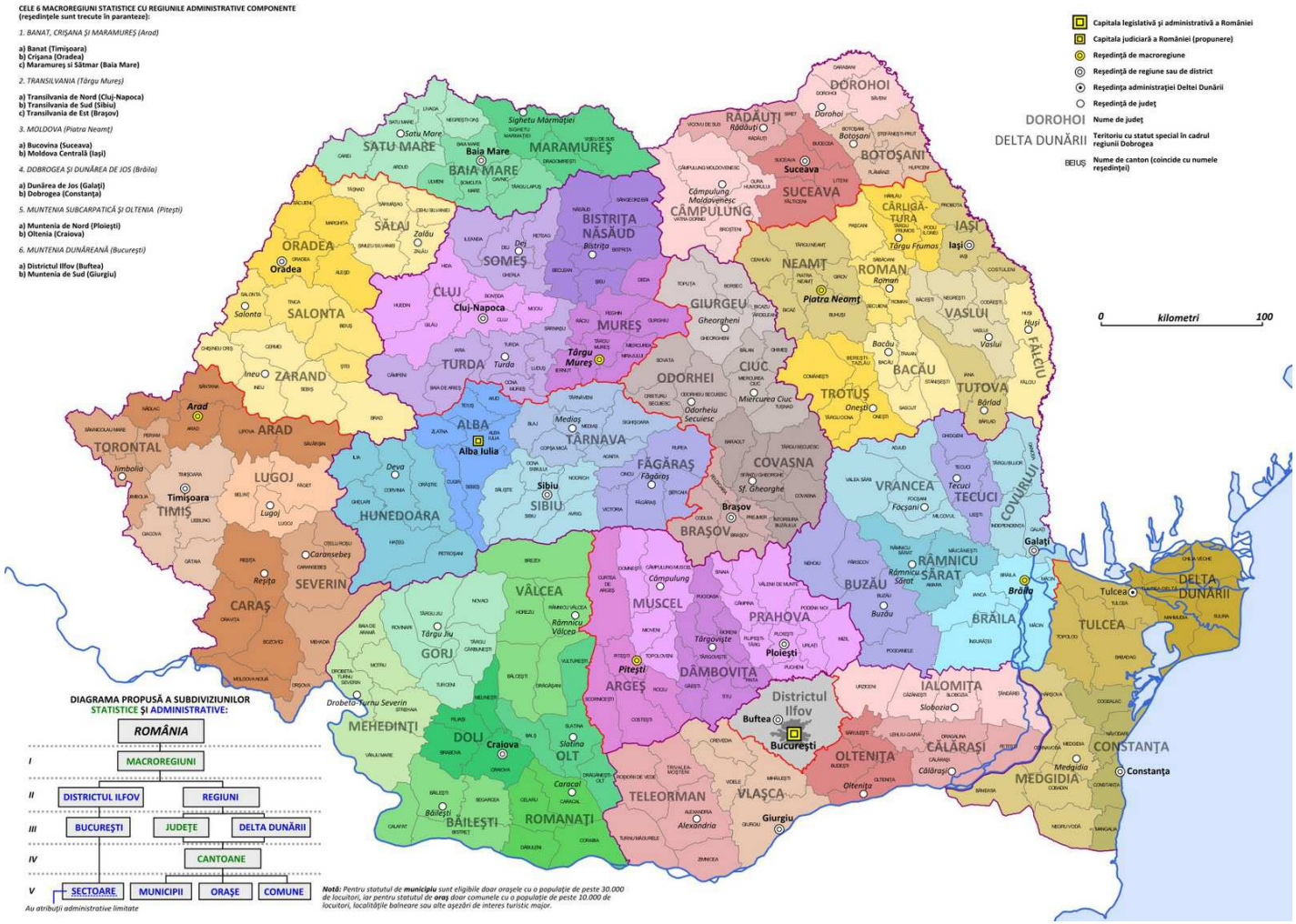
The early Turkish businessmen operating in Romania were running small activities, mainly in the food industry, such as bakeries and restaurants. Thanks to their successful experience, new waves of investment from Turkey started to arrive all along the 1990s, targeting an increasingly wider range of sectors.

Today, the majority of enterprises is engaged in manufacturing, trading, and construction. Manufacture productions vary largely, from metal to food products, from wood to home appliances. The banking sector is also very active in Romania, and it accounts for the bulk of the invested capital. By 2012, 274 Turkish companies were registered in Romania. Compared with the other main recipients of Turkish FDI, this number appears very high, thus showing that Romania mainly hosts small activities with relatively little invested capital.

