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THE ILLUSIONAL EFFECT OF DEMOCRACY ON FDI INFLOWS

THE CASE OF TURKEY

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Demokrasi'nin DYY Girişleri Üzerinde Etkisi

Türkiye Örneği

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ABSTRACT

The effect of democracy on foreign direct investments (FDI) are among the most commonly discussed topic in international political economy. According to the liberal approaches, there is a positive causal relationship between democracy and FDI. It is claimed that democracy has a positive impact on FDI inflows. On the other hand, according to the critical approaches this relationship has been considered as more complex issue. In Turkey's literature the impact of democracy on FDI inflows is understudied. Yet, with the decline in democracy this topic has become a critical issue in order to see the fate of future FDI inflows in Turkey. Therefore, the main purpose of this thesis is to give a broader perspective for understanding the possible reasons under FDI inflows in Turkey which are declining recently. In the light of these, this thesis first analyzes Turkey's democratic breakdown between 2002-2018, after it discusses the effects of decreasing democratic indicators on FDI inflows in Turkey. As a result, there is no causal relationship between FDI inflows and democracy.

Keywords: Foreign Direct Investment (FDI), Democracy, Turkey, Multinational Companies (MNC), Macroeconomy

ÖZET

Demokrasinin doğrudan yabancı yatırımlar (DYY) üzerindeki etkisi, uluslararası politik ekonomide en çok tartışılan konular arasındadır. Liberal yaklaşımlara göre demokrasi ve DYY arasında pozitif nedensel bir ilişki vardır. Demokrasinin, DYY girişlerini olumlu yönde etkilediği iddia edilmektedir. Öte yandan eleştirel yaklaşımlarda bu ilişki daha karmaşık olarak tanımlanmıştır. Türkiye literatüründe ise demokrasinin DYY girişlerine etkisi üzerinde pek fazla çalışılmamıştır. Ancak, günümüzde demokratik yapının hızla azalması ile birlikte liberal ekonomi politikalarına devam etmeye çalışan Türkiye için, gelecekteki DYY girişlerini öngörebilmek adına, yabancı yatırım ve demokrasi arasındaki ilişki önemli bir çalışma alanı haline gelecektir. Bu sebeple, bu tezin temel amacı, Türkiye'de son zamanlarda düşüş gösteren DYY girişlerinin belirleyicilerini anlama ve bu konuda geniş bir perspektif sunma şeklinde belirlenmiştir. Tüm bunlar ışığında bu tez öncelikle Türkiye’de 2002-2018 yılları arasında yaşanan demokrasideki negatif yönlü değişimi incelemektedir. Daha sonra ise bu değişimin DYY girişlerine olan etkisi tartışılmıştır. Sonuç olarak DYY girişleri ile demokrasi arasında nedensel bir ilişki bulunmamıştır.

Anahtar Kelimeler: Doğrudan Yabancı Yatırım (DYY), Demokrasi, Türkiye, Çok Uluslu Şirketler (ÇUŞ), Makroekonomi

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ABBREVIATIONS

AKP – Justice and Development Party

BA – Bureaucratic- Authoritarian

CEEC – Central and Eastern European Countries

DMC – Daewoo Motor Company

EU – European Union

FDI – Foreign Direct Investment

GDDS – Government Domestic Debt Securities

GDP – Gross Domestic Product

GNP -Gross National Product

HDP- Peoples' Democrat Party

ISIS – Islamic State in Iraq and Syria

KCK – Union of Communities in Kurdistan

MNC – Multinational Company

M&A – Mergers and Acquisitions

MNE - Multinational Enterprises

NGO- Non- Governmental Organization

OECD – Organization for Economic Co-operation and Development

OLI – Ownership Specific Internalization

PKK – Kurdistan Workers Party

TAF – Turkish Armed Forced

TNC – Transnational Company

UNCTAD - United Nations Conference on Trade and Development

US – United States

WEF- World Economic Forum

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INTRODUCTION

The 21st century has been a witness to breakdowns of democracies throughout the world. According to Freedom House report in 2017, rapid decline in democracies has become distinguishable since 2006. Over the last decade every indicator of democracy -electoral process, pluralism and participation, functioning of government, expression and belief, association and belief, association and assembly, rule of law, personal and individual rights- presented a dramatic decline, especially expression and belief ranked the poorest in the world. (Puddington, 2017)

This decline is dedicated to increasing poor performance of established democracies in the west, especially in the US. In the matter of US democracy, the ever-mounting cost of election campaigns, the resurging role of non-transparent money in politics, and low rates of voter participation were the small signs of democratic ill health (Diamond, 2015, p.152). In addition to US, the problems such as unemployment in the aftermath of Europe's economic crisis, gave their places to democratic problems in a very short time such as increasing number of right wing populists along with the nationalist patterns throughout Europe. Briefly, it would be appropriate to claim that the architects and advocators of democracy have become weak in order to promote democracy confidently outside of their boundaries. Failures of US and Euro zone decreased the legitimacy of their democratic system and gave an opportunity to leaders in the emerging markets to undermine democracy and become more repressive. Now the questions are 'Is this going to be a huge threat to today's neo-liberal order? Are open market policies at risk?' In the light of these, according to Freedom House, in the last decade Turkey is one of those countries and performs the fastest decline in the matter of democratic indicators (Puddington, 2017), whereas in the beginning of 2000s it was considered as success story. Hence, my research question formed as 'Does decreasing democracy in Turkey affect foreign direct investment (FDI) inflows -which considered as a main tool of economic globalization?'

Liberals, the promoters of globalization, claim that economic globalization is responsible for spreading democracy, can we blame today's neoliberal economic model for declining democracy throughout the world? Interestingly enough, awareness of this fact indeed represented lately in United Kingdom, the country which gave birth to Liberal idea; now claims that the neoliberal economic model is broken (Asthana, Elgot, & Mason, 2017). In this context, many developing countries affected from these breakdowns, particularly, Turkey.

The main turning point of Turkey's declining democracy has not reached any consensus yet. Some claim that Ergenekon case in 2008 was a remarkable starting point, some suggest that Arab spring played a huge role in changing Erdogan's attitude especially in the foreign policy, others underlines the importance of Gezi protest in 2013 followed by Erdogan's repressive reaction and disproportionate force towards it. Nevertheless, most scholars agree on the fact that 2014 presidential election consolidates Erdogan's power and carry him to the one-man power (Diamond, 2015).

Recently, Turkey faced a failed coup attempt in 2016 and since then Turkey is under state of emergency. Erdogan's response was drastically rough; arrest of 60,000 people, the closure of over 160 media outlets, and the imprisonment of over 150 journalists (Abramowitz, 2018). One arrestment is actually worth to mention specifically. Deniz Yücel, a German journalist arrested for spreading pro-terrorist propaganda in 2017. This caused huge diplomatic problems with Turkey's important partner Germany. However, Yücel was evacuated in February 2018, but the problems between two countries still continued; for instance, German tourists still refrain from political tension between countries. The number of German tourist to Turkey decreased significantly by 30 per cent compared to 2015 (TURSAB, 2018).

Last year, Turkey changed its constitutional framework via referendum for full presidential system. This centralized power in the presidency for Erdogan and weakened Turkey's democracy. Recently, Turkey lacks from freedom of expression and freedom of press, perception for elections are biased, opposition muzzled - the leaders of the third-largest party in the parliament are in prison, and nearly 100 mayors across the country have been replaced through emergency measures or political pressure from the president-, and Kurdish minority despised. Thus, Freedom House changed Turkey's status from partly free to not free in 2018 and referred to Turkey as a 'Illiberal democracy'. After analyzing modern authoritarian states for our century, included Turkey, in the report 'Breaking Down Democracies'; media, academic community, business community, European union, private foundations, mainstream political candidates, human rights organizations and countries are warned against authoritarianism and invited fighting for democracy. At this point, particularly, the task of business community aroused my curiosity. It is recommended that business community should think twice before investing in those authoritarian states and they should stand up against any authoritarian methods such as censorship. These recommendations indeed directly connect with the general liberal thought that claims one of economic globalization task is to spread democracy. Therefore, in this thesis, I chose to analyze Foreign Direct Investment (FDI).

In Turkey, FDI inflows decreases rapidly, especially in the last three years which includes the period of state of emergency. However, despite the decreasing trend of FDI inflows under one-man regime, some huge investments from MNC in Turkey can be still observed in 2017, respectively, Siemens new greenfield investment in Gebze, $184.2 million approved FDI of Bosch and the acquisition of Petrol Ofisi to Dutch Company Vitol Investment. In the light of these, this thesis problematizes the fact that, if multinational companies (MNC) the liberal ideas own products should not support authoritarian states as liberalism dictates, why do huge MNCs invest in countries like Turkey, which are lack of democratic factors? What could be the determinants for FDI in Turkey?

In order to find an answer to these questions; in the first chapter I will discuss the internalization theory which problematize the determinants of FDI in a firm-specific level and after I will examine the literature which argues the determinants of FDI inflows in different perspectives, in the second chapter after I give a brief outlook of Turkey's macroeconomic indicators between 2002-2018, I will analyze their impact on FDI inflows, in the third chapter I will elucidate the process that Turkey has been through from so-called democratization to one-man regime and lastly in the fourth chapter I will discuss the impacts of decreasing democracy on FDI inflows in Turkey. Finally, these will be followed by concluding remarks.

CHAPTER 1

THEORITICAL FRAMEWORK AND LITERATURE REVIEW

1.1 Why Multinational Companies Invest Abroad?

1.1.1 Internalization Theory

In 1976 Buckley & Casson developed ‘internalization theory’. They question why firms are investing in foreign markets rather than licensing. In another words, they question when firms internalize the external market. Their answer based on three main criteria;

(1) Firms maximize profit in a world of imperfect markets.

(2) When markets in intermediate products are imperfect, there is an incentive to bypass them by creating internal markets. This involves bringing under common ownership and control the activities which are linked by the market.

(3) Internalization of markets across national boundaries generates MNEs. (p.33)

According to Buckley & Casson (1976), beside the benefits of internalization there are also some challenging internalization costs for firms. They underline that if internalization costs higher than benefits, then firm does not internalize the imperfect market. This theory gives a wide range of place to internalization costs which determines investment factors. These costs can be listed as resource cost, communication cost, political discrimination cost and administrative cost. First of all, resource cost determines industry-specific factors. Resource cost is the cost of the product and external market’s structure. Second, communication cost determines region-specific factors. If there is too much difference between host country’s economic, social and linguistic structure and the firms’, communication cost become higher. Third, political discrimination cost determines nation-specific factors. While, discrimination against foreign firms raises internalization costs, stable political relations and favorable economic regulations reduces. Last, administrative costs, here firm's ability to organize an internal market plays a huge role. Thus, it determines firm-specific factors.

Although, Buckley & Casson (1976) underline that 'the main emphasis throughout this book is on the industry-specific factors.' (p.34), he points out the importance of interaction between host countries socio-political actors, thus, nation-specific factors with these words;

> The foreign subsidiary may be involved in activities with considerable social and environmental externalities, e.g. training labor, inducing regional migration of workers, depleting unpriced natural resources, etc.
>
> …to become sympathetic to the host-country point of view, and to be adept at assessing to what extent, and in what way, acquiescence in government policy is consistent with, or even enhances, longrun profit-maximization for the firm.
>
> MNEs may find it increasingly important to justify their products and production methods in the light of social criteria endorsed by the host government. An ability to harmonize corporate strategy with these views will be a key ingredient in successful multinational operations (Buckley & Casson, 1976, p.106)

However, Buckley & Casson's (1976) theory explains the post-war pattern of foreign direct investment which claims that internalization happens between capital-abundant countries in need of benefit from host countries' technology or research and development and protecting its own proprietary knowledge.

Henisz (2003) extended Buckley & Casson's (1976) internalization theory by underlining the institutional differences between host and investors country and the ability to manage these differences. Henisz (2003) differs from Buckley & Casson (1976) in a way that he points out the substantial amount of FDI inflows to developing countries. In another words, he suggests that unlike Buckley & Casson (1976) MNC may choose to invest in capital-scarce countries rather than capital abundant countries, moreover countries don't need carry similar socio-cultural norms. According to Henisz (2003), developing countries may include unique risks, however, MNCs task is to define market hazards and minimize them via lobbying actions if firm wants to internalize those market. Henisz (2003) calls this as firm's ability to manage institutional idiosyncrasies. While Buckley & Casson (1976) believe the importance of innovation abilities of firm to overcome market imperfection, Henisz (2003) believe the importance of ability to manage institutional idiosyncrasies.

Buckley & Casson (1976) suggest that intervention of government carries huge risks, but they did not mention that this risk depends on industries. According to Henisz (2003), industries like electricity generation, telecommunications, water, finance, natural resource extraction and transportation services, may carry strong societal values, thus have more intervention risk than other sectors. Henisz (2003) claim that, in the eyes of public, even if those industries should be managed by state ownership, need for capital push governments to privatize those industries. At first glance, domestic firms are favored for privatization. However, since foreign investors has more advantages in raising capital abroad in case of any financial deadlock, governments tend to privatize state-owned companies through foreign capital.

Thus, relationship with socio-political actors covers most part of the Henisz's (2003) study. Although foreign direct investments are required in capital-scarce countries and approved by their governments, expropriation risks are still available for foreign investors. Therefore, MNCs should be able to manage those institutional idiosyncrasies by building up good relations with relevant socio-political actors via successful lobbying and influence strategies. According to Henisz (2003), these relations can be maintained by building direct or indirect ties; first includes direct relations with political or regulatory actor, latter includes embassies, export-import financing agencies, multilateral or regional development banks etc. He furthers this line of argument by underlining that sometimes one political actor can be more credible than host country's legal structure. On the other hand, these political actors would also do their best for MNC investment in order to gain support from public due to lucrative investments. Thus, these kind of good relations with socio-political actors make investments durable and minimize risk of expropriation. Briefly, with successful strategies and good relations based on sufficient knowledge and effective lobbying actions firms can maintain their profits in capitally-scarce countries and benefit from them.

In an extension of Buckley & Casson (1976) and Henisz's (2003) theories, Hadjikhani, Lee, & Ghauri (2008) point out the importance of interdependency between socio-political actors and MNC which governments. According to Hadjikhani, Lee, & Ghauri (2008), this interdependency stem from mutual gain of both sides which governments benefit from multinational investments as multinationals benefit from socio-political actors. First, socio-political actors are interdependent on MNCs' because their market activity increases GNP and creates jobs and develop local industries. Latter MNC's are interdependent on socio-political actors' support for maintaining its competitive position in the market.

Hadjikhani, Lee, & Ghauri (2008) explain the reasons behind MNC's socio-political behavior with respect to this interdependency by 3 concepts: legitimacy, commitment and trust. Firms need socio-political actors' support to gain legitimacy in the eyes of the society, and legitimacy can be achieved only if the society in question trust MNC's good-will. In addition to this, MNC is aware of the fact that socio-political organizations are embedded in media, voters, unions, and people (customers). Thus, MNC shows its commitment to socio-political actors by making long term investment, by knowing the socio-political actors' next action to share these long-term investments with public via the media. According to Hadjikhani, Lee, & Ghauri (2008), this move is inevitable by socio-political actors because they are generally ambitious to show the gains stem from huge investments such as employment and increased economic prosperity in order to gain publics, thus, their political position is maintained. Here, the crucial point is, trust between both sides can only be sustained if socio-political actors gain as well. In other words, while the MNC maintains its competitive position and increase its profits rapidly, the socio-political actors should gain something in return such as economic prosperity or employment opportunities. Thus, trust can be sustained.

As far as we know from Henisz (2003) how MNC manage institutional idiosyncrasies via lobbying, Hadjikhani, Lee, & Ghauri (2008) divide the actions of MNC in two; adaptive and influential actions. According to Hadjikhani, Lee, & Ghauri (2008) when MNC acts adaptive, the investment is generally a weak investment, on the other hand, when a company present influential actions it is obvious that there is a huge investment behind this action. For example, despite the political risks in Turkey, the huge investments from an MNC such as Siemens in Gebze, could mean that those multinationals have an influential factor on socio-political actors and include tight interdependency. In addition to this, Hadjikhani, Lee, & Ghauri (2008) claim that MNCs action could be determined by the acts of socio-political actors' coercive or supportive act.

