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Questionnaire Survey regarding the Determinants of FDI in Turkey: the significance of shadow economy

Motivation and Aim of the article

The aim of this paper is to analyze the motives of Foreign Direct Investments in the banking sector of Turkey during the decade 2001-2011, using the elements of a sample of ten major FDI deals. Based on these preliminary results, a questionnaire will be formulated for conducting a questionnaire review during June-August 2013 of major foreign investors in Turkey.

Turkey is a characteristic example of economic development which took place in the period 2001-2013 (March). Cumulative FDI inflows (net) until March 2013 reached $137 billion from $15 billion in 2002-1954. The number of companies with foreign capital participation reached 33,451 from 4,869 respectively. The number of investor countries increased to 152. In the period 2003-March 2013, Netherlands ranked first with $15.8 billion and is followed by the USA with $8.2 billion; also, Greece is included in the top positions, with inflows estimated to approximately $6.5 billion.

FDI inflows in the Turkish financial intermediation sector are the main contributor. Also, acquisitions of real estate by foreigners are substantial and reached $22.6 billion in the period 2003-2013 (March).

Finally, the shortage of related or updated academic research focused on questionnaire surveys/interviews on direct investments in Turkey was a significant motivation for the current research. Accordingly, only 12 relevant studies were identified to have been contacted during the period1995-2011 (the majority of which are before 2004), of which one (Coskun, 2001) compares the results of three previous surveys (Kontakos, 2013). The majority of papers are focused on the analysis & estimation of the importance of FDI determinants in Turkey.

Motives, Incentives and barriers for Foreign Investors in SEE, CEE and Turkey

Bitzenis (2006, 2007) has conducted a comprehensive literature review of questionnaire surveys regarding the FDI determinants in CEE and SEE regions. Based on this review a Questionnaire has been constructed. The conceptual framework is derived from the Eclectic Paradigm, or the "OLI" approach, developed by Dunning (1993), and is further expanded to include expanded in a more synthetic approach, i.e. the so called "Universal" model (Bitzenis 2011, 2003)

Kontakos (2012) applied a similar approach for the motives in the case of FDI in the Turkish banking sector. These motives will also be considered during the construction of the conceptual framework of the questionnaire. The motives are exported from feedback retrieved from interviews and supplemented from information communicated in the bulletins of major financial institutions on the official date of statement of repurchase. Even if other factors can be announced to investors, he considers that the information also contained in the official bulletins as rather significant, precise and constructive for their real motives (Table 1).

Table 1: Foreign Banks in Turkey: FDI Determinants

Buyer	*CITI*	*BNP*	*HSBC*	*NBG*	*EFG*	*UCG*	*Denis*	*ING*	*NCB*	*BBVA*
Target	*Akbank*	*TEB*	*Demir*	*Finans*	*Tekfen*	*Yapi Kr*	*Denis*	*Oyak*	*TFinans*	*Garanti*
Location – Country Advantages										
Geographical proximity				■	■					
Cultural similarities /closeness									■	
Market Advantages										
Expected economic growth				■	■	■				■
Political stability										■
Macroeconomic stability										■
Potential entrance in EU										
Unexploited market, or demand, growth potential		■	■	■	■	■	■	■	■	■
Market size				■	■		■			■
Bank's (Efficiency) Advantages										
High profitability size or margins of the target	■		■				■			■
Economies of scale		■	■	■	■	■		■		
Economies of scope (and cross-selling)		■	■	■	■	■		■		
Competition pressures in home country										■
International or regional player	■	■	■	■	■	■	■	■		■
Increasing the global presence				■	■			■	■	
Become a local leader player	■	■				■		■		■
Exploiting or acquiring know-how and expertise	■	■	■	■	■	■	■	■	■	■
Exploiting or acquiring know-how in IT technology	■				■					■
Exchange "best practices" with the target	■		■	■	■					
Product/customer profile of the target				■	■					
Synergies in loan/deposit ratio with the target				■					■	
Risk diversification				■			■			■
Government's Incentives										
Deregulation / Financial liberalization										

Source: Press releases, P. Kontakos
Note: Tonal box signifies that motive is applicable to that bank.

The motives have been categorized in four categories: Location and country advantages, market advantages, efficiency advantages for the foreign bank investors and incentives from the Turkish government. The first three categories have been determined according to the frame of modified approach of selected example OLI of Dunning and the Internalization Theory.

Finally the significance of Turkish shadow economy as an FDI determinant will be explicitly analyzed in the questionnaire review, particularly given its size, as previously indicated by Bitzenis, Schneider & Vlachos (2012) in other cases (Table 2).