To conclude, it is out of doubt that Turkey is reorienting its political and economic interest to emerging areas of Europe and to its neighboring countries. the high number of agreements and meetings both at the public and private level confirm this statement. Indeed, today more than in the past, the Turkish political and economic realm are highly interconnected and interdependent. It is no secret that high representatives of Turkey firmly sustain the entrepreneurial class and try to facilitate the economic exchanges with foreign countries. This is particularly true for the groups of economies we took in consideration in this work, which represent very good opportunities for Turkish firms to expand and strengthen their influence at the international level.

Map of Turkey (http://www.worldembassyinformation.com/world-maps/maps-of-turkey.html)

Map of Romania, by regions and counties (http://www.deferlari.ro/2011_05_01_archive.html)



REFERENCES

BOOKS AND ARTICLES

Acemoğlu, Daron, and Robinson, James. 2013. “The political economy of Turkey”. *Why nations fail blog*, Febraury 2013. http://whynationsfail.com/blog/2013/2/27/the-political-economy-of-turkey.html.

Aizenman, Joshua, and Marion, Nancy. 2004. “The merits of horizontal versus vertical FDI in the presence of uncertainty”. *Journal of International Economics* 62 : 125-148. Doi:10.1016/j.jinteco.2003.08.003.

Akyüz, Yılmaz, Boratav, Korkut. 2003. “The making of the Turkish financial crisis”. Paper presented at the conference “Financialization of the Global Economy”, Peri, University of Massachusetts, December 7-9.

Alfaro, Laura, and Chanda, Areendam, and Kalemli-Ozcan, Sebnem, and Sayek, Selin. 2000. “FDI and economic growth: the role of local financial markets”. *Journal of International Economics*, Vol. 64, No. 1 : 89-112. http://econweb.umd.edu/~kalemli/jiefinal.pdf.

Altomonte, Carlo, and Guagliano, Claudia. 2003. “Comparative study of FDI in Central and Eastern Europe and the Mediterranean”. *Economic Systems* 27 : 223–246. Doi:10.1016/S0939-3625(03)00042-6.

Anıl, İbrahim, and Armutlulu, İsmail, and Canel, Cem, and Porterfield, Rebecca. 2011. “The Determinants of Turkish Outward Foreign Direct Investment”, *Modern Economy* 2 : 717-728. Doi:10.4236/me.2011.25080.

Aybar, Sedat, Songur, Hilmi, Yelutaş, Nihan, İnanır, Samet. 2009. “Survey provides the first ever ranking of Turkish multinationals investing abroad”. Paper presented at the OECD Eighth Global Forum on International Investment, Istanbul and New York, December 03.

Aykut, Dilek, and Goldstein, Andrea. 2006. “Developing countries multinationals: South-South investment comes of age”, *OECD Development Centre Working Paper* 257. http://www.oecd.org/dev/wp.

Baker, Paul. 2012. “An Analysis of Double Taxation Treaties and their Effect on Foreign Direct Investment”. University of Cambridge. http://www2.warwick.ac.uk/fac/soc/economics/news_events/conferences/peuk12/paul_l__baker_dtts_on_fdi_23_may_2012.pdf.

Bilefsky, Dan. 2012. “Resilient Romania Finds a Currency Advantage in a Crisis”. *New York Times*, November 3. http://www.nytimes.com/2012/11/04/world/europe/resilient-romania-finds-advantage-in-a-crisis.html?pagewanted=all.

Birsan, Maria, and Buiga, Anuta. 2008. “FDI in Romania: Evolution and Main Types of Large Firms in the Manufacturing Sector”. Paper presented at the OECD 7th Global Forum on International Investment, March 27-28.

Blonigen, Bruce A. 2005. “A Review of the Empirical Literature on FDI Determinants”. *Atlantic Economic Journal* 33 : 383-403. DOI: 10.1007/s11293-005-2868-9.

Bonaglia, Federico; Goldstein, Andrea and Mathews, John. 2006. “Accelerated Internationalisation by Emerging Multinationals: the Case of White Goods Sector”. *MPRA Paper* No. 1485. http://mpra.ub.uni-muenchen.de/1485/.

Böwer, Uwe, and Fernandez, David, and Thimann, Christian. 2009. “Outward FDI from Emerging Markets: Evidence from Firm-Level M&A Data”. http://www.eea-esem.com/files/papers/EEA-ESEM/2009/1137/2009-02-12-OFDI-paper-Boewer.pdf.