The study of Hadjikhani, Lee, & Ghauri (2008) is based on a case study which analysis DMC the Korean MNC investment in Poland by in-depth interview. Company's relationships with socio-political actors analyzed in 4 different fields; namely, political actors, trade unions, sectoral employers' union (in this case, EU Automotive Manufacturing Association), and socio-cultural aid organizations in the host country (in this case, Poland). Moreover, Hadjikhani, Lee, & Ghauri (2008) point out the difficulties on demanding an interview from the MNC in question:

> The subject of "the firms' relationships with socio-political actors" tends to be a sensitive area as many firms are unwilling to disclose information on this topic to outsiders. Firms aim to keep the relationship out of sight of public scrutiny, and those who are dissatisfied are afraid of negative publicity. Accordingly, the study started with a survey of more than hundred firms who were asked about their willingness to disclose information on their socio-political networking. The positive responses were few, and, consequently, the study only focused on those who were willing to provide information.

To conclude, according to Hadjikhani, Lee, & Ghauri (2008) study based on internalization theory, I can state that FDI depends on neither general economic nor its democratic indicators of the host country, it depends on direct and private relationship between socio-political actors and MNC. Furthermore, this relationship under huge investments can be beneficial for both parties, namely socio- political actors and the MNC. Therefore, a Korean MNC, Daewoo Motor Company (DMC) invested in an under-developed automotive industry in Poland, which is weak by being a democratic state but has socio-political actors who has strong relationship with DMCs managerial levels. At the end, government strengthen its position in the political area and MNC strengthen its position in the market. Perhaps, this could be the same case in Turkey, behind those huge investments.

1.1.2 Eclectic Paradigm

Eclectic paradigm, in other words, OLI paradigm developed by John Harry Dunning. This paradigm tries to explain the factors of international production. It includes more than one theories particularly internalization theory which I analyzed above, in order to explain MNCs cross-border value adding activities extensively. Thus, Dunning (1993) enhanced internalization theory by adding location-specific factors which emphasis on ‘where to produce’ (p.143). Founders of internalization theory, Buckley & Casson later accept the significance of location specific factors in the late 80's (Dunning, 1993, p.76)

Now I will go into detail by analyzing three factors of OLI paradigm. First of all, if a firm has some unique assets, they called as ownership-specific (O) advantages. These assets can be tangible, intangible or both. Tangible assets are natural endowments and man power and capital; intangible assets or capabilities are technology and information, managerial, marketing and entrepreneurial skills, organizational systems and access to intermediate or final goods of the market. The possessing of firm may not be available in the host country and in that case, firm will have O advantage over the host country (Dunning, 1993, p.77). However, O advantages might be specific to a particular location, which creates the location-specific (L) advantages. The location choice of MNC activity may vary with the type of FDI and the stage of development of both the investing an recipient countries (Dunning, 1993, p.143). Location advantages depends on home countries' cultural, legal, political and institutional environment which they are deployed market structure and government, legislation and policies. The advantages can be resource availability, financial strength, entrepreneurial vision and managerial competence.

Moreover, only having O and L advantages over a country might end up with export or licensing. However, if there is market failure in targeted market, firms are generally willing to carry their value-added activities- i.e. production facility- abroad in order to exploit their O advantages over the market. Thus, in another words, an external market can become an internal market, when it includes market failures which will contribute MNCs profit maximization and this explains the internalization advantage (I). At the end, the interplay of three advantages O, L and I generates the international production via foreign direct investments.

Briefly, if a MNC wants to protect its own possession and develop its O advantages by itself, and not to sell them, MNC might strengthen its monopolistic power over its assets while keeping activities within the firm, which called as internalization. At the end, a location which is available for exploiting those advantages, in other words which carries L advantages is chosen.

1.2 Determinants of FDI Inflows in Country-Specific Level

There have been conflicting explanations with regards to FDI’s determinants in the literature. While conventional approaches claim that MNC’s prefer to invest in democratic countries rather than less-democratic ones and walk away slowly from the countries whose democratic indicators start to decrease, critical approaches argue that within developing countries MNCs chose authoritarian regimes over democratic ones in order to enjoy privileged benefits and present an exploitative behavior.

Jensen (2003) one of the main contributors in the conventional approach starts his research by claiming once an investment had been made by multinational in a foreign market, disinvestment of physical asset is costly such as the disinvestment of production facilities. Therefore, in his study main determinant of FDI inflows to a foreign market is credibility that can sustain the presence of the physical asset in a long term. Jensen (2003) argues that low-political risks make countries credible and can be found in democratic governance. He underlines the importance of political preconditions of the host country that has to be democratic when multinational wants to invest in a foreign market. According to Jensen (2003), from MNCs point of view, the most unfavorable political risks are nationalization and expropriation. He outlines two main characteristics of democracies that leads to decrease those political risks.

First, veto players can sustain political stability by retaining frequent changes on investment policies that has been promised to MNC by socio-political actors. Latter is audience cost that is the fear of losing elections, in case political actors renege on the open market policies that has been given as a promise to public. Thus, he points out that those mechanisms make democracies credible and reduces political risks.

After analyzing 114 countries, both developed and developing, in the matter of how FDI inflows in 90's is affected by economic conditions, policy decisions and democratic political institutions of 80's, he reaches to the conclusion that multinationals avoid investing in authoritarian regimes whose political risks are higher than those in democracies. Although Jensen (2003) found out the same results by controlling developed countries, his study might have been more convincing if he only focused on developing countries. Therefore, Harms & Ursprung (2002) assumptions seems to be more convincing in the way that they only focused on developing countries and paid attention to exploitative behavior of MNC. However, they maintain the traditional liberal argument that MNCs care about political right and civil liberties and don't exploit the politically and economically repressed workers in developing authoritarian countries, therefore prefer to invest in democracies where those rights are protected. Thus, Harms & Ursprung (2002) disagree with the activists who are against to economic globalization and who accuse multinationals for hurting environment, exploiting workers and disregarding civil society's concerns. As opposed to anti-globalists, they claim that individual freedom is an investment decision criterion for MNC in a foreign market. Harms & Ursprung (2002) underline that this individual freedom consists developed worker rights and organized labor that are located in democratic countries which have developed unionization mechanisms. They attribute this decision criteria of multinational to the need of educated labor due to the increasing technology and its requirements to skilled labor rather than unskilled that has undergone exploitative behavior of MNCs back in the days.

Harms & Ursprung (2002) come to the conclusion that although economic freedom is a prerequisite for foreign direct investment, lack of civil liberties deters FDI. Thus, they claim that globalization and human rights can go together. In addition to Harms & Ursprung (2002), Jakobsen & de Soysa (2006) are also the one who support the argument of 'free market and democracies go together'. They begin to support this argument by challenging Li & Resnick (2003) theory which claims that when property right protection is controlled, multinationals choose authoritarian regimes over democracies.

Three of Li & Resnick (2003)'s arguments have been criticized by Jakobsen & de Soysa (2006) and can be listed as, better conditions in authoritarian regimes in order to strengthen MNCs monopolistic or oligopolistic position, more incentives in authoritarian regimes and restrictive behavior of local business representative in democracies due to wide political participation. In another words, theory of Li & Resnick (2003) 'decreasing democratic institutions increase FDI inflows in developing countries', is deliberately criticized by Jakobsen & de Soysa (2006).

First of all, Jakobsen & de Soysa (2006) find monopolistic market opportunities as a self-defeating argument. They underline that if one MNC enjoys monopolistic profit, on the other hand, it prohibits others to share the profit, hence it does not lead to more FDI inflows as Li & Resnick (2003) claims. Second, abundant incentives which Jakobsen & de Soysa (2006) call 'sweet deals' do not always have to attract FDI, according to them, if multinational's priority is skilled labor no other condition can make multinational to stay in authoritarian regime that is lack of skilled labor and full of generous incentives packages. Jakobsen & de Soysa (2006) also point out that high-tech industries abound with skilled labor are also in a competition with each other to attract more FDI inflows, hence offer generous incentives as well as authoritarian regimes. Lastly, they claim that in democracies majority of representative support free-trade policies while in authoritarian regimes representatives consist of narrow-local capital who tend to be more offensive against to foreign capital than the one in democracies and they underlined that rent-seeking behavior of domestic capital is less observable in democracies.

Briefly, as opposed to Li & Resnick (2003) what Jakobsen & de Soysa (2006) suggest is, conditions caused by decreasing democratic institutions do not lead to higher FDI inflows. In addition to this, Li & Resnick (2003)'s variable of 'democratic institutions' is also criticized by them that it underestimates the pure importance of democracy. Beside challenging Li & Resnick (2003)'s argument, Jakobsen & de Soysa (2006) claim that government preference does matter for MNC. Moreover, according to them, leftist governments among democracies get more FDI inflows than rightist-democracies. To sum up, according to Jakobsen & de Soysa (2006), there is more important criteria for foreign investors than property right protection. They suggest that competitive markets, skilled labor, less-rent seeking environment, preference of government are the most crucial factors which determine the investment location. Therefore, according to them, democracy and open market policies go hand to hand.

Although Busse (2003) also claim that MNCs prefer to invest in democracies rather than authoritarian, he accept the fact that in 70's and in the beginning of 80's the situation was different. Thus, he underlines the changes over time on MNCs behaviors. According to Busse (2003), these changes happened by two developments, first, sectoral changes and second increasing awareness in the public against to multinationals exploitative behavior via Non-Governmental

Organizations (NGOs). Busse (2003) explains the first reason by claiming that the international production shifted from primary goods to manufacturing and services by the time, thus, in the 90's MNE became less interested in countries who are only rich by resources and more interested in to countries whose industry is more developed or whose market is bigger or whose geopolitical position is more advantageous with respect to exports and imports. He furthers this by claiming that those countries whose industry is not only based on primary goods tend to have more developed political rights and civil liberties than those whose industry is only based on primary goods. Therefore, he states that increasing interest on developed manufacturing industry and services, also increased the FDI flows to democratic countries among the developing countries.

According to Busse (2003), second reason why MNEs investments are falling down in repressive regimes can be explained increasing effectiveness of NGO activities against to foreign investors. He explains that the technology that gives advantages to MNC to enjoy profits in the low-cost repressive countries also gives advantages to NGO such as developed global information system, internet. Busse (2003) claims that NGO's create awareness in the public via developed information systems, thus, they pay attention to MNCs' activities to invest in repressive regime, which can be interpreted in to indirectly supporting those regimes that ignores political rights and civil liberties. Therefore, in order to avoid negative publicity, consumer protest and decrease negative publicity, MNC starts pull away from repressive regimes as Busse (2003) argues. Busse (2003) gives an example which proves this situation clearly, in 1988 dictatorship in Myanmar took over and the FDI flows in 1997 fell from US $ 387 million to US $ 123 million in 2001.

Last but not the least, according to Busse (2003), MNEs behavior has changed during the time and they started to invest in democracies more than before. Especially, he finds out that in 90's MNEs choses democracies over authoritarian. The year we are living in is 2018 and such investments to those authoritarian countries are increasing rapidly in the last 10 years. Based on Busse (2003)'s study, it wouldn’t look absurd to suggest that MNC point of view could have changed in the last 10 years and there may be other reasons can be found in authoritarian states which make MNCs to invest in authoritarian states rather than democracies. Those reasons are explained by critical thinkers who believe that authoritarian countries have superiority over democracies among developing countries.

While traditional approach claims multinationals priority of choosing democratic governments as an investment area, critical approaches assert the contrary and claim that they do not seek for democracy, but economic advantages thus chose authoritarian states over democracies. Dependency school was the first criticism against to multinational companies, in other words, to FDI. They rise against to modernization theory that claims one of the purposes of MNC is to go under-developed countries to carry them in a developed level via technology, investment and employment. Dependency school agree to the fact that multinationals go under-developed countries but disagree on multinationals good will of contributing host-country's development and leading its modernization.

O'Donnell (1978) from dependency school draws a distinction between political and economic development. In his study he focuses on Bureaucratic-Authoritarian (BA) states in Latin America and he claim that transnational companies (TNC)may bring economic development to those BA states but unusually bring political development such as democracy. According to O'Donnell (1978) TNCs main purpose is to reach maximum amount of profit and only way to do it is to exploit host countries resources such as labor. He points out the need of TNCs which are repressed worker rights and economic openness, therefore, they need to cooperate with authoritarian states. In addition to this, according to O'Donnell (1978) BA states help those TNC to profit in a maximum amount by excluding popular-domestic sector from production process and political area. He furthered this by claiming beside reinforcing TNCs profit, BA had to maintain continuity of profits in the future for the maintenance of TNCs continuity within the country. According to O'Donnell (1978), BA states prepare those favorable conditions in return of deepening of the production structure' by TNCs investments within the country which must lead to economic development. O'Donnell (1978) calls this relationship between BA states and international capital as 'mutual indispensability', in addition to this he suggests that this trade-off comes with a social cost.

Moreover, O’Donnell’s (1978) theory shows how workers’ rights are diminished, domestic sector is eroded, media is repressed, and political repression is viciously applied to public for the sake of international capital investments. At the end, it could be indicated that neither international capital comes to democracy, nor it brings democracy. However, Oneal (1994) argued that if MNCs benefited from those suppressive regimes as O'Donnell (1978) claims, companies must have earned extremely high rates of return in those authoritarian countries when we compare with other democratic countries. Therefore, beside analyzing the effects of regimes on FDI flows, Oneal (1994) also analyzed the effects of regime on multinationals’ profitability.

Unfortunately, Oneal (1994)’s study is restricted with only US investors, on the other hand, its sample size is enriched by 22 developing and 26 developed countries. As opposed to liberal thought such as Jakobsen & de Soysa (2006), Oneal (1994) finds out that regime type is not significantly correlated with FDI flows, where profitability is significantly correlated with FDI flows. He claims that among whole countries, developing and developed, FDI profits best in developed democracies, on the other hand, among developing countries multinationals earned greater in authoritarian countries.

Furthermore, Oneal (1994) compares BA regimes with other previous authoritarian regimes in the same country and at the end he cannot find any distinctive feature of BA regimes, which multinational creates better profits than previous authoritarian regimes as O'Donnell (1978) claims. Briefly, according to Oneal (1994) foreign investors are not making their choice of where to invest according to host countries regime type, however, among developing countries, they profit best in the authoritarian regimes. In addition to this, he also points out that those results can change depend on the region, for example, in Asia multinationals profits best in democracies. He concludes by suggesting all good things don’t go together as opposed to conventional liberal perspective.

As opposed to Oneal (1994), Li & Resnick (2003) find out the significance of regime type on FDI inflows. They claim that democratic institutions can be obstructive against to foreign investors. However, according to their study, property right protection has priority over regime type. In other words, MNCs choose authoritarian regimes over democracies, when property rights are controlled.

Li & Resnick (2003)’s study is based on Dunning's eclectic paradigm that explain why firms invest abroad. According to Dunning's eclectic paradigm, foreign investors decide on firms’ location where they can enhance their ownership and internalization advantages. However, Li & Resnick (2003) claim that democratic institutions don’t allow these enhancements due its wide political participation and its tendency toward local business man. Thus, Li & Resnick (2003) highlight that those institutions seek to reduce MNCs monopolistic or oligopolistic power over the market.

According to their study, the reason behind politicians’ restrictive behavior against to foreign investors is re-election desire, therefore they favor local business man over foreign investors to guarantee their future votes. Due to same reasons, democratic institutions also do not offer generous incentives to MNC as Li & Resnick (2003) point out. Thus, according to Li & Resnick (2003) democratic institutions expel foreign investors to less-democratic countries who has limited pluralism and biased in favor of narrow elite control over public policy. Li & Resnick (2003) argue that those narrow elite strata don’t protect local industry as much as in democracies and mind their own business that is benefiting in an optimum level from foreign investments. Hence, autocratic states provide generous incentives, tax holidays and some privileges more than democracies as Li & Resnick (2003) suggest.

They also add that less democratic countries tend to be also the less developing ones; therefore, those countries crave for FDI inflows in order to strengthen their economy and this makes them co-operate with MNC by meeting their demand such as strengthening their monopolistic position over the market. Thus, according to Li & Resnick (2003) foreign investors are attracted by autocratic states.

However, there is one exception, Li & Resnick (2003) find out that If an autocratic state doesn't have protected property rights, then investors will definitely choose democracies whose property rights are generally protected. On the other hand, if authoritarians develop their property rights protection laws, then democracies don't have chance any in front of foreign investors eyes as an investment area. Gehlbach & Keefer (2011) also highlights the importance of property rights in authoritarian states. They claim that ruling party institutions in an authoritarian country can guarantee property right. Thus, according to Gehlbach & Keefer (2011), the credibility that Jensen (2003) points out can be gained by those institutions just as in the case of China.