Empirical evidence from cross-border acquisitions in the Turkish banking sector during the period 2001-2011: Concluding remarks

The foreign investors in Turkey banking which were analyzed are (in bracket is included the acquired local bank): Citigroup (Akbank), BNP Paribas (Turk Economy Bankasi, TEB), HSBC Bank (Demirbank), National Bank of Greece (Finansbank), EFG Eurobank Ergasias (Tekfenbank), UniCredit (Yapi Kredi Bank), Dexia (DenizBank), ING (Oyak Bank), National Commercial Bank (Turkiye Finans), and Banco Bilbao Vizcaya Argentaria (Turkiye Garanti Bankasi).

Location country advantages mainly arise from the existence of positive cultural and geographical linkages. Cultural similarities and closeness, either historical, religion, linguistic or other, can significantly reduce the costs of operating abroad, while facilitating the exploitation of other efficiencies or competitive advantages. Cultural proximity may also lead to advantages in product differentiation (Swoboda, 1990) and knowledge transfer (Guillen and Tschoegl, 1999). At the same time, geographical proximity between the home and host countries can prompt mutual or unilateral exchange of FDI flows, particularly in the presence of cultural ties. The cultural proximity is more obvious in the case of the acquisition by National Commercial Bank (NCB) of Turkiye Finans.

Foreign banks need to establish a physical presence abroad in order to provide effectively a range of financial services to their customers (Focarelli and Pozzolo, 2005). Host market advantages such as its size, level of development, GDP growth rates, political and macroeconomic stability, can provide foreign investors with an indication about profit opportunities. A robust result in the empirical literature is that the size of the local economy, measured either by the levels of GDP (Goldberg and Johnson, 1990, Brealey and Kaplanis, 1996, Buch, 2003), population (Papi and Revoltella, 2000, Buch, 2000), or industrial production (Buch, 2003), has a positive effect on banking sector FDI. Focarelli and Pozzolo (2005) suggest that banks are more likely to be present in countries with higher expected economic growth and find evidence that this happens when per capita GDP is lower. According to host market advantages, the expected economic growth can be characterized as a very important motive in the cases of National Bank of Greece, EFG Eurobank Ergasias, UniCredit and Banco Bilbao Vizcaya Argentaria (BBVA). Also, in terms of political stability, Turkey was characterized by BBVA as a "powerful democracy for more than 80 years and a model of country which is example for other countries". However, among the sample of banks which were analyzed, political stability was reported as a motive only from BBVA.

Macroeconomic determinants of FDI are generally classified in two major groups: push (or home-country related factors), and pull (or host country-related ones). For the first, there is no literature in the case of financial FDI, while it exists for the second (Herrero and Simon, 2003). In the context of macroeconomic stability in the host country, Bumin (2007) notices that the fluctuations in macroeconomic indicators of the countries in which the banks invest have a significant effect on their decisions. The periodic crises experienced by national economies have caused a decrease in the proceeds from the investments, and a decrease in the expected profit. Therefore, foreign banks consider the macroeconomic indicators of the host countries and invest where future expectations are positive. The macroeconomic stability per se, or in terms of inflation, monetary stabilization, fiscal consolidation, or exchange-rate volatility, was mentioned indirectly only from BBVA when it referred to the Turkish economy as one characterized by "stable and disciplined economic policies".

The market size of Turkey, in the logic of expected economic growth, usually defined in terms of GDP growth, was mentioned as a motive from the Greek investors, NBG and EFG Eurobank Ergasias, and also from NBC and BBVA. Also, foreign bank efficiency advantages were considered by Citibank, NBG, Dexia and BBVA. The economies of scale, as communicated through the press releases/official announcements of most of foreign investors are in accordance with the theory. For example, the exploitation of know-how of products and the techniques of cross-selling of BNP Paribas and TEB, under specific conditions, can be proved very important for successful synergies.

Finally, the Internalization Theory emphasizes the importance of information asymmetries and transaction costs in imperfect markets and views foreign direct investment in banking as a way to circumvent, or exploit such imperfections, by organizing an internal market within the boundaries of the firm (Williams, 1997). The importance of information in banking has persuaded some researchers that possibly the Internalization Theory is more appropriate for explaining banking FDI. It is related to the "follow the client" hypothesis in multinational banking, which states that banks "follow" their clients from their home countries into overseas markets, as the latter engage in a growing volume of international trade and FDI.

The deregulation of the Turkish financial system is not explicitly mentioned by any of the investors in this study, but can implied that is an important factor driving the decision of foreign investors to invest in the Turkish banking sector, since the entrance of most of foreign banks coincided with or shortly followed after the deregulation of the Turkish financial system in 2001.