Celâsun, Merih, and Rodrik, Dani. “Turkish Economic Development: An Overview”. In *Developing Country Debt and Economic Performance, Volume 3: Country Studies - Indonesia, Korea, Philippines, Turkey*, edited by Jeffrey D. Sachs and Susan M. Collins, 617-629. Chicago: University of Chicago Press, 1989.

Celâsun, Merih, and Rodrik, Dani. “Stabilization and Adjustment Policies, 1980-85”. In *Developing Country Debt and Economic Performance, Volume 3: Country Studies -*

Indonesia, Korea, Philippines, Turkey, edited by Jeffrey D. Sachs and Susan M. Collins, 662-679. Chicago: University of Chicago Press, 1989.

Celâsun, Oya. 1999. “The 1994 currency crisis in Turkey”. *World Bank e-library*. Doi: 10.1596/1813-9450-1913.

Chapin Metz, Helen. 1995. “Turkey: A Country Study”. *GPO for the Library of Congress.* Washington.

Choi, Changkyu. 2006. “Does foreign direct investment affect domestic income inequality?” *Applied Economic Letters* 13 : 811-814. DOI: 10.1080/13504850500400637.

Cojocaru, Bianca. 2010. “Romanian-Turkish trade to reach USD 10 bln”. *Nine O’Clock*, May 30. http://www.nineoclock.ro/romanianturkish-trade-to-reach-usd-10-bln/.

Constantin, Daniela L., and Goschin, Zizi, and Danciu, Aniela R. 2011. “ The Romanian Economy from Transition to Crisis. Retrospects and Prospects”. *World Journal of Social Sciences*, Vol. 1, No. 3 : 155-171. http://www.wjsspapers.com/static/documents/July/2011/11.%20Aniela.pdf.

Constantin, Daniela L., and Goschin, Zizi, and Dragusin, Mariana, and Padina Valeria. 2010. “Ethnic entrepreneurship as a gate to a more entrepreneurial Romania. The case of Turkish entrepreneurs”. Paper presented at the Regional Studies Association Annual International Conference, Pécs, Hungary, May 24-26.

Demekas, Dimitri G., and Horváth, Balázs, and Ribakova, Elina, andWu, Yi. 2007. “Foreign direct investment in European transition economies—The role of policies”. *Journal of Comparative Economics* 35 : 369–386. Doi:10.1016/j.jce.2007.03.005.

Demirbağ, Mehmet, and Tatoğlu, Ekrem, and Glaister, Keith W. 2010. "Institutional and transaction cost determinants of Turkish MNEs' location choice", *International Marketing Review*, Vol. 27, No. 3 : pp. 272 – 294. Doi:10.1108/02651331011047989.

Demirbağ, Mehmet, and Glaister, Keith W., and Tatoğlu, Ekrem. 2007. “Institutional and transaction cost influences on MNEs’ ownership strategies of their affiliates: Evidence from an emerging market”. *Journal of world Business* 42 : 418-434. Doi:10.1016/j.jwb.2007.06.004.

Deng, Ping. 2012. “Accelerated internationalization by MNCs from emerging economies: determinants and implications”. *Organizational Dymanics* 41 : 318-326. Doi:10.1016/j.orgdyn.2012.08.007.

Dolzer, Rudolf, and Stevens, Margrete. *Bilateral Investment Treaties*. The Hague: Kluwer Law International, 1995. http://books.google.it/books?id=u2CF6a6yvCoC&printsec=copyright&hl=it#v=onepage&q&f=false.

Dufour, Mathieu, and Orhangazi, Özgür. 2009. “The 2000-2001 Financial Crisis in Turkey: A Crisis for Whom?”. *Review of Political Economy,* Vol 21, No. 1 :101-122.

Dunning, John H. 1987. “The eclectic paradigm of international production: a restatement and some possible extensions”. *Journal of International Business Studies* 19, 1–31. Doi:10.1057/palgrave.jibs.8490372.

Erdem, Nilgün. 2009. “Financial Crises and New Patterns of Dependency in the Turkish Economy”. Paper presented at the Third International Initiative for Promoting Political Economy (IIPPE) International Research Workshop, Ankara, September 14-15.

Erdil, T. Sabri. 2012. “An analysis of internationalisation behavior of firms through activities and the case of Turkish firms”. *Procedia - Social and Behavioral Sciences* 58 : 1247 – 1255. Doi: 10.1016/j.sbspro.2012.09.1107.