Mathur & Singh (2013) disagree with the finding that property right protection is the only important criteria for MNC. They claim that MNCs consider other economic indicators as well as property rights, before making their investments in a host country. Mathur & Singh (2013) analyze net inward FDI between 1980-2000 to developing countries and they find out that regime type is not significantly correlated with FDI. Hence, they reject the theory of reinforcing democratic institutions in order to get more FDI inflows in developing countries. According Mathur & Singh (2013), investors are not attracted by political freedom but economic freedom. They further this by claiming improving political rights for citizens are not an automatic guarantee for economic freedom which multinationals seek for, on the other hand, property rights, tax rates, capital controls, trade openness are direct guarantee of economic freedom.

Thus, as opposed to Li & Resnick (2003), Mathur & Singh (2013) underline that only property rights are not sufficient to guarantee economic freedom. Hence, according to Mathur & Singh (2013), FDI can go to any authoritarian regime that provides all those economic freedom, even if the country is lack of freedom of thought or has biased elections. A strong example from their study disproves Oneal (1994) argument that in Asia multinationals choose democracies over authoritarian among developing countries. Mathur and Singh compare China and India; first is an autocratic regime and latter is ruled by democracy. They find out the FDI inflows to China is 17 times bigger than India. Thus, it is very appropriate to claim that all good things do not necessarily go together.

1.3 FDI Inflows in Turkey

Before going further with the determinants of FDI inflows in Turkey, it should be known how crucial FDI's role on Turkey's economy is. Economic globalization sustains capital investments between countries, therefore it is particularly advantageous to Turkey where national savings are inadequate. Thus, just like other developing countries, Turkey must do its best to attract foreign investors. Foreign capital investments are divided in two; direct (foreign direct investment), indirect (short-term capital investments). Direct investments contribute more than indirect investments to host countries. It provides economic growth, employment and technology (Kula, 2003). However, in the matter of economic growth, there is conflicting results in Turkey's literature. Some claim that FDI does not affect economic growth in Turkey (Aslanoğlu, 2002; Alıcı & Ucal, 2003; Alagöz, Erdoğan, & Topallı, 2008; Kula, 2003), some claim FDI's positive effect on economic growth (Ozan & Şen, 2010; Kahramanoğlu, 2009; Ekinci, 2011). At the end, the majority is of the opinion that although FDI generally has a positive effect on economic growth, however, it does not contribute to Turkey's economy as it is expected.

In Alagöz, Erdoğan, & Topallı's (2008) study it is stated that the number of existing companies' aquisitons are more than the new facilities established by foreign investors due to mass privatization in Turkey, therefore, FDI doesn't contribute to economic growth despite the increasing number of MNC. Mucuk & Demirsel (2009) agree that greenfield investment should be encouraged if higher economic growth is aimed. On the other hand, Ekinci (2011) claim that FDI has a positive effect on economic growth but don't have any effect on employment which is supposed to have in a first raw due to M&A. The reason behind non-increasing employment rate explained by Saray (2011) that FDI concentrated in limited employment capacity sectors such as finance, communication and transportation.

On the contrary, Kahveci & Terzi (2017) argues that FDI, indeed, seeks economic growth in Turkey. In another word, for them FDI is not the cause but the result of growth. In addition to this, it is underlined that FDI supposed to bring employment and technology to the host countries, however, according to Kahveci & Terzi (2017), the technology that MNCs bring could reduce the need for workers, thus, reduces firms' costs. It increases the competitive power of MNCs against the local firm and the local firm might also go downsizing in order to strengthen its competitive power. At the end, FDI might even decrease the employment rate in Turkey especially if the type of investment is M&A. Kahveci & Terzi (2017) conclude that FDI neither affect growth nor employment positively in Turkey. They suggest that better conditions should be sustained in the matter of political and economic stability for attracting greenfield investment which has more efficient for Turkey's economic growth than M&A.

According to the literature, FDI can contribute to Turkey via capital accumulation, employment and modern technologies. Unfortunately, it does not have any remarkable impact on employment and economic growth. The reason behind this attributed to the M&A type of FDI and preferred sectors which lacks employment capacity. After reviewing the literature on the impact of FDI inflows in Turkey, I will now go further with the determinant of FDI inflows. The aim is to find a correlation between the democracy in Turkey and FDI inflows.

1.3.1 Determinants of Turkish FDI Inflows

Throughout the empirical evidences, one might observe that the studies on determinants of FDI inflows mostly concentrated on economic factors in Turkey. Thus, it is suggested that having a strong economy is enough to attract high levels of FDI inflows.

Due to the majority of European Union countries in Turkey's FDI inflow mix, the determinants of EU's FDI inflows has been analyzed in Atik (2005)'s study. She analysis the period of 1991-2003 and find that GDP per capita, credit from international organizations and infrastructure investments affect FDI inflows positively. Moreover, it is stated that the customs union agreement with EU in 1996 rises expectations for more FDI inflows, however, FDI inflows stayed lower than it is expected. According to Atik (2005) the reasons behind this fact are low rate of GDP per capita and infrastructure investments. Last but not the least, unexpectedly, Atik (2005) finds that terrorist attacks do not affect EU FDI inflows. Karagöz (2005) furthers the questions why FDI inflows are lower than expected even after EU agreement and he finds that the importance of trade openness and the previous investments on FDI inflows. Karagöz (2005) claims that only the success of previous investments and increase in exports would be sufficient to increase FDI inflows to Turkey. In addition to this, Turan Koyuncu (2010) suggests the same results with Karagöz (2005) and underlines the importance of political stability.

After 24 January 1980 decisions Turkey began to apply open market policies and get in the competition with other developing countries to attract foreign investors rapidly. Thus, first incentive certificates were presented to foreign investors in 1980. Gürler Hazman (2010) analysis the effects of those incentive certificates on foreign direct investments till the year of 2007. However, according to Gürler Hazman (2010) incentives couldn't reach the target and couldn't succeed to attract sufficient amount of FDI as it is planned. Gürler Hazman (2010) finds incentives weak, therefore, suggests tax reforms and more comprehensive incentives. She also underlines the fact that only the incentives are not enough to pull more FDI inflows; better conditions are necessary in the matter of economic and political instability, the appreciation of currency, complex tax system and bureaucratic obstacles. However, Öz & Buyrukoğlu (2017) find the positive effect of investment incentive policies on the employment growth. It is stated that incentive packages are comprehensive enough and have a positive effect on Turkey's economy. However, according to Öz & Buyrukoğlu (2017) the impact of incentives packages is unfortunately insufficient on FDI inflows. They find that rather than incentives, Government Domestic Debt Securities (GDDS) interest rates play a crucial role on foreign investors. Therefore, they conclude that although the incentive packages are finally well comprehensive, the reason behind its insignificance on FDI inflows is foreign investors priority interest on GDDS.

Vergil & Çeştepe (2005) find the direct effect of real exchange rate on FDI inflows. However, it is underlined that the real exchange rate volatility doesn’t have any impact on FDI, while a depreciation of Turkish Lira leads to an increase in inflows in Turkey. According to Vergil & Çeştepe (2005) instability do effect FDI inflows negatively but in the matter of general economic instability of the country which is measured by GDP volatility. Moreover, Bayar & Kılıç (2014) find the significance of sovereign credit ratings on FDI inflows. In other words, high credit rates lead more FDI inflows Bayar & Kılıç (2014). However, they underline that decrease in FDI inflows based on decreasing credit rate does not happen instantly, it is affected negatively by the volatility of credit rates over time. Moreover, if credit rating agencies evaluates institutional efficiency, political risk and major macroeconomic indicators, it would be right to claim that Turkey should be more careful on the volatility of those indicators in order to attract FDI inflows. Besides, since Bayar & Kılıç (2014) also find out two-way causality between FDI inflows and credit rating agencies -only S&P and Fitch-, increasing FDI inflows can also increase credit ratings, that at the end leads more FDI inflows. The main determinant of FDI inflows in Turkey has been found to be market volume by Çiftçi & Yıldız (2015).

Aydoğan (2017) compares Turkey with the Central and Eastern Europen Countries (CEEC) between the period of 1990-2013. She tries to find an answer to the fact that Turkey recieves less FDI inflows than the CEEC despite their huge smilarity on macroeconomic indicators. She reaches to an outcome that Turkey’s current account deficit is the highest among CEEC. According to her, the current account deficit of Turkey creates an economic risk for foreign investors. Nevertheless, she points out the sharp increase in FDI inflows during 2000’s and attribute this to attained political stability after conflicting coalitions for a long time.

Despite the limited number, political determinants on FDI inflows has also been studied in Turkey's literature. Şanlısoy & Kök (2010) analysis the political instability of Turkey between the years of 1984 and 2007 and its effect on economic growth. They find the negative effect of political polarization, military coups, terror attacks, corruption, economic instability, ethnic conflicts, government stability and anti-secular pattern in politics on economic growth. The causality between growth and foreign direct investment is explained by claiming that political instability creates an uncertain environment for the future and decreases foreign investor's trust, thus decreases economic activities and decreases growth. Şanlısoy & Kök (2010) point out the positive effect of stability of AKP government on economic growth between the period of 2002-2007, on the other hand, they underline the increasing social segregation and cultural fragmentation for the same period, which creates uncertainty for the medium and long term. Thus, they underline that long-term political stability can be attained only if it is based on improved democratic indicators.

Uzgören & Akalın (2016) analysis the effects of macroeconomic indicators and democracy on FDI inflows in the period of 1991-2012. According to their study, while the real income per capita has a positive impact, democracy has a negative effect on Turkey's FDI inflows. In addition to this, Uzgören & Akalın (2016) also find the negative effect of labor productivity and tax increases on MNC. At this point they are agree with Li & Resnick (2003) and claim the tendency of MNCs' towards less-democratic or autocratic countries. According to Uzgören & Akalın (2016) this tendency caused by autocratic governments' irresponsible attitudes towards the voter which end it up providing more generous incentive packages to the foreign investors, restricting union workers' rights and contributing MNC's activities to improve their monopolistic or oligopolistic power. Thus, it is appropriate to claim that the outcome of increasing labor productivity and its negative effect on FDI inflows undoubtedly caused by foreign investors dissatisfaction about any possible increase on wages.

The effect of corruption has been found to be highly significant on FDI inflows by Tosun & Yurdakul (2016). They claim that the increasing FDI inflows between 2002-2008 was affected by the corruption level of the country, which named as mid-level corruption during the EU negotiations. With their findings they support the theories that calls bribery or corruption as a helping hand to foster FDI inflows or efficient grease. Therefore, it is stated that any increase in corruption level may cause an increase in FDI inflows. They also find that EU negotiations has a positive effect on FDI inflows. Moreover, it is found that MNCs motivations in Turkey based on market and efficiency seeking. On the contrary, Kızılkaya & Ay (2016) find the opposite results in the matter of corruption by analyzing 10 developing countries between the period of 1995-2013. At the end, for Turkey they point out the depressing effect of corruption and democracy level on FDI inflows, while the results for other countries can be change.

After reviewing the literature, it can be said that Turkish FDI inflows are mostly in the form of M&A investments due to the mass privatization policies. Moreover, flows are mostly concentrated in the sectors which has limited employment capacities such as fiancé, communication and transportation. This actually already proves the market and efficiency seeking pattern of FDI inflows in Turkey. Therefore, it would be appropriate to claim that macroeconomic performance of the country more important than the democratic factors for foreign investors. The reason of limited number of studies on the impact of democratic indicators on FDI inflows might be explained by this fact. Hence, in the next chapter I will analyze the macroeconomic outlook of Turkey.

On the other hand, the studies which analyze the impact of democracy on FDI inflows gives conflicting results just as in the general literature. However, latest study on this topic, Durmaz (2017) suggest that increasing democratic institutions will lead to more FDI inflows. The study contains the period 1977-2011, however, Turkey is rapidly losing its democratic structure since 2011. In this case it is expected that as democracy decreases it creates the diminishing effect on FDI inflows. Thus, after I analyze the macroeconomic outlook of Turkey, in the following chapter I will analyze the changing structure of democracy.

CHAPTER 2

MACROECONOMIC OUTLOOK OF TURKEY AND FDI INFLOWS

Unlike the general literature review, in the previous chapter, the majority of Turkish scholars agree on the significance of stable macroeconomic conditions on FDI inflows rather than democratic structure. In addition to this, they also point out the importance of political and economic stability of the country in order to attract more FDI inflows. Therefore, in this chapter I will analyze Turkey's macroeconomic indicators and its effect on FDI inflows during AKP government which is in power since 2002.

2001 crisis was a game changer for Turkey which gave rise to a political party called Justice and Development (AKP) which will stay in the government for more than 15 years. The adjustment program for the crisis recommended by the IMF, the Transition to a Strong Economy, formed the backbone of AKP's economic policies (Akçay, 2018). The new economic liberalization was based on tight monetary policy, the liberalization of labor markets and the privatization of state enterprises (Akçay, 2018). With this program AKP was able to lower and stabilize the 30 years of long chronic inflation and reach single digit inflation rates. Thus, double digit inflation rates came to an end in 2004 with 9.3 per cent (Yeldan & Ünüvar, 2016). In addition to this, the average growth rate of GDP was 7.5 per cent between 2003 and 2007 where it was 4.6 per cent between 1993 and 2013 (Sungur, 2015).

Inflation and GDP growth rate have been hailed as two main success criteria for AKP government. In addition to this, party's new economic agenda successfully reduces Turkish public debt from 76.1 per cent of GDP to 28.2 per cent between

2001 and 2017 (Akçay, 2018). AKP also could go further with the Europeanization process. For instance, the negotiations for the full EU membership had started 3rd October 2005 (Atik, 2005). At the end, Turkey gets $ 22 billion dollar of FDI inflows in 2007 and hit its historical record (UNCTAD,2018).

These developments affected the western media as they called Turkey a successful harmonization of moderate Islam and neoliberal policies (Akçay, 2018). However, this so-called success story did not last too long; unemployment and current account deficit began to increase gradually, growth rate of GDP slowed down after 2011, inflation rate met back with double digits, foreign policy turned from peaceful to assertive and more importantly democracy suffered severe losses. In addition to this, the country faced two recessions; first one was in 2009 after the global financial crisis, the latter was after the coup attempt in the third quarter of 2016. The effect of this economic turmoil on FDI inflows during the AKP government will be analyzed in three periods according to the periodization of Öniş (2015); golden age, stagnation and declining.

First, I will analyze the golden age of AKP between the years of 2002 and 2007. In this period, the strength of AKP was based on high growth rates and low inflation rate, therefore AKP's economic policy is called transition to a 'strong economy' (Akçay, 2018). This economic policy was reinforced by the democratization process in the domestic affairs and peaceful attitude under 'zero problem with neighbor' slogan in foreign policy. The successful harmony of economy, democratization and foreign policy, maintained AKP's power with the help of Europeanisation process (Öniş, 2015).

As so-called success criteria of AKP, GDP reached the highest growth rate with respect to 9.7 per cent in 2004 (TCMB,2018). Inflation rate fell even under the targeted rate of 8 per cent with 7.7 per cent in 2005 (Yeldan & Ünüvar, 2016). Nevertheless, two huge problems began to rise in Turkey's macroeconomic scene in this period; unemployment and current account deficit.

First of all, when the growth rate reached its peak point with 9.7 per cent in 2004, unemployment rate rose up to 10.8 per cent for the same year, thus, rapid rates of growth for this period called as jobless-growth (Yeldan & Ünüvar, 2016). Second, current account deficit has been omitted for the sake of high growth rates under AKP government. Especially during the so-called golden age current account deficit increased rapidly. Between 2001-2002, current account deficit as a percentage of GDP was -1.43 and it raised up to -4.75 by the end of 2008.(Yeldan & Ünüvar, 2016).