Table 2: Shadow economy (GDP percentage).

Country/Year	2003	2004	2005	2006	2007	2008	2009	2010	2011
Bulgaria	35,9	35,3	34,4	34,0	32,7	32,1	32,5	32,6	32,3
Romania	33,6	32,5	32,2	31,4	30,2	29,4	29,4	29,8	29,6
Lithuania	32,0	31,7	31,1	30,6	29,7	29,1	29,6	29,7	29,0
Estonia	30,7	30,8	30,2	29,6	29,5	29,0	29,6	29,3	28,6
Latvia	30,4	30,0	29,5	29,0	27,5	26,5	27,1	27,3	26,5
Cyprus	28,7	28,3	28,1	27,9	26,5	26,0	26,5	26,2	26,0
Malta	26,7	26,7	26,9	27,2	26,4	25,8	25,9	26,0	25,8
Poland	27,7	27,4	27,1	26,8	26,0	25,3	25,9	25,4	25,0
Greece	28,2	28,1	27,6	26,2	25,1	24,3	25,0	25,4	24,3
Slovenia	26,7	26,5	26,0	25,8	24,7	24,0	24,6	24,3	24,1
Hungary	25,0	24,7	24,5	24,4	23,7	23,0	23,5	23,3	22,8
Italy	26,1	25,2	24,4	23,2	22,3	21,4	22,0	21,8	21,2
Portugal	22,2	21,7	21,2	20,1	19,2	18,7	19,5	19,2	19,4
Spain	22,2	21,9	21,3	20,2	19,3	18,4	19,5	19,4	19,2
Belgium	21,4	20,7	20,1	19,2	18,3	17,5	17,8	17,4	17,1
Czech Republic	19,5	19,1	18,5	18,1	17,0	16,6	16,9	16,7	16,4
Slovakia	18,4	18,2	17,6	17,3	16,8	16,0	16,8	16,4	16,0
Sweden	18,6	18,1	17,5	16,2	15,6	14,9	15,4	15,0	14,7
Denmark	17,4	17,1	16,5	15,4	14,8	13,9	14,3	14,0	13,8
Finland	17,6	17,2	16,6	15,3	14,5	13,8	14,2	14,0	13,7
Germany	17,1	16,1	15,4	15,0	14,7	14,2	14,6	13,9	13,7
Ireland	15,4	15,2	14,8	13,4	12,7	12,2	13,1	13,0	12,8
France	14,7	14,3	13,8	12,4	11,8	11,1	11,6	11,3	11,0
United Kingdom	12,2	12,3	12,0	11,1	10,6	10,1	10,9	10,7	10,5
Netherlands	12,7	12,5	12,0	10,9	10,1	9,6	10,2	10,0	9,8
Luxembourg	9,8	9,8	9,9	10,0	9,4	8,5	8,8	8,4	8,2
Austria	10,8	11,0	10,3	9,7	9,4	8,1	8,5	8,2	7,9
EU27 unweighted average	*22,3*	*21,9*	*21,5*	*20,8*	*19,9*	*19,3*	*19,8*	*19,5*	*19,2*
Non-EU European countries									
Croatia	32,3	32,3	31,5	31,2	30,4	29,6	30,1	29,8	29,5
Turkey	**32,2**	**31,5**	**30,7**	**30,4**	**29,1**	**28,4**	**28,9**	**28,3**	**27,7**
Norway	18,6	18,2	17,6	16,1	15,4	14,7	15,3	15,1	14,8
Switzerland	9,5	9,4	9,0	8,5	8,2	7,9	8,3	8,1	7,8
Highly developed non European OECD countries									
Canada	15,3	15,1	14,3	13,2	12,6	12,0	12,6	12,2	11,9
Australia	13,7	13,2	12,6	11,4	11,7	10,6	10,9	10,3	10,1
New Zealand	12,3	12,2	11,7	10,4	9,8	9,4	9,9	9,6	9,3
Japan	11,0	10,7	10,3	9,4	9,0	8,8	9,5	9,2	9,0
United States	8,5	8,4	8,2	7,5	7,2	7,0	7,6	7,2	7,0

Reference: Bitzenis, A., F. Schneider, and Vlachos, V.,The neglected impact of shadow economy and corruption on Greece's sovereign debt crisis, working paper, submitted at Journal of Economic Issues, 2013

Overall, the results of the sample of the ten foreign banks of the study are overall in accordance with previous studies, with the noticeable exception of the prospect of Turkey's accession to the European Union, which doesn't appear explicitly relevant as an explanatory factor.

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