Erdilek, Asım. 2010. “Turkey’s foreign direct investment performance and potential”, *Today’s Zaman*, August 2.

Erdilek, Asım. 2009. “Turkey’s inward and outward foreign direct investment performance”. *Sunday’s Zaman*, January 26.

http://www.todayszaman.com/columnists/asim-erdilek-165093-turkeys-inward-and-outward-foreign-direct-investment-performance.html.

Erdilek, Asım. 2008. “Internationalization of Turkish MNEs”. *Journal of Management Development*, Vol. 27, No. 7 : 744 – 760. http://dx.doi.org/10.1108/02621710810883634.

Erdilek, Asım. 2005. “Case Study on Outward Foreign Direct Investment by Enterprises from Turkey”. Paper presented at the Expert Meeting on Enhancing Productive Capacity of Developing Country Firms through Internationalization, Geneva, December 5-7.

Erdilek, Asım. 2005. “Historical breakdown of foreign direct investment in Turkey”. Paper presented at the YASED Conference “The new favourite destinations for foreign direct investment: Turkey, where the opportunities abound”, Istanbul, November 8-9.

Erdilek, Asım. 2003. “A comparative analysis of inward and outward FDI in Turkey”. *UNCTAD Trasnational Corporations*, Vol. 12, No. 3.

Ertuğrul, Ahmet, and Selçuk, Faruk. 2001. “A brief account of the Turkish economy, 1980-2000”. *Russian and East European Finance and Trade*, Vol. 37, No. 6 : 6-30.

Falcetti, Elisabetta, and Lysenko, Tatiana, and Sanfey, Peter. 2005. “Reforms and growth in transition: re-examining the evidence”. *EBRD Working Paper* No. 90.

“FDI with Chinese characteristics”. 2012. *Economist*, September, 6. http://www.economist.com/blogs/graphicdetail/2012/09/focus.

Goldstein, Andrea. 2009. “Multinational companies from emerging economies composition, conceptualization & direction in the global economy”. *Indian Journal of Industrial Relations*, Vol. 45, No. 1.

Goldstein, Andrea. 2007. *Multinational Companies from Emerging Economies: Composition, Conceptualization and Direction in the Global Economy*. Basingstoke and New York : Palgrave MacMillan.

Goldstein, Andrea, and Bonaglia, Federico. 2005. “Emerging Multinationals in Global Value Chains: Arçelik, Haier and Mabe”. *Draft version.* http://www.dagliano.unimi.it/media/Bonaglia.pdf.

Government of Romania 2008. *National Reform Programme – Implementation Report*. ec.europa.eu/social/BlobServlet?docId=6263&langId=en.

Görmez, Yüksel, and Yiğit, Serkan. 2009. “The economic and financial stability in Turkey : a historical perspective”. Paper presented at the Fourth Conference of South East Europe Monetary History Network.

Gülsoy, Tanses, and Özkanlı, Özlem, and Lynch, Rihcard. 2011. “International branding strategies of developing countries: The case of Arçelik”. *Procedia Social and Behavioral Sciences* 24 : 1201–1217. Doi:10.1016/j.sbspro.2011.09.136.

Gros, Daniel, and Selçuki, Can. 2013. “The changing structure of Turkey’s trade and industrial competitiveness : implications for the EU”. *Center for European Policy Studies*, Working Paper 3.

Havrylyshyn,, Oleh, and Izvorski, Ivailo, and van Rooden, Ron. 1998. “Recovery and Growth in Transition Economies 1990-1997: A Stylized Regression Analysis”. *IMF Working Paper* 98/141. http://www.imf.org/external/pubs/ft/wp/wp98141.pdf.

Hunya, Gábor. 2004. “Foreign Direct Investment in South-East Europe in 2003-2004”, A study commissioned by the *OECD Investment Compact for South-East Europe*. http://www.stabilitypact.org/investment/2004,%20FDI%20in%20SEE.pdf.

IMF. 2000. “Transition Economies: An IMF Perspective on Progress and Prospects”. http://www.imf.org/external/np/exr/ib/2000/110300.htm#I.

Invest in Turkey. 2013. “FDI in Turkey”. http://www.invest.gov.tr/en-US/investmentguide/investorsguide/pages/FDIinTurkey.aspx#PageTop.

-Iordache, Mihaela. 2005. “Romania e Turchia, sguardi attraverso il Mar Nero”. *Osservatorio Balcani e Caucaso*, January 25.

http://www.balcanicaucaso.org/aree/Romania/Romania-e-Turchia-sguardi-attraverso-il-Mar-Nero.