It would be appropriate to claim that while Turkey is known as a successful harmonization of moderate Islam and neoliberal policies, some macroeconomic indicators are getting worse in this period. However, despite the deteriorating indicators in this period, FDI inflows reached the highest amount ever (see Figure 1). Therefore, rather than macroeconomic indicators, the huge amount of FDI

Figure 1: FDI Inflows to Turkey, 2002-2017 in US $ Million by UNCTAD[1]

Source: UNCTAD, 2018

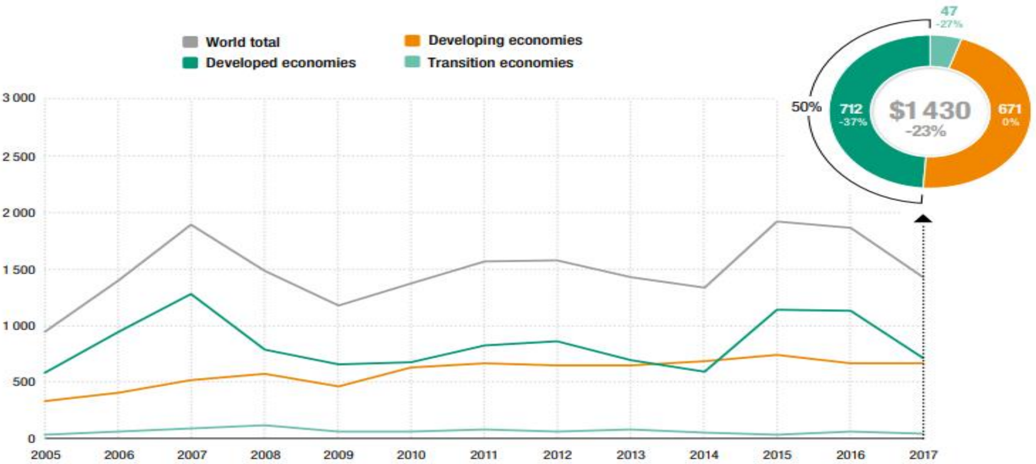
inflows can be attributed to boosted neo-liberal policies reinforced by IMF adjustment program. Specifically, reduced wages and increasing privatization

[1] In December 10,2016, TUIK changed the calculation method of GDP (TUIK,2016). The level of macroeconomic indicators from previous years has been through a change. FDI seems to be one of them. Especially after 2014, TCMB and UNCTAD data on FDI inflows do not match for Turkey. Therefore, in this thesis, two kinds of data were used for FDI inflows. UNCTAD data was used to compare Turkey fairly with other countries. TCMB data was used when only Turkey was observed; for example, in the beginning of chapter four, when FDI by sectors or countries were analyzed for Turkey.

actions can be the pull factor of FDI inflows for this period. Moreover, the global economic conjuncture also plays a crucial role. Before the 2008 crisis, FDI inflows peaked in every group of economies just like in Turkey (see figure 2).

In addition to this, the relationship between FDI and GDP growth stays questionable for this period. It seems that there is a positive correlation between FDI and economic growth, which both have high rates, however, any causality can be claimed by only considering one period of AKP. In another words, high rates of economic growth cannot be claimed as a pull factor of increasing FDI inflows in Turkey during the so-called golden age. Because, maybe the FDI inflows is the reason of GDP growth in Turkey.

Figure 2: FDI Inflows, Global and by Group of Economies, 2005-2017 (Billions of dollars)



Source: World Investment Report, UNCTAD, 2018

Stagnation period for AKP starts from 2007 and continues until 2011 (Öniş, 2015). This period is remarkable with the global financial crisis in 2008 and its impacts on Turkey’s economy. Turkey affected dramatically by the crisis, even though Erdoğan, the prime minister of the period, asserted that the crisis slightly touched Turkey (Milliyet, 2008). First of all, in 2008, Turkey’s GDP stayed stagnant according to the previous year and shrank by 4 per cent in 2009 (TCMB,2018). Latter FDI inflows fell by half in 2009 (see figure 1). In this context, it can be stated that foreign investors ran out of the country after the crisis. It is obvious that the considerable amount of FDI outflows from Turkey stems from the global conjuncture which includes the financial crisis but not from Turkey's country specific factors. This can be seen by looking at world's FDI inflow trend for the related period. The sharp decrease in the FDI inflows from 2008 to 2009 is observable for every group of economies (see figure 2). To sum it up, the sharp decrease in 2008 was not caused by Turkey's macroeconomic indicators but the economic crisis in the world. Moreover, this crisis not only affect FDI inflows for the following year but also the whole period after 2008 until today (see figure 2). After 2008, FDI inflows in Turkey has never reached the levels in the golden age. However, it recovered fast together with the economic growth until 2011.

When we look at macroeconomic indicators for this period, it could be easily stated that Turkey performs poorly. First, the inflation rate was not as inspiring as the previous period. It went back to double digit with 10.8 per cent in 2008, moreover, it was highly volatile and always above the targeted rate for the whole period except in 2010 (Yeldan & Ünüvar, 2016). Second, the current account deficit increased at an alarming rate reaching $ 77 billion in 2011 (TUIK, 2012). Lastly, unemployment climbed up to 14.8 per cent and saw the highest level in the first quarter of 2009 (TCMB, 2018). In addition to this, when current account deficit has the poorest numbers, first in 2008, latter in 2011 (see Appendix), the amount of FDI that Turkey receives was not the poorest. If FDI inflows in a country do not affected from any worsening in the macroeconomic indicators such as increasing current account deficit, no one can claim the causality of macroeconomics and FDI. Therefore, I would not explain the general slowdown in FDI inflows for this period with the poor macroeconomic performance of Turkey. The negative effect of global financial crisis seems more significant here.

After the surges in 2010 and 2011, GDP growth recedes in the following years, hence, Turkey becomes part of the culminating great recession (Yeldan & Ünüvar, 2016). Therefore, the support for AKP government, which based on the continuation of economic growth, begin to decline slowly and AKP gets into the declining period (Akçay, 2018). When we look at FDI inflows, in 2012, they decline after the sudden increase in 2011 and in the following years FDI inflows stay stagnant until 2015 (see figure 1). In the period between 2011 and 2015, ongoing problems in the macroeconomics also stay stagnant such as unemployment and current account deficit (see Appendix). However, just after the peak on FDI inflows in 2015 Turkey gets into a period of increasing political turmoil. On 15 December 2016 Turkey experienced a failed coup attempt. This was followed by a recession in the third quarter of 2016 by 1.8 per cent (TUIK, 2016). Moreover, in November 2017, inflation rate raised up to 12.98 per cent and this was the highest rate of inflation since 2003 (BBC, 2017). Thus, the two main castles of AKP -inflation and economic growth- fall.

Moreover, the US dollar, which has been on the rise since 2013, increased rapidly with the depreciation of Turkish Lira (TL) after the failed coup attempt. The US Dollar which was around 2.8 TL before the coup attempt, has reached 3.5 TL at the end of the year 2016 and now it is around 4.2 (TCMB, 2018). At the end, S&P which is a significant determinant of foreign investments in the host countries, changed Turkey's rating from B to B- in July 2016 (Cullinan, 2018).

In the light of this, FDI inflows in Turkey decreases after 2015. At the first glance, this decline can be attributed to global conjuncture in the matter of international production which slowdowns in the recent years. Nevertheless, this decline mostly concentrated on developed countries especially during 2017. Developing countries do not affected from the slowdown as much as developed countries, instead FDI inflows to developing countries stay stagnant. However, unlike the other developing countries, Turkey's FDI inflows decline in a considerable amount after 2015. Therefore, it would be appropriate to claim that the slowdown in Turkey's FDI inflows carry unique parameters for this period.

Moreover, just like the sudden fall in FDI inflows in 2009, the fall in 2016 happened after the recession. Hence it can be stated that there is a positive correlation between FDI and GDP. However, after the recession in 2016, Turkey catches a high growth rate in GDP with respect to 7.5 per cent (TCMB,2018) but

FDI inflows still continued to fall. This rejects the theory that FDI seeks economic growth. On the other hand, it confirms the significance of Vergil & Çeştepe (2011) that FDI inflows are affected negatively from GDP volatility. Hence, it would be appropriate to claim that slowdown in GDP does not directly affect FDI inflows, but the economic instability affects FDI inflows negatively.

It is also well known that the economic instability occurred under the recent political turmoil in the country. Thus, the reason behind the decline in FDI inflows seems political as much as economic. Except GDP growth, when macroeconomic indicators have performed poorly in Turkey since the beginning years of AKP, FDI inflows could hit historical records. FDI inflows were going parallel with the global trends, however, in the last 3 years, flows are not going parallel with the conjuncture (see figure 1 and 2). Turkey performs poorly compare with its region and other developing countries. Therefore, the determinants of low level FDI inflows is unique for Turkey in the last 3 years. In these years, the most remarkable change happened in the political stability and GDP growth rates. Hence rather than macroeconomic indicators, those factors are more significant to explain this recent slowdown.

Till this point, I first presented the fact that Turkey was called strong economy and got high level of FDI inflows despite its poor macroeconomic condition. Then, I tried to show the breakdowns after the golden age of AKP. This breakdown was largely stem from the slowdown in GDP after 2011. Change in GDP growth rate was followed by other problems such as double-digit inflations and high unemployment rates. I will now analyze the reasons behind this fragility of Turkey's economy, thus, the volatility of GDP.

One of the main reason behind this slowdown was the policy response of the US to the 2008 financial crisis. When Fed declared that it would cut back its easy money policy and increase interest rates, Turkey was faced with a high amount of capital outflows to US market (Akçay, 2018). Turkey was dramatically affected by these outflows because its economy was highly dependent on hot money flows.

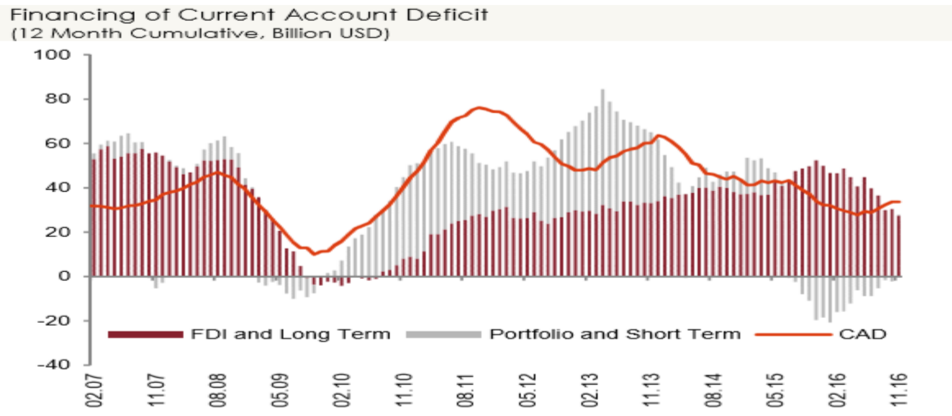
In the post-2001 crisis Turkey was pressured to keep its interest rates at the high level by the IMF program in order decrease inflation. Although, Turkey successfully reached the targeted inflation rates between 2002-2006, interest rates still continued to stay over the average of other developing countries. Therefore, foreign capital inflows increased rapidly in Turkey. Thus, during AKP government GDP growth was sustained by short-term foreign capital rather than industrial production. This indeed clarifies the high growth rates of GDP in the first years despite the increasing rate of unemployment and current account deficit. Thus, the economic growth sustained by AKP government was called as speculative led-growth. (Yeldan & Ünüvar, 2016)

Another problem is, when macroeconomics are managed by finance instead of real sector, problems begin to arise and the economy becomes fragile to foreign exchange speculations. The share of agriculture in GDP decreases from 12 percent in 2000 to 9,2 percent in 2011, in other words, agricultures growth rate is diminished rapidly year by year since the beginning of 2000's (TUIK, 2012). In addition to this, the industry is not as developed as much as the service sector where it supposed to be the strongest part of the GDP as a developing country. Especially, when there was a peak in the economic growth with 9 percent in 2004, industry calculated as approximately the half of service sector, with respectively 26 billion TL and 45 billion TL (TUIK, 2012). Briefly, real economy was not producing enough to finance the void of foreign capital. Turkey’s economy was fragile, therefore, unstoppable slowdown in GDP growth was seen after the outflows of foreign capital.

Beside the reasons of declining economic growth, I will now go further with the reasons of increasing current account deficit and unemployment rate. The source of things worsening again stemmed from the short-term foreign capital. It caused appreciation of Turkish Lira (TL) which will affect current account balance and employment negatively. First of all, it caused a huge deepening for current account deficit. With the appreciation of TL, import of high value-added goods became considerably more affordable. Thus, sectors like automobile, auto parts and consumer durables benefited highly from this new development. Therefore, imports rose rapidly. On the other hand, the competitiveness of Turkish exportables diminished significantly. The prices increased for the sectors like textile, clothing, small scale glass and ceramics in the world market. Hence, exports began to decrease in Turkey. Ultimately, increasing imports and decreasing exports deepened the current account deficit. Secondly, instead of producing high value-added goods domestically which increases the need for labor, it was mostly imported which affected unemployment rate negatively. Therefore, automobile, auto parts and consumer durables couldn't contribute to employment as expected. In addition to this, Turkish exportables went for cost-saving methods due to the decreasing sales that stem from appreciation of TL. This meant, they had to remove their employees from their jobs. I can state that, under the banner of short-term capital inflows, appreciation of Turkish Lira caused both the increasing rates of unemployment and current account deficit. (Yeldan & Ünüvar, 2016)

The solutions for financing the current account deficit, indeed, caused bigger problems. One way to finance current account deficit was portfolio investments. Portfolio investments financed 85 per cent of the current account deficit for the year 2012, namely $48.5 billion, while in 2010 and 2011 only around 40 percent of current account deficit was financed (Yeldan & Ünüvar, 2016). Given so much place to portfolio investments generally result with excessive volatility and uncertainty in real sectors of the national economy (Yeldan & Ünüvar, 2016) which we experience today in Turkey's economy. Other ways of financing current account deficit are FDI flows and long-term borrowings (Çetinkaya, 2017). In figure 3, it can be seen that the share of FDI and long-term borrowings in financing current account deficit leaves portfolio and short-term capital behind after 2014. In addition to this, FDI is the most beneficial among them due to its ability to sustain employment and new technologies. Unfortunately, as it is examined in literature, FDI also cannot contribute to Turkey's economy due to the expedited privatization under AKP government. Privatization was $8.053 billion in the period of 1986-2002 and reached up to $35.255 billion between 2003 and 2012 when AKP was on the government (Angın & Bedirhanoğlu, 2013). Briefly, rather than launching new facilities with the new employment capacities -called greenfield investments- FDI could be seen mostly in Mergers & Acquisitions (M&A) via privatizations which does not have any contribution to employment. Just as FDI cannot contribute to employment, as it can be seen in figure 3, after 2015 it cannot finance the current account deficit as well. It would be appropriate to claim that even the solutions could not save the problems in the macroeconomy.

Figure 3: Financing of Current Account Deficit, 2007-2016



Source: Macroeconomic Outlook and Monetary Policy in Turkey, TCMB, 2014

Especially, current account balance which is found as a crucial determinant of FDI inflows by Aydoğan (2017) became problematic. Turkey's current account deficit increased rapidly after 2001 crisis and in 2011 it hit the highest number ever. This seems to be the consequence of AKP's economic policy based on IMF adjustment program. Thus, Turkish current account deficit cannot be the reason behind the decreasing amount of FDI inflows in the last three years because it has been an ongoing problem since the beginning of 2000's in Turkey, however, it may be the reason of low level of FDI inflows in general.

This chapter tried to represent the main problems in Turkey's macroeconomic scene. There are some other problems in Turkey's economy which are even more crucial. However, I tried to focus on the problems which might affect FDI inflows directly. I found that poor macroeconomic indicators do not directly cause a decrease in FDI inflows in Turkey. The effect of the global investment conjuncture seems to be more significant on FDI inflows. Moreover, recent GDP volatility in Turkey, which stem from the increasing political turmoil in the last three years, seems to have a correlation with decreasing FDI inflows. However, macroeconomic analysis in this chapter is not enough to explain the determinants behind this decrease, therefore in the following chapter I will analyze the change in Turkey's democracy to see its effect on FDI inflows afterwards.