"Istanbuls and bears Turkey has one of the world's zippiest economies, but it is too reliant on hot money". 2012. *Economist*, April 7. http://www.economist.com/node/21552216.

Istituto nazionale per il Commercio Estero (ICE), Bucharest office. Updated 2012. "Struttura dell'economia romena". http://www.icebucarestnews.ro/articol/336/STRUTTURA-DELL-ECONOMIA-ROMENA.html.

Kaya, Harun. 2009. "Unfavorable business environment and Foreign Direct Investment activities of Turkish manufacturing firms". BDDK Bankacılık ve Finansal Piyasalar, Vol. 3, No. 1.

Keane, Michael P., and Prasad, Eswar S. 2000. "Inequality, Transfers and Growth: New Evidence from the Economic Transition in Poland". *IMF Working Paper* 00/117. http://www.imf.org/external/pubs/ft/wp/2000/wp00117.pdf.

Krugman, Paul. 2013. "This Age of Bubbles". *New York Times*, August 22. http://www.nytimes.com/2013/08/23/opinion/krugman-this-age-of-bubbles.html.

Jorland, Patrice. 2011. "La civette turque". *Recherches Internationales*, No. 91 : 25-36.

Landon, Thomas. 2013. "Istanbul Skyline Reflects Cheap Dollars Now Growing Scarce". *New York Time*s, August 20. http://www.nytimes.com/2013/08/21/business/global/turkish-skyline-foreshadows-emerging-market-slowdown.html?hp&_r=0.

Luo, Yadong, and Xue, Qiuzhi, and Han, Binjie. 2010. How emerging market governments promote outward FDI: Experience from China". *Journal of World Business* 45 : 68–79. Doi:10.1016/j.jwb.2009.04.003.

Macovei, Mihai. 2009. “Growth and economic crisis in Turkey : leaving behind a turbulent past?” *European Commission Economic Paper* 386. Doi:10.2765/2888.

Mody, Ashoka. 2004. “What is an emerging market?” *IMF Working Paper* 04/177. http://cdi.mecon.gov.ar/biblio/docelec/fmi/wp/wp04177.pdf.

Myant, Martin, and Drahokoupil, Jan. 2011. *Transition economies: Political economy in Russia, Eastern Europe and Central Asia.* Hoboken, NJ: John Wiley and Sons.

OECD 2013, *OECD Factbook 2013: Economic, Environmental and Social Statistics*, OECD Publishing. Doi: 10.1787/factbook-2013-en.

Oxford Business Group. 2013. “An unorthodox approach : understanding the Central Bank’s corridor interest rate policy”. http://www.oxfordbusinessgroup.com/news/unorthodox-approach-understanding-central-bank%E2%80%99s-corridor-interest-rate-policy.

Öktem, Kerem. *Turkey since 1989 : Angry Nation*. London: Zed books, 2011.

Öniş, Ziya. 2010. “Crises and transformations in Turkish political economy”. *Turkish Policy Quarterly*, Vol. 9, no. 3. http://www.turkishpolicy.com/dosyalar/files/45-61.pdf.

Öniş, Ziya. 2006. “Varieties and Crises of Neoliberal Globalization: Argentina, Turkey and the IMF”. *Third World Quarterly*, Vol. 27, No. 2 : 239 – 263. Doi:10.1080/01436590500432366.

Öniş, Ziya. 2004a. “Turgut Özal and his economic legacy: Turkish neo-liberalism in critical perspective”. In *Middle Eastern Studies* 40 : 113-134.

Öniş, Ziya. 2004b. “The political economy of Turkey’s Justice and Development Party”. http://papers.ssrn.com/sol3/papers.cfm?abstract_id=659463.

Özatay, Fatih. 2002. “Turkey’s 2000-2001 financial crisis and the Central Bank policy in the aftermath of the crisis”. Paper prepared for the conference “Bank of Albania in the Second Decade of Transition”, Tirana, December 6.

Pauwels, Stefaan, and Ionita, Lorena. 2008. “FDI in Romania: from low-wage competition to higher value-added sectors”. *ECFIN Country Focus* Vol. 5, No. 3. http://ec.europa.eu/economy_finance/publications/publication_summary11899_en.htm.

Phinnemore, David. 2006. The EU and Romania: *Accession and Beyond*. London : Federal Trust for Education and Research. http://books.google.it/books?id=sZ92gFH7RtIC&pg=PA156&lpg=PA156&dq=Turkish+enterprises+Romania&source=bl&ots=-7QX7_uhMg&sig=OeIEagYlZFM3.

Pirciog, Speranta. 2004. “Foreign Direct Investment in Romania: Legal Framework and Incentives”. *EURECO Workpackage* No. 4. http://www.zei.uni-bonn.de/dateien/zeib/eurec/WP4_Romania.pdf/at_download/file.

Platis, Eirinikos. 2012. “Legal Considerations for Foreign Investors in Romania”. *Ernst&Young*. http://www.ey.com/Publication/vwLUAssets/Legal_considerations_for_foreign_investors_in_Romania_(EN)/$FILE/MCR_Legal%20considerations%20_EN_%2019%20Apr12.pdf.

Rajan, Ramkishen. 2004. “Measures to attract FDI: Investment Promotion, Incentives and Policy Intervention”. *Economic and Political Weekly*, Vol. 39, No. 1. http://www.jstor.org/stable/i400644.

Rawdanowicz, Lukasz. 2010. “The 2008-09 Crisis in Turkey: Performance, Policy Responses and Challenges for Sustaining the Recovery”, *OECD Economics Department Working Paper*, No. 819, OECD Publishing. http://dx.doi.org/10.1787/5km36j7d320s-en.

Rodrik, Dani. 2013. “How well did the Turkish economy do over the last decade?” *Dani Rodrik’s weblog*, June 20. http://rodrik.typepad.com/dani_rodriks_weblog/2013/06/how-well-did-the-turkish-economy-do-over-the-last-decade.html.

Rodrik, Dani. 2012. “The Turkish economy after the global financial crisis”. *Ekonomi-tek*, Vol. 1, No. 1 : 41-61.

Romania Business Law Handbook Vol.1 : Strategic Information and Basic Laws. 2013. Washington DC : International Business Publications.

Sachs, Jeffrey. 2013. “Turkey's economy is thriving in a dangerous neighborhood”. *Guardian*, May 28. http://www.theguardian.com/business/economics-blog/2013/may/28/turkey-economy-thriving-jeffrey-sachs.

Sauvant, Karl P. and Sachs, Lisa. 2009. *The effect on treaties on foreign direct investment*. New York: Oxford University Press.

Sauvant, Karl P. 2008. “Outward FDI from emerging markets: some policy issues”. *Progress in International Business Research*, Vol. 2 : 279–284. Doi:10.1016/S1745-8862(07)00012-X.

Sauvant, Karl P. 2005. “New Sources of FDI: The BRICs”. *Journal of World Investment and Trade*, Vol. 6, No. 5 : 639-709. http://www.vcc.columbia.edu/pubs/documents/Website_JWIT_New_Sources_of_FDI_The_BRICs_KPS_article.pdf.

Săviou, Gheorghe, and Popa, Suzana. 2012. “Foreign Direct Investment (FDI) in Romania”. *Romanian Statistical Review* Vol. 60, No. 1 : 42-56. http://www.revistadestatistica.ro/Articole/2012/art3en_rrs_%201_2012.pdf.

Serin, Vildan, and Çalışkan, Ahmet. 2010. “Economic Liberalization Policies and Foreign Direct Investment in Southeastern Europe”. *Journal of Economic and Social Research*, Vol. 12, No. 2 : 81-100. http://www.fatih.edu.tr/~jesr/jesr_12_2_3%20jesr.serin.%20caliskan.son.publ.%20221010%20Re-edit.pdf.

Sethi, Deepak. 2009. “Are multinational enterprises from the emerging economies global or regional?” *European Management Journal* 27 : 356– 365. Doi:10.1016/j.emj.2009.04.009.

Shenkar, Oded. “Foreign direct investment theory and application”. In *International Business*, written by Oded Shenkar and Yadong Luo. SAGE publications, 2007.

Sidar, Cenk. 2012. “Turkey’s fragile success”. *Foreign Policy*, September 20. http://www.foreignpolicy.com/articles/2012/09/20/turkeys_fragile_success.

Slaveski, Trajko, and Nedanovski, Pece. 2002. “Foreign Direct Investment in the Balkans: the Case of Albania, FYROM and Bulgaria”. *Eastern European Economics*, Vol. 40, No. 4 : 83-89. http://mesharpe.metapress.com/link.asp?target=contribution&id=3T7BYNB9FLTTMXRF.

Stănculescu, Manuela Sofia, and Marin, Monica. 2011. *Impacts of the international economic crisis in Romania 2009-2010*. UNICEF. Bucharest : Vanemonde.