CHAPTER 3

ROAD FROM DEMOCRATIZATION TO ONE-MAN REGIME

AKP, which is the dominant party for more than 15 years in Turkey, started its path with an extended democratization process in 2002. They came into power by vowing to demote the old-authoritarian regime based on Kemalist elites and bring democracy (Somer, 2016). In addition to this, AKP defined itself as the victims of this old-authoritarianism and promised to embrace people who felt the same (Somer, 2016), in other words, who felt excluded as well. However, AKP failed to consolidate democracy. They soon created their own political elites, but this time it was Islamists based (Somer, 2016). As the dominant party, they gave two main battles on this road, respectively, with Kemalist-elites and with the Gulen Movement (Akçay, 2018). They won the first battle, with Kemalist-elites, but at the end caused a deep polarization between people. Second battle came unexpected and happened with Gulen movement which belonged to the AKP's political elite previously. Moreover, when we consider each election -except 2015 election- after these battles, AKP emerged even stronger and its supporters became monopolized under the former chairman Erdogan's increasing power. At the end, as many scholars come together, Turkey under Erdogan's power lost its democratic pattern and moved towards a new type of authoritarianism. In this chapter, I will analyze Turkey's road from democratization to one-man regime in three periods as I also did in the previous chapter. This analysis of Turkey's democracy is based on Freedom House's democracy index which are political rights and civil liberties.

During the 'golden age', AKP represents the successful harmony of economy, democratization and foreign policy. The 'democratization process' involved reordering of civil-military relations and extended minority rights. This period was especially marked by extended rights for Kurdish citizens, such as improved language and cultural rights. Democratization process was reinforced by ‘the strong economy model’, which I tried to analyze elaborately in the previous chapter, and peaceful foreign policy under ‘zero-problem with neighbors’ slogan. Moreover, this harmony maintained AKP’s power with the help of Europeanisation process. (Öniş, 2015)

Stagnation period started with the Kemalist battle in 2007. AKP’s candidate Abdullah Gül, for the 2007 presidential elections, created a tremendous concern between secular based Kemalist-elites due to him being a political Islamist. First of all, AKP was warned by Turkish Armed Forces (TAF), with an e-memorandum posted on the general staff’s website, for being a threat to secularism. This led the large groups of people to fall into the street for protecting secularism under the name called Republican Meetings organized by Kemalist associations. AKP respond to this with early elections which concluded with victory. Its vote increased from 34.3 per cent in 2002 to 46.6 per cent in 2007 and at the end Abdullah Gül was elected as the 11th president of Turkey. Moreover, in October 2007 AKP changed the presidential election system via referendum and underlined its victory. (Akçay, 2018) The crucial point is, this was the first time people began to polarize under AKP’s populist propaganda. In addition to this, the year 2007 was also remarkable with series of assassinations against non-Muslims; Hrant Dink the Turkish-Armenian journalist was assassinated, and Zirve Publishing House was attacked. (Akçay, 2018) Thus, it would be right to claim that this year was the year that democracy got injured for the first time under AKP government. The battle with Kemalists, however, was not over yet. The last round included the counter attack of Kemalists with party closure case and; Ergenekon and Balyoz cases in 2008 where a large of number of high-ranking military personnel were arrested. The constitutional court known as the guardian of the Kemalist republic filed a party closure case in 2009 against AKP due to its anti-secular pattern. However, the majority for the closure cannot be sustained. Thus, the attempt of Kemalist was resulted with loss again and AKP got its second victory. Unfortunately, people lost their trust for the judicial system. (Akçay, 2018)

This period was also remarkable with two striking external shocks; the global financial crisis in 2008 and Arab Spring starting in 2010. In the light of these developments AKP's foreign policy turned out be more assertive, for instance Erdogan's 'one minute' stance in Davos (Benhold, 2009) and his active role during the Arab Springs. Turkey, under Erdogan's government, became a role model for the Arab World (Kirkpatricksept, 2011). On the other hand, problems started to arise with neighbors, especially with Syria. AKP criticized Esad's repressive attitude towards the opposition many times and when the free trade agreement suspended in 2011, relations with Syria came to the breaking point (Kirişçi, 2013). At this point, one might claim that AKP's foreign policy, 'zero-problems with neighbors' came to an end. Meanwhile, the first sparks of AKP's second battle started with the Mavi Marmara incident in 2010 and this time the battle was between AKP and the Gulen movement. Mavi Marmara, aid flotilla to Gazza, was attacked by Israel forces and resulted with loss of nine lives (Akçay, 2018). The Gulen movement accuse AKP for being responsible for the loss of civilian lives and underlined the prior necessity of taking permission from Israel government. Gulenists were one of AKP's main support groups, however, were not known to be against Israel as much as AKP. Thus, disagreement among AKP's political elites had begun (Akçay, 2018). At this point I would like to assert that stagnation period is remarkable with Turkey's change from Western to Middle East oriented state. Turkey slowly began to move away from Western-sense of democracy. The reason behind this might be Euro crisis or loss of hope to be a membership of EU or both. (Öniş, 2015) While some groups among AKP's Islamist based political elites supported this change, Gulenists did not find it well. Although this divergence did not cause a big loss for AKP for the beginning, its effect was going to be devastating for Turkey at the end.

Despite all of these, in 2011 general elections AKP increased their votes with 3 per cent and elected as the leader party again (Appendix 4). Thus, AKP entered the second decade of 21st century more self-confident. The stronger it started, the more AKP was hit and the more it was hit, AKP got more repressive. Moreover, moving away from Europe also caused AKP to lose its western-sense of democracy. In addition to this, beside the powerful beginning with 2011 elections, AKP had to face many threats during this period, therefore, the period after 2011 called as declining period of AKP.

The year 2013 is very significant. First, a modest environmental protest in Istanbul Gezi Park turned into mass uprising over the country during May-June 2013. The reason behind this change in direction was the excessive use of force which was responsible for suppressing the uprisings (Öniş, 2015). These uprisings show how AKP became intolerant of opposition. Another striking point of uprisings was the silence of mainstream media. They refrained from broadcasting the developments (Esen & Gümüşçü, 2016). In the same year one hundred and six journalists were fired and thirty-seven of them forced to resign (Önderoğlu, 2015). Hence, the usage of social media became more crucial to get connected and organized during the uprisings. In the light of these, Freedom House changed the status of Turkish press from 'partly free' to 'not free' in 2014. Last but not the least, Gezi Park Uprisings reflected the weakness of the opposition parties in Turkey. Opposition had stuck in social media and political parties failed to take this as advantage to topple the ruling party (Öniş, 2015). The governments' attitude during the Gezi Uprisings is the main turning point that push people to extreme polarization.

After the Gezi uprisings the second shock came from The Gulen Movement-corruption scandal in December 2013. This was the clear start of the AKP-Gulen battle after Mavi Marmara incident. The Gulenist prosecutors revealed a bribery scheme that included Erdoğan and his family along with four of his ministers. In response, Erdoğan defended himself by claiming that the documents are fake. However, at the end he had to sacrifice his accused ministers. After this scandal, ties between Gulenists and AKP cut completely and Erdoğan called the movement a parallel state. Together with the Gezi movement the corruption scandal damaged AKP's credibility. (Akçay, 2018)

Although AKP's credibility had been undermined during 2013, they got two victories in 2014, respectively, general elections in March and presidential elections in August. AKP raised its votes even more than the previous local elections in 2009 and Erdoğan was selected as twelfth president of Turkey with 51 per cent of the votes. While some of the people were expecting AKP to lose, they even raised their votes. According to Öniş (2015), this can be explained as ‘bounded communities’. He states that “Bounded communities can be considered part of a system of exclusion and inclusion. In certain forms of bounded communities, attachment to a specific political identity plays a central role for individuals. In these communities, individuals sometimes develop strong moral sentiments towards other group members, and refrain from punishing ‘insiders’ to preserve the unity of their communities” (p.36). Thus, according to this notion, people refrained to punish Erdoğan or AKP via ballot box and chose to continue with them instead of trusting an outsider. At this point, it is obvious that Erdoğan’s majoritarianism, since the beginning of 2000’s, again played a crucial role for gaining the elections.

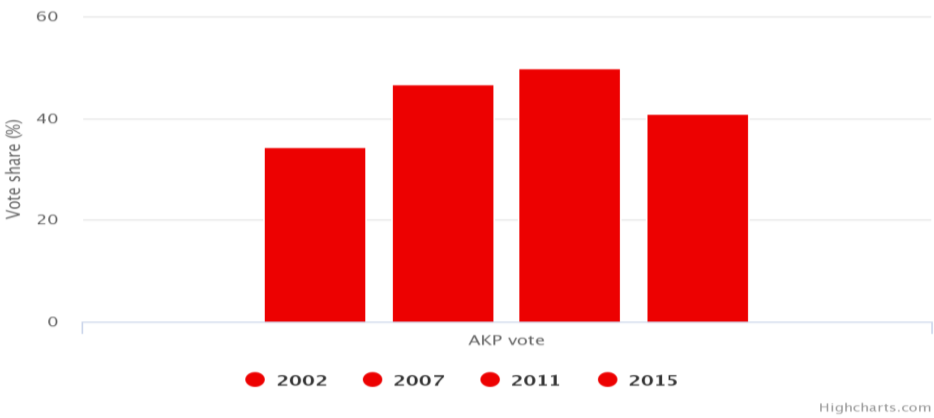
In 2015, Freedom House decreased Turkey’s electoral process note by underlining the irregularities in the campaigns, media’s self-censorship, lack of transparency in campaign finances, and voter fraud for 2014 elections. Elected as a president Erdoğan, consolidates the power under himself and Turkey slowly has moved towards one-man regime.

Before going further, I would like to mention one important realm for Turkey's future democracy. Except than two incidents during 2013 that caused a huge damage on democracy, respectively, the Gezi Uprising which reflects the suppressed opposition in Turkey and the corruption scandal, an important step was taken in the matter of Kurdish peace process. In 2013 ceasefire was achieved between Turkey and PKK at the end of the ongoing negotiations with Abdullah Öcalan. This achievement was the result of the ‘democratization opening’ process that AKP has been pursuing since 2009 (Keyman & Gümüşçü, 2014).

In retrospect, AKP has been known by its reformist peaceful agenda to Kurdish question since the very beginning of its first years. In 2009, government revealed 'the democratic opening' package for minorities. This included reforms in the field of education, broadcasting, organization, and expression of cultural difference. Following this package AKP opened the first official TV station broadcasting in Kurdish, returned the original Kurdish names to villages, introduced optional Kurdish courses in private schools, and established Kurdish-language institutes in universities (p.105). Meanwhile, negotiations with PKK had been started for disarmament by the government. However, in a short-term government had to end the process because public majority was not content by the ongoing developments such as PKK-demonstrations after negotiations. At the end, although some rights and freedom had been ensured for Kurdish people, AKP failed to provide disarmament and the extension of political rights. Armed conflict between two parts continued vigorously and reached its peak point with the influence of Arab Spring in 2011. While the turmoil had been increasing rapidly in the Syrian border, Turkey had to develop a new security paradigm. Thus, in October 2012 peace process was started, and in 2013 ceasefire achieved between two parts with Abdullah Öcalan's withdrawal request. Nevertheless, for more sustainable peace process the co-chairman of BDP (Peace and Democracy Party) Selahattin Demirtaş underlined the importance of extensive democratization process in the matter of political pluralism. His statement addressed that the ceasefire and extended minority rights was not enough for long-term peace (Keyman & Gümüşçü, 2014).

Above, the paragraph elaborates how fragile Kurdish question in Turkey is. As a matter of fact, peace was only sustained until 2015. Now I will go further with 2015 elections which are very significant for both the rise and the fall of Turkey's democracy. In June, AKP's votes decreased for the first time over the last 12 years (see figure 4). AKP lost nine-point of its votes compared to the previous election in 2011. On the other hand, HDP achieved to enter the parliament by exceeding 10 percent of threshold as the first Kürdish Party in Turkey's history (see appendix 1). In the matter of political pluralism this was a big step for Turkey's democratic future. In other words, this could be a chance to see other parties in the government after a long time. In addition to this, having a fourth party in parliament which served rights for minorities as well as the whole public, was also beneficial for

Figure 4: AKP's Vote Share in General Elections, 2002-2015



Source: The Telegraph, 2015

democracy. In the meantime, since AKP could not catch the majority in the parliament, they had to go for coalition. However, no negotiations could be achieved with any party and Turkey went for a second election in 1 November. At the end, AKP got back the 9 points of the votes that they lost in the previous elections.

The year 2015 is also remarkable with the increasing terrorist attacks all over Turkey. The attacks from PKK and ISIS caused the loss of hundreds of people included civil, military men and police. In addition to this, after the June 7 elections successive attacks took place: July 20 Suruç suicide bombing and July 22 Ceylanpınar assassination, ensured that the peace process was no longer valid. The attacks continued violently (Esen & Gümüşçü, 2016). Just after PKK's attack in Dağlıca in September 6 which caused 17 deaths and several injured, Erdoğan underlined the importance of political stability and made a statement on TV that if 400 members of parliament were given, such attacks would not have occurred (Esen & Gümüşçü, 2016). The period between two elections 167 people were killed in Turkey (Sözcü, 2015). Moreover, political turmoil within the country continued even after the political stability sustained with the November 1 election. Beside the domestic crisis, Turkey was also having crisis in the matter of international relations. On November 24th, a Russian warplane was shot down because the plane was inside of Turkey's airspace and did not leave despite of the warnings. On the other hand, Russia was claiming that its warplane was outside of the Turkey's border and did not receive any warning (BBC, 2015). This incident started the political turmoil between Turkey and Russia which lasted more than 1 year. Thus, beside the problems in domestic affairs, Turkey's foreign policy was going far away from the 'zero problem with neighbors' policy. Moreover, violation of civil liberties became more distinct in 2015, especially in the matter of freedom of expression. In 2015, 460 people were investigated for insulting Erdogan, 50 were journalists, while 281 were members of formal opposition (Esen & Gümüşçü, 2016). Defamation lawsuits spread abroad in April 2016 with German comedian's satirical poem that insults Erdoğan (Staufenberg, 2016). This was the first spark of the breakdowns between Germany and Turkey after ongoing refugee crisis. At the end, Erdoğan's name began to be mentioned together with other authoritarian leaders, for example in *Breaking Down of Democracy*.

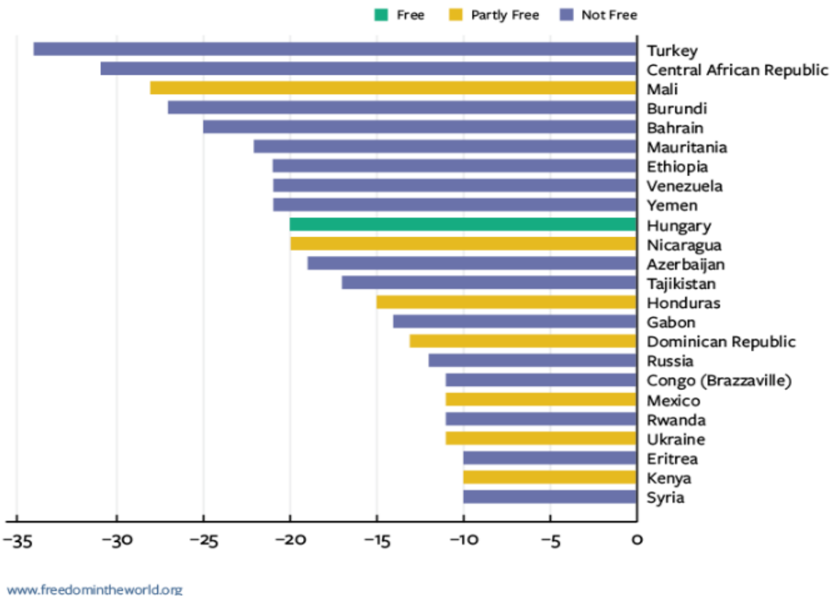
Political turmoil reached its peak point on July 15,2016 with the coup attempt organized by the Gulenist wing of the TAF. This was the last and the most devastating move of the Gulen movement against AKP. On the same night, Erdoğan addressed Turkey via Facetime connection on TV. He called on people to go out on the streets to resist the coup (Reuters, 2016). In twelve hours the coup attempt failed (Akçay, 2018). The smart usage of media, here social media, had contributed significantly to the failure of the coup. Soon after, Erdoğan declared the state of emergency which is still ongoing (May 2018).

Under state of emergency ongoing intolerance of opposition turn into dispose of opposition; fifty thousand people were arrested, and one-thousand public officials were expelled from their jobs only in one year (Hayatsever, 2017). In the light of these, Turkey was defined as a country whose democratic indicators have declined the most among others in the last 10 years (see figure 5). According to Freedom House, modern authoritarianism defined as;

> An illusion of pluralism, state or oligarchic control over key elements of the national economy, state or oligarchic control over information on certain political subjects and key sectors of the media, suppression of

nongovernmental organizations (NGOs) that are focused on human rights or political reform, legalized political repression, with targets punished through vaguely worded laws and politically obedient courts, limited, selective, and typically hidden use of extralegal force or violence, with a concentration on political dissidents, critical journalists, and officials who have fallen from favor, Opportunistic, non-ideological cooperation with fellow authoritarian states against pressure for democratic reform or leadership changes' (Puddington, 2017, p.6).