Stephan, Johannes. 2006. *Technology Transfer via Foreign Direct Investment in Central and Eastern Europe.* Basingstoke and New York : Palgrave MacMillan.

Svejnar, Jan. 2002. “Transition Economies: Performance and Challenges”. *Journal of Economic Perspectives,* Vol. 16, No. 1 : 3–28. DOI: 10.1257/0895330027058.

Togan, Sübidey. 2012. “The EU-Turkey Customs Union : A Model for Future Euro-Med Integration”. *MEDPRO Technical Report* 9.

Tkyay, Menekse, and Ciocoiu, Paul. 2013. “Romania and Turkey deepen strategic partnership”. *Southeastern European Times in Istanbul and in Bucharest*. http://www.setimes.com/cocoon/setimes/xhtml/en_GB/features/setimes/features/2013/03/29/feature-04.

Trifonova Marinova, Svetla, and Alexandrov Marinov, Marin. 2003. *Foreign Direct Investment in Central and Eastern Europe*. Ashgate Publishing.

“Turkey posts sharp fall in growth rate for 2012”. 2013. *Hürriyet Daily News*. April 1. http://www.hurriyetdailynews.com/turkey-posts-sharp-fall-in-growth-rate-for-2012.aspx?pageID=238&nid=44032.

“Turkey 2013 : the shift, the growth and the promise”. 2013. *Ernst and Young’s Attractiveness Survey*.

http://www.ey.com/Publication/vwLUAssets/Turkey_attractiveness_survey_2013/$FILE/turkey_attractiveness_2013.pdf.

"Turkish Business in the BSEC Region: Direct Investments, Contracting Services, Prospects for Cooperation". 2005. *Foreign Economic Relations Board of Turkey (DEİK)*. http://www.oecd.org/turkey/34479020.pdf.

Uckun, Duygu, and Doerr, Mark. 2010. "Emerging Markets: Theory & Practice / Turkey's Reforms Post 2001 Crisis". *Journal of Global Analysis* 1.

UNCTAD 2013, *World Investment Report 2013: Global Value Chains: Investment and Trade for Development*, United Nations Publication. http://unctad.org/en/pages/PublicationWebflyer.aspx?publicationid=588.

UNCTAD 2012, *Investment Country Profiles: Turkey*, United Nations Publication. http://unctad.org/en/PublicationsLibrary/webdiaeia2012d6_en.pdf.

UNCTAD 2012, *World Investment Report 2012: Towards a New Generation of Investment Policies*, United Nations Publication. http://unctad.org/en/pages/PublicationWebflyer.aspx?publicationid=171.

UNCTAD 2012, *Global Investment Trends Monitor No. 9: Global FDI outflows continued to rise in 2011 despite economic uncertainties; however prospects remain guarded*, United Nations Publication. http://unctad.org/en/PublicationsLibrary/webdiaeia2012d19_en.pdf.

UNCTAD 2008, *World Investment Report 2008: Transnational Corporations, and the Infrastructure Challenge*, United Nations Publication. http://unctad.org/en/pages/PublicationArchive.aspx?publicationid=732.

UNCTAD 2007, *Global Players from Emerging Markets: Strengthening Enterprise Competitiveness through Outward Investment*. United Nations Publication. http://unctad.org/en/Docs/iteteb20069_en.pdf.

UNCTAD 2006, *World Investment Report 2006: FDI from Developing and Transition Economies: Implications for Development*. United Nations Publication. http://unctad.org/en/pages/PublicationArchive.aspx?publicationid=709.

UNDP 2002, *National Human Development Report Romania 2001-2002: A decade later: Understanding the Transition Process in Romania*. United Nations Publication. http://hdr.undp.org/en/reports/national/europethecis/romania/name,3191,en.html.

Uray, Nimet, and Vardar, Nukhet, and Nacar, Ramazan, and Aktan, Canan, 2010. "Do Turkish MNCs with outward FDI into Europe have different motives than other EMNCs?: An International Marketing Focus".

Vasilescu, Laura Giurcă. 2007. "Foreign Direct Investment in Romania – Recent Trends". *Revista Tinerilor Economisti (The Young Economists Journal),* University of Craiova, Faculty of Economics and Business Administration, Vol. 1, No. 9S : 27-34. http://feaa.ucv.ro/RTE/009S-04.pdf.

Voyvoda, Ebru, and Yeldan, Erinç. 2006. "Macroeconomics of *Twin-Targeting* in Turkey : A General Equilibrium Analysis". http://www.bilkent.edu.tr/~yeldane/econmodel/Voyvoda%26Yeldan_AltIT-Turkey_2006.pdf.

Walsh, James P., and Jiangyan, Yu. 2010. "Determinants of Foreign Direct Investment: A Sectoral and Institutional Approach". *IMF Working Paper* 10/187. http://www.imf.org/external/pubs/ft/wp/2010/wp10187.pdf.

"Why the tail wags the dog". 2011. *Economist*, August 6. http://www.economist.com/node/21525373.

Wooldridge, Adrian. 2010. "The emerging emerging markets: Businesses will learn to look beyond the BRICs". *Economist*, November 22. http://www.economist.com/node/17493411

World Bank. 2013. *Turkey Regular Economic Brief*. July. http://www.worldbank.org/content/dam/Worldbank/document/eca/tr-reb-eng-jul-2013.pdf.

Yalçin, Mehmet. 2012. “Evaluation of the 2008 Global Financial Crisis’ Effects on Turkish Economy. Is it tangential?”. http://www.academia.edu/1564330/Effect_of_2008_Global_Financial_Crisis_over_Turkey

Yaprak, Attila, and Karademir, Bahattin. 2011. “Emerging market multinationals’ role in facilitating developed country multinationals’ regional expansion: A critical review of the literature and Turkish MNC examples”. *Journal of World Business,* 46 : 438–446. Doi:10.1016/j.jwb.2010.10.004.

Yeldan, Erinç. 2006. “ Turkey 2001-2006 Macroeconomics of Post-Crisis Adjustments”. *Global Policy Network*. http://www.gpn.org.

Yeung, Henry Wai-chung. 1999. “Introduction: competing in the global economy”, in *The Globalisation of Business Firms from Emerging Economies* edited by Henry Wai-chung Yeung, Two Volumes, Cheltenham: Edward Elgar.

Yılmazkuday, Hakan, and Akay Koray. 2007. “An analysis of regime shifts in the Turkish economy”. *Economic Modelling* 25 : 885–898. http://papers.ssrn.com/sol3/papers.cfm?abstract_id=995557.

Zamfir, Paul-Bogdan. 2010. “The global financial crisis, where does place Romanian economy in EU?” *Annals of the University of Petroşani, Economics,* Vol. 10, No. 1 : 371-378. http://econpapers.repec.org/article/petannals/v_3a10_3ay_3a2010_3ai_3a2_3ap_3a371-378.htm.

WEBSITES

Arçelik official Website :
http://www.arcelikas.com/UserFiles/file/ArcelikFRENG2011.pdf

Central Bank of Turkey, English version : http://www.tcmb.gov.tr/yeni/eng/

Maps of Romania : http://www.deferlari.ro/2011_05_01_archive.html

Embassy of Romania in the Republic of India : http://newdelhi.mae.ro/en/node/795

International Finance Corporation :
(http://ifcext.ifc.org/ifcext/masterinternet.nsf/AttachmentsByTitle/ifctFS.htm/$FILE/ifctFS.htm)

Ministry of Foreign Affairs of Turkey, Relations between Turkey and Romania :
http://www.mfa.gov.tr/relations-between-turkey-and-romania.en.mfa

Ministry of the Economy of Turkey, Countries & Regions :
http://www.economy.gov.tr/index.cfm?sayfa=countriesandregions&country=RO&region=8

National Bank of Romania : http://www.bnro.ro/Home.aspx

National Trade Register Office, Ministry of Justice :
http://www.onrc.ro/english/legislation.php

OECD Statistics : http://stats.oecd.org/

Office of the Commercial Counsellor, Turkish Embassy in Bucharest :
http://www.economy.gov.tr/index.cfm?sayfa=counsellor&region=2&country=RO&city=0311B631-B87B-FE4F-5CE726FF79BA4CA7

The Romanian Digest : http://www.hr.ro/digest/200809/digest.htm

Turkish Statistical Institute : http://www.turkstat.gov.tr/Start.do

Turkish Undersecretariat of Treasury : http://www.treasury.gov.tr/default.aspx?nsw=8rarpuRhEnYdhfGWl2a5sA==-SgKWD+pQItw=

UNCTAD Statistics : http://unctadstat.unctad.org/ReportFolders/reportFolders.aspx

World Bank : http://www.worldbank.org/

World Embassy Information : http://www.worldembassyinformation.com/world-maps/maps-of-turkey.html