Figure 5: Largest 10-Year Declines in Freedom



Source: Freedom in the World 2018, Freedom House

Moreover, the tactics, that those modern authoritarian leaders apply, are, in general; majoritarianism, squelching opposition, increasing arrestments, aggressive foreign policy, refashioning history, smart-censorship in media and targeting enemies (Puddington, 2017).Turkey under state of emergency with Erdoğan's presidency implement these tactics indefectibly.

First of all, with respect to majoritarianism AKP uses the tool of marginalizing the opposition since the very beginning of 2000's. It reaches the higher levels during the Gezi Uprisings. However, the climax was after the failed coup attempt. For instance, the ones who did not attend or support ‘Yenikapı Soul’ which was organized after the attempted coup or the ones who did not vote ‘yes’ for 2017 referendum named as ‘traitor’ or ‘terorist’. Following this, some ‘traitors’ were arrested with the accusation of supporting terrorist propaganda, particularly the party members of HDP, included both co-chairman (BİA Haber Merkezi, 2018). Beside opposition party leaders, Osman Kavala’s arrest is very significant in the matter of him, being a businessman and human rights activist. (Altıntas, 2017). Briefly, beside the responsibles of failed coup attempt, many people who oppose Erdoğan were arrested for various reasons.

Furthermore, prosecution of journalists had continued, and foreign press also took a share of it. A German- Turkish journalist Deniz Yücel was arrested on 14th of February (Reuters in Istanbl, 2017). This increased the diplomatic crisis between Turkey and Germany which has been going on since the refugee crisis. Soon after, when Germany as well as the Netherlands did not allow for referendum campaign within their borders (Cumhuriyet, 2017), these countries were declared as anti-democratic and fascist. At this point, I can state that enemies were declared both inside and outside of the country. As enemies rise, he was becoming a hero thus he can strengthen the ties with his bounded community. In addition to this, assertive foreign policy branch out to military invasion in Syria. It has been told by the government that Turkey invade Syria on the purpose of clearing terror organization. Just as other modern authoritarians such as Putin, Erdoğan was also bullying his neighbors.

As other modern authoritarian leaders, Erdoğan gives a huge importance to media. Media is significant for maintaining the ties with AKP’s electorate base, in other words, with its bounded community. Thus, beside controlling the media, it is also manipulated. First of all, the instruments of controlling media are judiciary and economic power of the state (Somer, 2016). As I have presented above judiciary power on media can be understood by the increasing arrests to journalists and state’s economic power can be found in the media companies when they feel obliged to fire their personnel who are not appreciated by the government. A recent example of this is anchor Nevşin Mengü who feels obliged to resign (CNN, 2017). Hence, media's fate in Turkey concludes with self-censorship. Second, pro-government channel is an efficient way to manipulate media without any control or restriction (Somer, 2016). Thus, the channel can make government propaganda which is very significant especially before the elections (Somer, 2016). It is a common instrument between modern authoritarians that they enjoy refashioning the history (Puddington, 2017). For example, in Turkey, Erdoğan's sympathy to Ottoman Empire is known widely. In some channels Ottoman-style janissary music has been used as an intro and the increasing number of TV Shows whose storyline is based on Ottoman history. As it can be seen, media is not only controlled but also used smartly. Indeed, this was actually obvious with Erdoğan's FaceTime connection in CnnTürk which was able to stop the coup attempt.

In 2018, Freedom House changed Turkey's status from partly free to not free. According to this, Turkey is not a free country, however, around 10 years ago, Turkey was praised to the skies with its well-developed democracy. In this chapter I found that political rights and civil liberties have been damaged since the beginning of AKP's first year, thus, being an anti-democratic country is not a new thing for Turkey, for instance; polarization between Kemalists and Islamists has been remarkable since AKP was in government, assassinations to non-Muslims can be observed in 2007, absence of judicial independence can also be seen clearly not long after 2007, intolerance of opposition and un-independent media is clearly visible during 2013 Gezi Uprisings and voter fraud has been a visible problem since 2014. These deficiencies in democracy increases under state of emergency but cannot be represented as a new breakdown. Democracy has been a loss since the beginning of 2000s. It did not breakdown suddenly. In the next chapter I will analyze the main turning point of breakdowns on FDI inflows.

CHAPTER 4

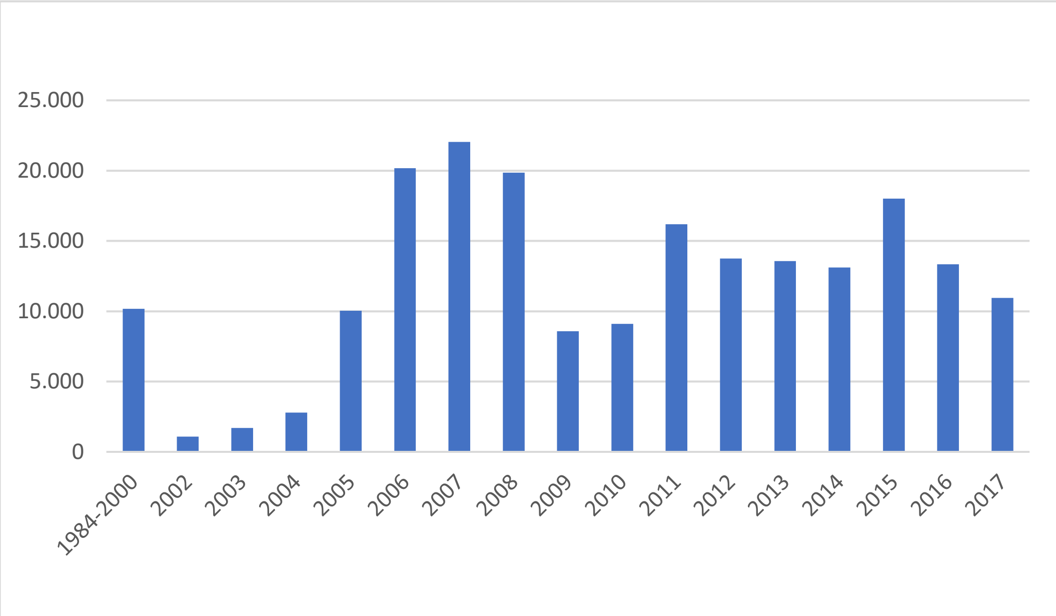
THE IMPACT OF CHANGING STRUCTURE OF DEMOCRACY ON FDI INFLOWS

As can be seen in the previous chapter, currently democracy is at peril in Turkey, however, this was not the case when the AKP came to power at the beginning of the 2000's. As Öniş (2015) states, in the first five years AKP presented a charming harmony blended with increasing Europeanization period and extended civil liberties and political rights in the matter of democratization process. Unfortunately, afterwards increased democratic rights began to breakdown gradually. Moreover, in the recent years Turkey slowly moves towards one-man regime. In the literature, according to the traditional liberal approaches, MNCs avoid investing in countries that are weak in terms of democracy. On the other hand, critical approaches claim that democracy is not a priority for foreign investors. Hence, in order to understand how FDI affected from the decreasing trend of democracy I will analyze the FDI inflows and its parameters in Turkey between 2002-2018 when the change in democracy has observed.

Before analyzing the period 2002-2018, I will start with a brief history of the FDI inflows in Turkey since 80's, to better understand the sudden increase in FDI inflows in the early 2000s. Turkey had started to liberalize its account since 24 January 1980 decisions, however, due to the military takeover between 1980 and 1983, FDI could only accelerate after 1983. During 90's FDI inflows continued to increase rapidly. Although, flows were affected negatively by the economic crisis in 1994, they recovered fast during the economic boom between 1995 and 2000. The reason behind this recovery attributed to the establishment of customs union between Turkey and EU on 1st of January 1996. However, FDI inflows were still lower than expected (Atik, 2005). As many scholars claim in Turkey's FDI literature, these low levels of FDI inflows was the result of chronic political instability during 90's. After 2001 crisis, AKP came to power with a new economic agenda under the name of ‘The Transition to a Strong Economy’ and the structure of FDI inflows in Turkey changed suddenly. While the total FDI inflows between 1984-2000 was $10.168 million, it reached up to $194.261 million between 2002-2017 (TCMB, 2018). One might say that AKP being a dominant party for more than 15 years has provided the political stability which could not be achieved since the 80’s, therefore, FDI inflows also increased.

In the golden age of AKP, FDI inflows increased rapidly. Especially, in 2007, flows reach the highest amount in the history $22.047 million (see figure 6). The high amount of FDI inflows in this period can be attributed to the rapidly evolving Europeanization process and expanded democratic rights in the same period.

Figure 6: FDI Inflows to Turkey, 2002-2017 in US $ Million by TCMB



Source: TCMB, 2018

However, after the 2008 financial crisis flows experience a rapid fall. This fall can be seen explicitly in Turkey’s dominant sector, finance and insurance from 2008 to 2009 (see table 1). In the following two years, FDI inflows continued to stay weak until 2011. As far as we know from previous chapters, the period between 2007-2011, was called the stagnation period, thus, beside the poor FDI inflows, democratic structure was also not as impressive as the first five years of AKP government. Since AKP came to office, the party had been faced with a great reaction for the first time. AKP accused as being anti-secular and received a memorandum from military. This was followed by the huge demonstration organized by Kemalist people. In the same period, disagreement was observed also within party's grassroots. In addition to this, Kurdish question came to a deadlock

Table 1: FDI by Sectors, 2008-2017

Sectors	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Total
Finance and Insurance	6.136,00	817,00	1.621,00	5.883,00	2.084,00	3.415,00	1.470,00	3.516,00	1.766,00	1.452,00	28.160,00
Manufacturing	3.972,00	1.640,00	924,00	3.599,00	4.519,00	2.843,00	2.742,00	4.227,00	2.241,00	1.262,00	27.969,00
Energy	1.055,00	2.153,00	1.824,00	4.293,00	773,00	1.794,00	1.131,00	1.338,00	676,00	947,00	15.984,00
Health and Social Care	147,00	105,00	112,00	232,00	546,00	106,00	204,00	58,00	274,00	62,00	11.846,00
Wholesale and Retail	2.088,00	389,00	435,00	707,00	221,00	379,00	1.137,00	599,00	688,00	501,00	7.144,00
Transportation and Warehousing	96,00	230,00	183,00	221,00	130,00	364,00	594,00	1.524,00	635,00	1.350,00	5.327,00
Construction	337,00	209,00	310,00	301,00	1.427,00	178,00	232,00	106,00	291,00	627,00	4.018,00
Real Estate	453,00	210,00	241,00	300,00	174,00	128,00	252,00	171,00	283,00	31,00	2.243,00
Hospitality Sector	25,00	55,00	113,00	122,00	16,00	59,00	24,00	11,00	259,00	66,00	750,00

Source: TCMB, Balance of Payments International Investment Position, FDI in Turkey by Sectors, 2018

with the arrests of eight thousand Kurdish activists between 2009 and 2012 under KCK (Union of Communities in Kurdistan) case (Keyman & Gümüşçü, 2014). Meanwhile in 2011 the armed conflict with PKK reached its peak point. However, in the same year, one might find it surprising that FDI inflows almost doubled compared with the previous year (see figure 6). At this point, we cannot claim that FDI inflows affected negatively by the political turmoil. Thus, our finding supports Atik (2005)'s argument that terror attacks do not have any significant effect on FDI inflows. At this point, when I both consider the increasing political turmoil during the stagnation period and the heavy increase of FDI inflows in 2011, I cannot claim that FDI inflows are affected from the political unrest in the country. On the other hand, this does not mean that decreasing political turmoil accompanying with the developed democratic rights, as it is observed for the golden age period, would not have any positive affect on FDI inflows.

The period from 2011 to the present is the declining period of AKP, which democracy is completely at peril. In addition to this, the average amount of FDI inflows for this period (2011-2017) is accounted for approximately $ 13 billion (TCMB, 2018). FDI inflows till 2015 amount on average, however, in 2015 flows rise above the average and reach its highest values of the declining period with $ 18 billion. On the other hand, the year 2015 was again the year which terror attacks was extremely intense all over the country. Moreover, unlike 2011 beside PKK, this time the country was also attacked by another terrorist group called ISIS. Indeed, it is already stated above that the terror attacks do not affect FDI inflows. Unfortunately, this was not the only distress for this period, democracy was also directly under attack. The years till 2015 has been witness to series of events that harm democracy directly. Especially, in the year 2013 AKP's intolerance to opposition became clearly visible with the disproportionate force during Gezi Uprising, and Erdogan's populist rhetoric which pushes people to a deep polarization. In addition to this, the corruption scandal in December led to decrease AKP's credibility. Moreover, 2014 elections were claimed as biased elections by opposition this casted a doubt about the country's democratic structure. Within this framework, we can hardly talk about democracy under the banner of political rights and civil liberties. Thus, the argument of Harms & Ursprung (2002) which claims that 'the countries that have a lack of human rights deter the investments of MNCs' seems to be weak. A huge loss is not observed in FDI inflows as much as in democracy. Moreover, they also claim that developed unionization attracts more FDI inflows. However, according to OECD data, trade union density in Turkey decreased from 29.1 per cent in 2001 to 6.3 per cent in 2015 (Akçay, 2018) where FDI inflows increased from $3.352 million to $17.717 million, respectively, in 2001 and 2015. Hence, this argument as well does not represent Turkey's situation.

Briefly, rapidly decreasing political rights and civil liberties do not seem to affect FDI inflows until 2015. However, the period after 2015, FDI inflows begin to fall gradually (see Figure 6). In this period, Turkey had experienced a failed coup attempt in July 2016. This was followed by the state of emergency which was declared right after the coup attempt and has lasted until today. During the state of emergency investors become the ones who panic the most. For instance, capital controls during these times are highly expectable and in Turkey's case, the statements of president Erdoğan could be the examples for this fact. For instance, on December 2017, he commented about the increasing outflows from the country as 'I hear some businessmen are trying to take away their assets from the country. Don't allow anyone to do it. Because it is betrayal' (Sputnik,2017). Those kinds of announcements are against the rule of open market policies which could push markets into panic and lead more capital outflows.

According to UNCTAD (2017) report, inflows only fell by 15 per cent in Turkey's region -developing Asia- while FDI inflows in Turkey fell sharply by 31 per cent in 2016. The fall in Turkey's FDI inflows seems to be caused by the recent state of emergency which is Turkey's specific factor. It does not seem to originate from the global conjuncture.

Beside the state of emergency poor relations with other countries can also be another cause of decreasing FDI inflows. After the Russian warplane was shot down by Turkey on November 2015, Russia-Turkey relations went through a crisis in the following years. As Buckley & Casson (1976) claim, stable political relations are primarily necessary for a healthy investment environment. Thus, in table 2, sharp fall of Russian investments can be observed from 2016 to 2017. In addition to this, since 2010 European countries and US have constituted the large portion of FDI in Turkey (see table 2). However, in the last years as Turkey slowly moves away from being European-oriented and become more East oriented, European investments began to fell. Thus, according to Buckley & Casson (1976), decreasing FDI inflows from Europe and Russia stem from un-stable political relations.

Table 2: FDI by Countries ($ Million)

	Countries	2010	2011	2012	2013	2014	2015	2016	2017	2018/ Feb.	2002 - 2018/ Feb.	2002 - 2018/ Feb. Share %
1	Netherlands	486	1.424	1.381	918	2.022	1.184	1.024	1.768	158	24.010	16,1%
2	U.S	323	1.401	439	326	334	1.619	338	171	62	11.379	7,6%
3	Austria	1.584	2.419	1.519	667	31	80	345	326	64	10.128	6,8%
4	U.K	245	906	2.044	300	1.051	585	974	324	8	9.894	6,7%
5	Germany	597	664	491	1.970	606	355	440	295	17	9.172	6,2%
6	Luxemburg	311	562	1.186	278	565	1.252	335	109	16	9.136	6,2%
7	Spain	205	2.251	193	581	74	2.305	318	1.451	43	9.114	6,1%
8	Belgium	48	1.495	39	60	38	767	13	226	0	8.425	5,7%
9	France	623	1.000	86	217	287	165	90	107	12	6.973	4,7%
10	Greece	436	111	58	68	52	48	0	0	0	6.831	4,6%
11	Russia	2	762	11	1.433	723	747	723	5	0	6.209	4,2%
12	Azerbaijan	12	1.266	338	803	884	839	661	1.009	76	5.993	4,0%
13	UAE	104	89	52	176	115	80	26	28	1	4.182	2,8%
14	Italy	25	111	154	148	488	180	87	124	12	3.103	2,1%
15	Japan	347	231	106	439	257	314	454	295	35	2.654	1,8%
16	Switzerland	123	233	454	204	149	177	339	52	28	2.512	1,7%
17	Saudi Arabia	39	9	439	39	10	17	21	9	2	1.970	1,3%
18	Kuwait	193	43	271	185	197	7	73	56	9	1.695	1,1%
19	Qatar	52	50	46	469	8	350	420	100	56	1.677	1,1%
20	Lebanon	29	45	315	573	35	0	152	2	0	1.287	0,9%
	First 20 Country in Total	5.784	15.072	9.622	9.854	7.926	11.071	6.833	6.457	599	136.344	91,7%
	Others	472	1.064	1.139	669	706	1.006	701	986	18	12.417	8,3%
	World Total	6.256	16.136	10.761	10.523	8.632	12.077	7.534	7.443	617	148.761	100,0%

Source: FDI Statistics, https://www.ekonomi.gov.tr

On the other hand, other investments from other parts of the world began to be more common. These investments are usually made in the form of Mergers and Acquisitions. Some big investments for 2017:

- OMV Petrol Ofisi is acquired by the Dutch Company Vitol Investment for $ 1.441 million

-The Spanish Bank BBVA acquires 9.95 per cent of Garanti Bank with $917 million

- Banvit is acquired by BRF (Brazillian Company) and Qatar Investment Authority for $ 315 million

-Mersin Port is acquired by IFM Investors (Australian Company) for $ 869 million

-Unit International Energy is acquired by SK Engineering for $ 177 million (YASED, 2018)

Here the crucial point is, although countries like Australia, Brazil, Qatar and South Korea constitute the considerable amount of the investments, the acquisition made by a Dutch company is the highest, therefore, it is very significant. In 2017, Turkey had a crisis with the Netherlands. Just before the referendum, the Dutch government did not permit political campaigns wanted to be done by the acting Turkish government. Following the crisis, both countries applied sanctions on each other. Therefore, it is interesting that the acquisition of Petrol Ofisi took place during this period. Chief Executive Officer of Vitol, Ian Taylor, made the following comments regarding the acquisition:

> "This is a strong business in a growing market. Its market leading brand has benefitted from OMV's focus on high standards of HSSE. We are committed to maintaining this excellent track record and greatly look forward to working with the Petrol Ofisi team to capitalize on Turkey's strong economic performance and growing demand for energy products." (Vitol, 2017)

According to Buckley and Casson (2017), it is expected that, the investments of a country fall in the host country where it has weak political relations. However, in the case of Dutch investments, this cannot be observed, considering the increasing investment in 2017 (see table 2) and the huge acquisition of Petrol Ofisi. Moreover, the statement of the Ian Taylor, claim the efficiency of the Turkish market. It seems that stable political relations do not play a crucial role in FDI.

Similar examples took place between other countries and Turkey. When Germany and Turkey are analyzed, although German companies' investments show a downward trend (see table 2), when the political tension between Turkey and Germany reaches to its peak point in the year 2017, Turkey witnessed constructive attitudes and activities of two huge German multinationals. First of all, in the same year, the president and senior manager of Bosch Turkey and the Middle East Steven Young has declared that the company will invest $184.2 million in Turkey. Moreover, he states that the company was not affected negatively by the political tensions between two countries and he add that Turkey's investment climate is quite good and that especially incentives are attractive. According to Young, Turkey has been through a lot for years, on the other hand, Bosch invests in Turkey for more than hundred years, thus the short-term turmoil in Turkey would not affect Bosch's long-term vision (Hürriyet, 2017). In addition to this, Bosch announced that they will support every step of the ‘Domestic Turkish Car Project’ gladly as the world’s biggest automobile sub-industry producer (Business HT, 2018).

Second, another leader company of Germany, Siemens made a huge investment in Gebze Organized Industrial Zone. The company established a new facility for the low- voltage switchgear plant. Due to being a greenfield investment with a new production facility one might claim that its contribution to the country is bigger than other investments. It is underlined that the new facilities contribution to Turkey’s economy is going to be €100 million per year and the company will employ 1000 people (NTV, 2017).

Moreover, after the breaking point of the relations with Russia and considerable decrease in Russian investments, Turkey announced the first incentive certificates of Akkuyu Nuclear JSC on November 2017 -VAT and customs duty exemption certificates were calculated on the fixed investment amount of 76 billion TL (Teşvik Uygulama ve Yabancı Sermaye Genel Müdürlüğü, 2017). In addition to this, there has been some rumors in the matter of exemption durations in the media that it will last 90 years. The detailed content of the certificates cannot be known completely due to confidentiality. However, the well-known fact is that Russian company gets a comprehensive incentive just after the crisis with Russia.

Meanwhile, just after Moody’s decreases Turkey’s note on March 2018, the CEO of General Electirc (GE), Alex Dimitrief, stated that Turkey is a significant part of their long-term plans due to its young population and rapidly developing market structure. Dimitrief added that they don’t know what exactly Moody’s is doing but GE will continue to invest in Turkey (Beyhan, 2018). At this point, also the evaluations of credit rating agencies do not seem to be significant on multinationals’ investment decisions in Turkey.

During this period when Turkey performed poorly both in democracy and economy, the huge investment that have been made by world’s famous MNCs can be explained by Hadjikhani, Lee, & Ghauri (2008). MNCs prove their commitment to host country by huge and long-term investments which contribute countries economy, hence, in return, they deserve to have some priviliges such as tax exemptions. This mutual relationship between socio-political actors and firms develop trust with each other. Thus, credibility to risky country is sustained. The actions of Bosch, Siemens and GE in Turkey can be explained like this. For example, Steven Young, pays attention to Bosch's satisfaction about the generous incentives in Turkey. According to Young, the company is proud of being the most incentive-receiving company in Turkey's automotive sector. As Li & Resnick (2003) also point out, incentives are one of the main determinants of FDI in authoritarian countries. these may explain the underlying causes of the huge investment that occurred during the unrest in Turkey and can also show how weak democratic indicators are, among these determinants.

Moreover, according to Henisz (2003) the relationship between socio-political actors and firms, which is necessary for healthy investment environment in risky countries, can also be maintained by firms' ability to make successful lobbying and connect direct ties with socio-political actors. In the case of Turkey, in order to find out these kind of relationship, I demanded interviews from different MNC. Unfortunately, I could not get any affirmative reply due to the sensitiveness of the topic. However, this is not an obstacle for understanding the relationship between firms and socio-political actors.

The huge investments and positive expectations form Turkey's future from MNCs, in the midst of state of emergency in Turkey, are signs of good relations between the firm and the government. Moreover, incentives are the fruits of this good relations. Nevertheless, to find out other possible determinants of Turkish FDI inflows, competitiveness index of WEF (2018) can be analyzed.

Table 3: Competitiveness Index of Six Emerging Countries

Country	Comp. Index	Sub-Indexes						
		Institutions				Infrastructure	Macroeconomy	Market Size
		Property Right Protection	Ethics and Corruption	Judicial Independence	Strength of Investor Protection			
United Arab Emirates	17th	15	3	16	9	5	28	29
Malaysia	23rd	28	34	41	3	22	34	24
Poland	39th	80	65	99	41	44	41	21
Turkey	53rd	75	50	103	21	53	50	14
Hungary	60th	116	93	120	74	56	46	55
Egypt	100th	105	55	31	95	71	132	25

Source: The Global Competitiveness Report 2017-2018, World Economic Forum

Turkey ranked 53rd among 137 countries in the global competitiveness index (WEF, 2017). Market size and strength of investor protection are found as Turkey's most competitive pillars. Unfortunately, high ranked 'strength of investor protection' presents the bitter face of injustice in Turkey since the judicial independence ranked one of the poorest. In other words, although the political rights and civil liberties are not protected in the country, the rights of investors are protected.

At this point, a key question may arise, how investors are protected in a country where democracy does not work very well? Investor protection index is defined in World Bank as the extent of transparency, ability to sue for the damages and easiness of accessing transaction documents (World Bank, 2017). If those rights are provided well to investors, they feel protected and invest freely. According to Turkey's strength of investor protection index, Turkey seems to provide these opportunities very well to the investors. This must be another reason why investors from countries such as Germany and the Netherlands, which Turkey has diplomatic problems, invest in Turkey. Apparently, with these rights investors feel protected and with incentive they feel privileged.

The importance of investor protection can be seen easily when table 3 is analyzed elaborately. Malaysia and United Arab Emirates (UAE) are the most competitive emerging market countries in table 3. In addition to this, strength of investor protection is one of their strongest pillars. However, those countries are the ones who have an authoritarian leader and weak from civil rights and liberties (see table 4). Therefore, it would be appropriate to claim that developed civil rights and political liberties in a host country are not a crucial determinant for investors if their own rights are protected.

Table 4: Comparison of Six Emerging Countries, Competitiveness, Democracy and FDI Inflows

Country	Comp. Index	Democracy Index	FDI Inflows					
			2013	2014	2015	2016	2017	Average
United Arab Emirates	17th	17/100 (not free)	9 764,9	11 071,5	8 550,9	9 604,8	10 354,2	9 869,3
Malaysia	23rd	45/100 (partly free)	584,3	946,2	2 824,0	2 989,0	4 341,0	2 336,9
Poland	39th	85/100 (free)	2 734,0	14 268,7	15 270,8	13 927,8	6 433,5	10 524,0
Turkey	53rd	32/100 (not free)	13 463,2	12 738,7	17 717,0	12 942,0	10 864,0	13 545,0
Hungary	60th	72/100 (free)	3 402,1	7 806,5	- 14 750,6	- 5 854,6	2 491,6	- 6 905,0
Egypt	100th	26/100 (not free)	4 256,0	4 612,0	6 925,2	8 106,8	7 391,7	6 258,3

Source: Democracy Index, Freedom House, 2018

Competitiveness Index, The Global Competitiveness Report 2017-2018, WEF

FDI Inflows, UNCTAD,2018

Moreover, when Turkey is compared with more democratic countries such as Hungary and Poland, Turkey receive more FDI inflows (see table 4). This can be explained by Li & Resnick (2003)'s theory that MNCs invest more in less-democratic countries and enjoy benefits only if the host country has improved property right protection. In table 3, the superiority of Turkey's property right protection can be seen among Hungary and Poland.

Another attractive factor is underlined by Mathur & Singh (2013) which is economic freedom. They claim that investors should feel free in the host country and the protection of property right is not enough to provide the economic freedom that foreign investors are expecting. According to Mathur & Singh (2013), tax rates, capital controls and trade openness are also very significant to determine the FDI in the host country. For instance, Turkey's corporate tax rate is the lowest among UAE and Malaysia with respect to 20 per cent (Trading Economics, 2018). However, although UAE and Malaysia are more competitive than Turkey, Turkey receives more FDI inflows. By only looking at this factor, it can be stated that low tax rates play a crucial role in the matter of attracting more FDI inflows.

On the other hand, FDI inflows in Turkey is decreasing gradually since 2015, as it has been already mentioned above. Certainly, there is a fact that FDI inflows throughout the world has a downward trend since 2015. However, it is mostly concentrated on developed countries. Developing countries stay more stagnant during this period while Turkey experiences a rapid fall. If controlling capital is a deterring factor on FDI inflows as Mathur & Singh (2013) claim, the president of Turkey, Erdogan, has a several speeches which can threaten the capital markets during the state of emergency. Hence, according to Jacobsen & de Soysa (2006), actions or attitudes against to open-market rules deter FDI inflows and those kinds of actions cannot be seen in democracies because democracy and open market policies go hand in hand. Investors should feel free. Therefore, democracies are more preferable than less-democratic ones. However, investors could survive in Turkey and FDI inflows hit the historical record when political rights and civil liberties under attack since the very beginning of 2000's.

Only in the last three years, except than some few examples such as GE and Bosch, investors in general don't seem to feel free and FDI inflows show a rapid downward trend in Turkey. This seems to be caused by the state of emergency which put investors in panic with the possible capital controls. As it is already mentioned above, one of the most important criteria for investors is freedom. Beside privileges, this could be the only thing which can hold them in countries who does not serve well to civil liberties.

To conclude, there is a fact that FDI inflows decreases rapidly while democracy is fading away under one-man regime since 2015. At the first glance, there seems to be a correlation between FDI inflows and democracy which cannot be denied. In this chapter, however, it is observed that the highest amounts of FDI inflows between 2002-2018 are seen in the years when political rights and civil liberties are at risk. Moreover, the big investments of famous MNCs in Turkey and their managers' hopeful expectations for Turkey's future, during the state of emergency, which is known to be one of the biggest enemies of democracy, is presented elaborately. At this point, it is found that incentives, good relations with socio-political actors and economic freedom are more significant determinants on FDI inflows than democracy in Turkey. At the end of this chapter, any causal relationship was found between FDI inflows and democracy.

CONCLUSION

This thesis problematized the relationship between FDI and democracy. The problem derives from liberalism which believes that economic globalization and democracy go hand in hand. According to liberal idea, FDI inflows move away from the countries where democracy is declining. In the light of this, the aim of this study is to understand the impact of decreasing democratic parameters on Turkey's FDI inflows. Therefore, I conducted a case study on Turkey's FDI inflows in order to understand the impact of changing structure of democracy from 2002 to 2018.

However, recently, a new pattern that contradictory to liberalism is observed in the world. In the last 10 years, the world has witnessed an increasing number of authoritarian leaders. On the other hand, their countries do not seem to have a full autarky as one may expect from authoritarian states, instead, they are open to world market. In this thesis, Turkey was chosen as a research area because Turkey takes the first place in the list of the countries whose democracy declines the most. Therefore, my research question formed as 'Does decreasing democracy affect FDI inflows in Turkey?'

In the beginning of this study, when FDI inflows are analyzed roughly, slowdown in FDI inflows can be observed in the last 10 years in Turkey, just like in democracy. Therefore, anyone who looks from liberal perspective would explain this slowdown by the decreasing democratic factors. Especially, in the last three years, political turmoil in the country has increased and democracy was imperiled remarkably. However, some big investments in the midst of this political turmoil in Turkey made me suspicious about the accuracy of liberal theory. For example, a famous German multinational, Siemens, established a new facility cost $ 65 million in Gebze, Turkey on December 2017. This investment was made when political turmoil between Turkey and Germany peaked and when democracy is at risk throughout the world. At this point, I would immediately assert that democracy is not one of the main determinants of FDI inflows and liberal approaches remain weak to explain this relationship. Therefore, in this thesis, I gave a large place to critical approaches in order to find more significant determinants of FDI inflows in a country where there is no democracy.

In this context, in the first chapter, I presented the theoretical framework which explains the MNCs actions in the firm-specific level based on internalization theory and the literature review which discusses the determinants of FDI inflows in country-specific level. I conclude the chapter by analyzing the determinants of FDI inflows in Turkey. Internalization theory contributes this thesis for interpreting the MNCs activities in imperfect markets. For example, in Turkey's case this helped to understand Siemens's motivation to invest in Gebze. This theory underlines the importance of firms' ability to manage market hazard. Moreover, those abilities are stated as successful lobbying and constructing good relations with socio-political actors. Therefore, the relationship between socio-political actors and the company is referred to as a main determinant of FDI in the host country. In addition to this, it is also mentioned that in return for good relations and huge investments that contributes to host countries economy, are rewarded with some privileges, in other words, generous incentives. Hence, incentives also become an important determinant of FDI in a host country. Thus, internalization theory elucidates the MNCs investments in Turkey in the midst of political turmoil. However, internalization theory stays in the firm-specific level, thus remain weak to discuss the effect of host countries' political regime on MNCs decisions. Therefore, to have more perspective I made a literature review on country-specific level which focused on countries ability to attract FDI inflows. The literature review includes two different approaches, respectively, liberal and critical approach. On the side of liberals, the effect of regime is asserted in the significance on FDI inflows. From this perspective, non-democratic countries carry political risks which reduces the credibility of the country, on the other hand, in democracies firms can ensure their ownership-advantages with developed property right protection mechanisms. Liberal idea underlines the risk of expropriation in authoritarian states which obstructs the long-term investment plans. Moreover, many reasons listed for assuring that the countries with enhanced political rights and civil liberties are favorable for MNC. One of the reasons is demonstrated as the activities of NGO which makes the otherwise not possible. Thus, these approaches claim the priority of MNC to invest in democratic countries. Moreover, they have identified the parameters through which I can search the impact of democracy on FDI inflows when FDI inflows reached their peak level in Turkey. On the other hand, critical approaches provide more comprehensive perspective in order to understand the determinants of FDI inflows in Turkey. It helps to identify the high level of FDI inflows where there is no democracy. Nevertheless, it cannot be said that critical approaches claim that the primary choice of MNCs is always authoritarian countries. These approaches just present the other determinants for FDI inflows which can be more significant than democratic indicators. For example, economic freedom can be a key determinant for MNC in the host countries where there is no democratic freedom. In the authoritarian countries economic freedom can be sustained by developed property right protection, low tax rates, absence of capital control and trade openness. This disproves the liberal perspective that claim economic freedom and democratic freedom go hand to hand. For critical approaches, the relationship is more complex. According to them, an authoritarian regime can provide credibility by guarantee to protect the property rights or can make the investments favorable by providing generous incentives. As it can be seen there are various possibilities for an authoritarian regime to make its country profitable for foreign investors. Therefore, critical approaches contribute me to have a broader perspective in order to understand the complex relationship between FDI and democracy. Moreover, it gives me ability to analyze the determinants of FDI inflows in Turkey comprehensively.

In the second chapter, macroeconomic indicators of Turkey between 2002-2018 is analyzed in order to understand their impact on FDI inflows. Turkey's macroeconomic performance was evaluated in three periods under AKP government, respectively, golden age, stagnation and declining. It is found that the 'transition to strong economy' program caused huge problems in Turkey's macroeconomic indicators. Thus, from the very beginning of AKP government Turkey performed poorly in the matter of macroeconomy. For example, current account deficit becomes extremely problematic and it deepens gradually under AKP government. However, it is observed that, when Turkey performs poorly, FDI could reach its historical levels in 2007. It is found that FDI inflows in Turkey tend to move together with global investment conjuncture and do not seek well-developed macroeconomy. For instance, it peaks during the economic boom in 2007 and falls sharply after the 2008 crisis.

Furthermore, while current account deficit and unemployment rates were increasing rapidly, economic growth rate was high and satisfying in the first decade of 2000s. One might attribute the high level of FDI inflows in this period to high growth rates. However, any causation is found between GDP growth rate and FDI inflows. Moreover, the growth of Turkey's economy named as speculative led growth. Because it is found that Turkey's economy dependent on hot money flows and its industry is extremely weak to survive against external shocks. Thus, Turkey's economy is highly fragile. In the last three years, when political turmoil increases within the country, Turkey's GDP became highly volatile since the economy is dependent on hot money flows. Moreover, this was followed by rapid slowdown in FDI inflows. Hence, in this chapter, macroeconomic indicators are not defined as the determinants of FDI inflows in Turkey. However, the negative effect of GDP volatility in the recent years is found on FDI inflows which might stem from increasing political turmoil. Moreover, the impact of global investment trend seems to be highly significant.

In the third chapter, democracy in Turkey was analyzed from the perspective of Freedom House data which are political rights and civil liberties. The analysis was based on the same periodization as in the chapter two. This chapter presented the change in democracy from so-called democratization period to one-man regime. Main turning points during this change is defined elaborately in order to find their impact on FDI inflows in the following chapter. Many different areas are analyzed to understand how power was consolidated under one-man; from assertive foreign policy to polarization, from limited political pluralism to presidential system. Unlike the general opinion, Turkey's democracy did not fall into danger with the state of emergency, it has been already in danger for more than 10 years. It is found that the losses in democracy did not came suddenly, it was an ongoing process. Suppressing opposition, restricting media, corruptions, increasing arrests and voter fraud was observed before the state of emergency. Therefore, it is found that democracy fell gradually under AKP government from the very beginning. The chapter concludes by comparing Turkey's current democratic structure with Freedom House's modern authoritarianism, at the end, many similarities was reached.

In the fourth chapter, I finally analyzed the effects of declining democratic factors on FDI inflows. Between 2002-2017. I conducted my analysis based on the theoretical framework and literature review of this thesis. Instead of analyzing with only one approach, I tried to look from different perspectives. In the light of internalization theory, the huge investments which are made by the world's famous MNCs in the midst of the political turmoil in Turkey are explained by the possible tight relationship with socio-political actors. In order to understand the relationship, this chapter included the interviews of those companies' managers. It is found that in return for big investments and good relations those companies get political guarantees and privileges such as tax reduction. Thus, Turkey become an efficient market for MNC who seeks to minimize its costs. Moreover, critical approaches also lead me to define the possible determinants of the huge investments when Turkey's democracy is at risk. One of the most salient determinant is stated as developed property right protection. Capital controls are found to be one of the most deterring factors of FDI inflows. According to the critical approaches, any authoritarian country can be attractive for foreign investors by providing economic freedom in the absence of capital controls. This might be the reason why Turkey got high level of FDI inflows before the state of emergency. Previously, as it is found in chapter three, Turkey had big problems in the democracy however extended freedom was provided for foreign investors. However, things have changed in the last three years and this change can be clearly seen in the current trend of FDI inflows. In the light of these, Liberal approaches remained weak to justify the favorable condition in Turkey when democracy was rapidly declining.

However, this chapter presented the decline in FDI inflows explicitly. At this point, liberal approaches were seen explanatory to explain this fact by the same decrease in democracy especially in the last three years. However, this chapter revealed that FDI was overflowing when democracy was suffering the times before. People lost their trust to judiciary system in the first decade of 2000s, Gezi Uprisings in 2013 proved the abscense of freedom of expression and belief, functioning of government broke down with the corruption scandal and in 2014 people lost their trust to fair elections. However, in 2015, FDI inflows increased. At this point, it is claimed that FDI inflows did not fall as much as democracy falls. Therefore, liberal approaches cannot be the one which explains the recent decrease in FDI inflows in the last three years.

As a conclusion, traditionally, it is claimed that the foreign investors prefer democracies over the less-democratic countries. There are many liberal studies in literature which addresses the pure relationship of economic globalization and democracy. This creates an impression on Turkey as well, particularly to the opposition. The AKP government has been criticized severely by opposition for being responsible for declining trend of FDI inflows in Turkey due to its anti-democratic actions. However, this study tried to present the fact that anti-democratic pattern of AKP's policies do not have any significant impact on FDI inflows. GDP volatility which caused by Turkey's fragile economy, global investment trend which slowdowns after 2008 crisis and increasing capital controls during the state of emergency seem to be more effective on the decreasing FDI inflows.

On the other hand, it is found that the freedoms that is provided for foreign investors, have a positive effect on FDI inflows. Therefore, some huge investments are seen in Turkey. At this point, a more pertinent criticism to government would rather be related with the unfairness of enhanced freedom to foreign investors where it is not provided for public. Moreover, the relationship of firms and socio-political actors has also been discussed in this study. Beside the comprehensive economic freedoms, good relations also play a huge role for the big investments in Turkey. In this framework, this thesis presents that the policies to foreign investors are friendly enough to pull the fruitful investments Turkey. However, in general, unfortunately Turkey's economy cannot benefit from these fruits. There can be different reasons underlying this fact, however, this is not the purpose of this study to give an explanation for this.

Democracy which is claimed to have a significant effect on FDI inflows is the main problem of this thesis, which I already discussed that it does not have any significant effect on FDI inflows. Nevertheless, the parallel slowdown between FDI inflows and democracy in the last years keep me back from fully neglecting the liberal approaches. In this study, I have reached to the conclusion that FDI and democracy has a complex relationship. FDI might be affected from decreasing democratic factors but also might not be. It depends on how democracy is defined. My purpose was to discuss the literature to provide a broader perspective on the possible determinants of FDI inflows beside democracy. Last but not the least, due to the complex relationship of FDI and democracy, future studies should elaborate this topic more often, especially today, where there is an increasing number of authoritarian leaders throughout the world.

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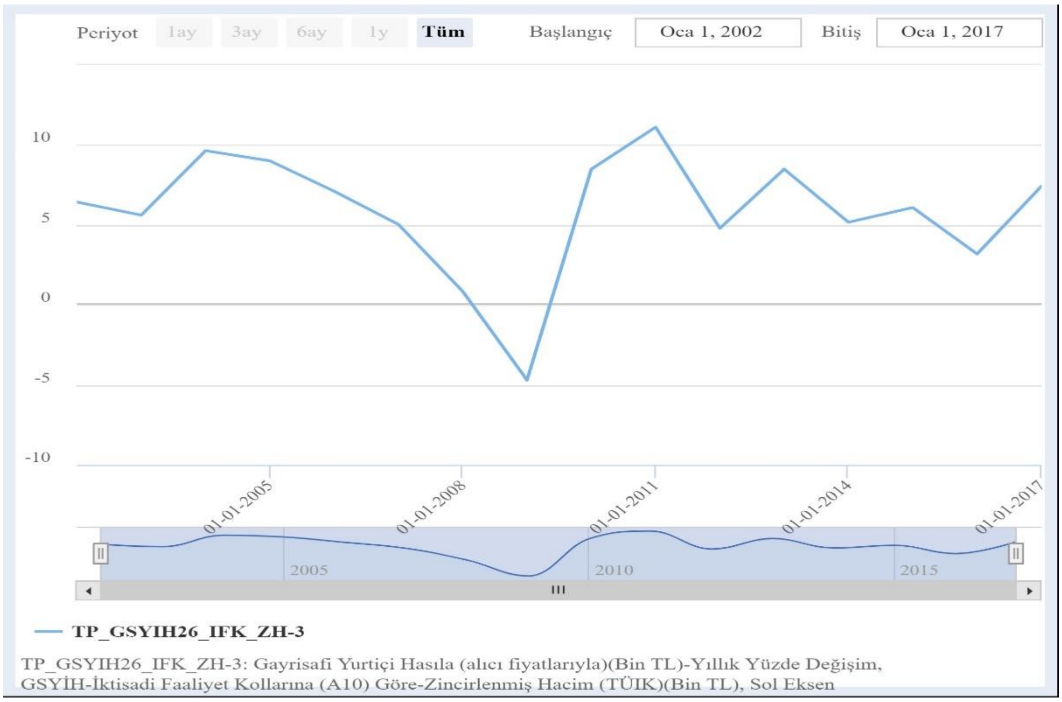
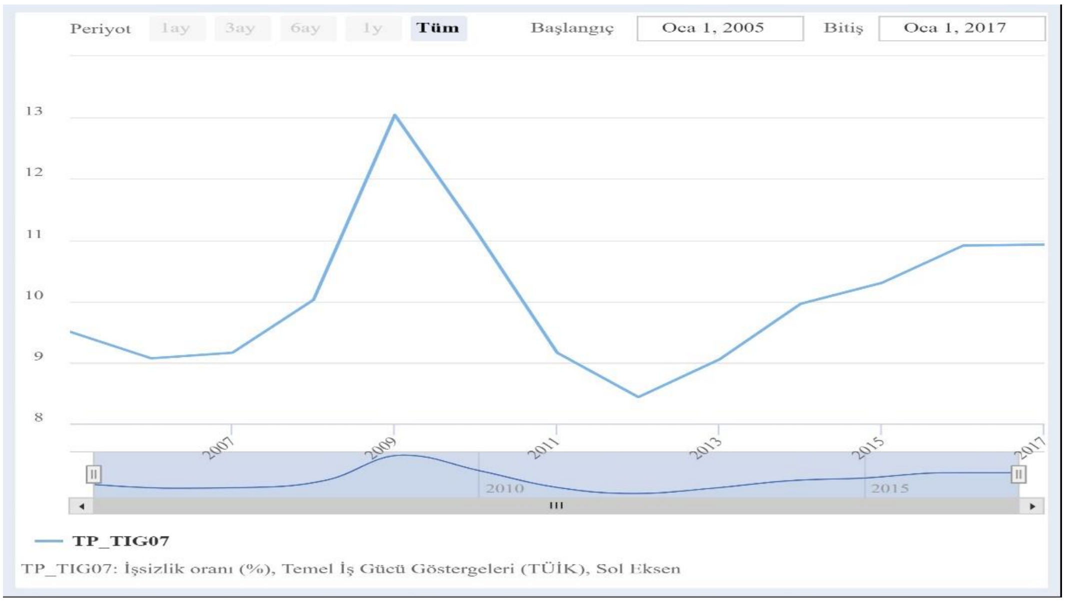
APPENDIX

Appendix 1: GDP growth (annual %) of Turkey in 2002-2017



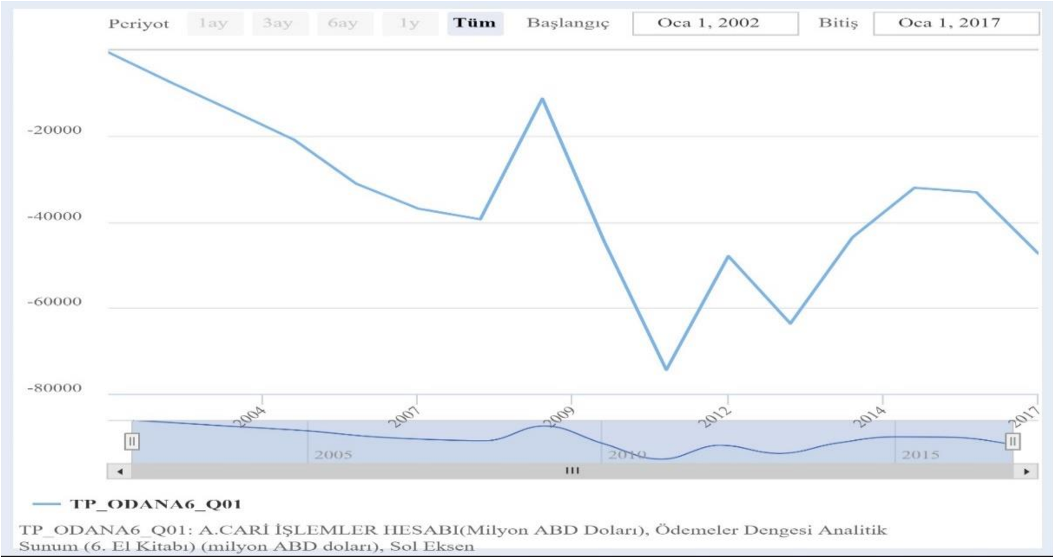
Source: (TCMB, 2018)

Appendix 2: Unemployment Rate in Turkey, 2005-2017



Source: (TCMB, 2018)

Appendix 3: Current Account Balance, Million USD



Source: TCMB 2018

Appendix 4: Member of Parliamentary General Election in Turkey, 2002-2015

Results of Parliamentary General Election by Year						
A.Number of Votes Received B.Vote Rate C.Mp Number						
Turkey						
		1 Nov. 2015	**7 Jan. 2015**	**2011**	**2007**	**2002**
Number of Registered Voters		56949009	56608817	52806322	42799303	41407027
Number of Voters Voting		48537695	47507467	43914948	36056293	32768161
Participation Rate (%)		85,2	83,9	83,2	84,2	79,1
Number of Valid Votes		46555267	45121773	42813896	34822907	31414748
Number of valid votes at foreign / customs gates		1284964	1041470	127867	226784	114035
Number of Valid Votes in Total		47840231	46163243	42941763	35049691	31528783
MP Number		550	550	550	550	550
AK PARTİ	A	23681926	18867411	21399082	16327291	10808229
AK PARTİ	B	49,5	40,9	49,8	46,6	34,3
AK PARTİ	C	317	258	327	341	363
CHP	A	12111812	11518139	11155972	7317808	6113352
CHP	B	25,3	25	26	20,9	19,4
CHP	C	134	132	135	112	178
HDP	A	5148085	6058489			
HDP	B	10,8	13,1			
HDP	C	59	80			
MHP	A	5694136	7520006	5585513	5001869	2635787
MHP	B	11,9	16,3	13	14,3	8,4
MHP	C	40	80	53	71	

Source: Tuik, https://biruni.tuik.gov.tr/secimdagitimapp/secim.zul