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## Evaluation of the Istanbul Finance Centre Potential and Its Possible Effect on the Turkish Economy

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### Abstract

*Emerging economies need foreign investments in order to capture sustainable growth trend. These transfers of funds are realized in two ways; first is foreign direct investments and the second is portfolio investments. Financial centres are becoming a centre of attraction especially for portfolio investments in their area. Finance Centre's potential of the portfolio investments is in the key position for the emerging economies in order to capture a sustainable growth. Turkey has a potential in its own region to become a finance centre.*

Keywords: Finance Centre, Foreign Direct Investment

### 1. Introduction

Emerging economies have insufficient capital problems in the economic development process compared to the developed economies and its effect of the world economy has led to a lack of effective resource allocation (Ayaydin, 2010:133). Under these conditions, developing countries capital needs are met with foreign direct investments.

The developments in economic and social lives affect the foreign direct investments directly and that developments cause that foreign direct investments start to be perceived as not only capital but also the source for creating technologic innovation and employment by providing the diversification of the investments in question (Ekinci, 2011:72).

As a result of the globalization movements, the mutual dependencies of national economies of developed and developing countries increase. Emerging markets appear as a subgroup of developing countries that can be integrated with the global financial markets macroeconomically and financially (Yaşar, 2011:3). Lack of internal savings and difficulty at accessing external financing in developing countries increases the importance of foreign direct investments (Ayaydin, 2010:134).

If we look at the obstacles to sustainable economic growth in developing countries, we need to consider these factors; low savings rate, level of insufficient productivity, low labor force participation, lack of institutional infrastructure, disruptions in the incentive system, inadequate

judicial and educational reforms, high rate bureaucracy, underground economy, barriers to access to finance, unstable political environment and unstable economic and fiscal framework(Doing Business Survey 13).

Technology brought to country via foreign direct investments, know-how, provides a basis for the creation of new trade channels and increases the export of a country in forms of a new production technique, a new product or a new organization perception (Bozdağlıoğlu, Özpinar, 2011:40).

As a result of these effects, foreign direct investments contribute to the increasing of the efficiency, modernization of businesses and development of technology in the country where the investments are realized (Bal, Göz, 2010:452).

## 2. The Role of Foreign Direct Investment in Turkey

At this point, access to financing is perceived as the most serious problem by Turkish companies and the other important factors are; tax rates, political instabilities, grey economy and unqualified labor (Investment Environment Evaluation, 2010:17). Especially, the financial crisis in 2008 caused liquidity shortage in the markets long with its effects on money and capital markets and therefore, credit institutions started avoiding to open new credits and moreover, the uncertainty in the markets and the increase in default risk caused harder credit standards and higher interest rates (Karabıyık, Anbar, 2010:48).

Heavy foreign dependency on imported products in domestic production, foreign dependency in terms of energy resources and high demand of domestic consumers for imported products are the main reasons of foreign trade deficit in Turkish economy. We can find the current account balance in the Turkish economy by adding the deficit in the investment income account and subtracting the surplus in the current transfer account. The main reason for current accounts deficit is certainly foreign trade deficit.

Table 1: Current Account Balance

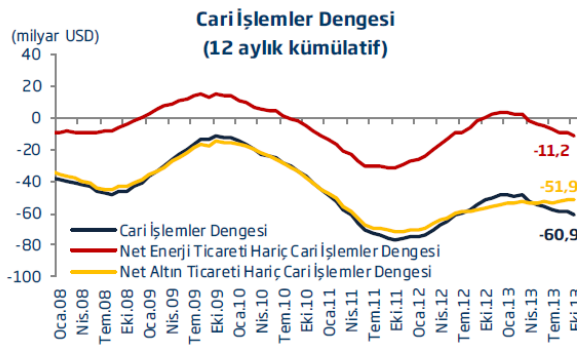
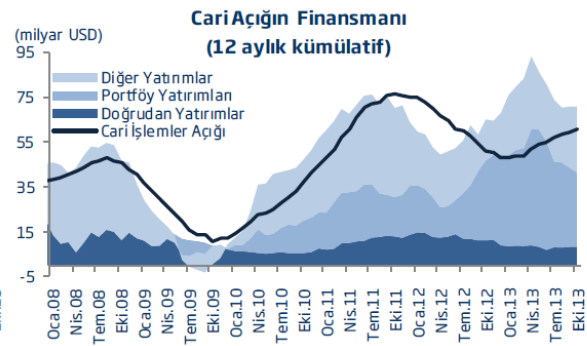


Table 2: Primary Deficit Financing



Kaynak: TCMB

(Türkiye İş Bankası, S.8)

Balance of payments stock account in financing of current deficit position, consists of two basic components. First of these components is the investments in the Turkish money and capital markets made by the foreign citizens. For the financing of current deficit, long term financing is certainly the first choice. At this point, direct investments intended to directly increase the

production volume of the country or long term portfolio investments made via capital markets can be seen as the most valuable financing resources.

### 3. Finance Center's Effect on Foreign Direct Investments

Financial markets have a key role for provide to required finance needed especially for the developing countries. Innovations observed in the financial markets enabled the markets operate more efficiently and risk dispersion conducted the more productively. Among the most important reasons for the afore mentioned financial innovations emerged are as follows;

1. The increase observed in the interest rates, inflation, share certificate prices and volatility in exchange rates,
2. Developments in computer and telecommunication technologies,
3. Academic and sophisticated education market riggers get,
4. Competition among financial instruments,
5. Tax laws and legislations developing in a way prompting financial markets (Fobozzi, Modigliani, 1996,s.32).

Philadelphia stock market is the first stock market established in the North America. New York Stock Exchange (NYSE) established in New York Wall Street a year after this has become the biggest stock market over time. First share certificate to be traded in Wall Street is exported by Bank of New York (Tanör,1999,s.10).

Royal Exchange, first stock market established in London in the second half of 16<sup>th</sup> century was an mercantile exchange and the establishment of London Stock Exchange (LSE) in 1773 followed this. London being a prominent finance center for Europe, instigated Germany and thus it tried to make good of its charge with modern financial instruments it developed on interests and indexes after 1990 and established finance centers in Frankfurt and Dusseldorf (Tanör,1999, s.12).

Apart from to Tokyo (1878) and Bombai (1860), Asian stock exchanges are generally young. Tokyo stock exchange (Nikkei) is the most important one in far east stock exchanges. Japanese financial system has entered in the a process of liberalization since the late 1970s and started to grow rapidly with the financial liberalization atmosphere the world conjuncture had been through (Tanör, 1999, s.14). The equity security trade volume in Japan in the mid 1980s, exceeded the share certificate trade volume in USA (Mishkin, Eakins, 2000, s.17). Stock exchanges of emerging economies such as Hong-Kong, Singapore, Malaysia, Korea and China have also become important stock exchanges in the last period. However, because of the cyclic uncertainties in these economies and the technical problems and lack of laws, markets in question are still not fully satisfactory in terms of authenticity (Tanör, 1999, s.14, 15).

Some strategic factors indicate investment climate and potential for to be a regional finance center.

- The size of the financial services market
- The number of international qualified financial expert
- The size of the local market
- High volume transactions capacity, capable of serving different markets

- Appropriate legal environment with the international norms
- Political and economic stability
- Effective and acceptable regulations
- Capacity to manage and set up local, regional and global scale business

These general factors are used to determine the potential for becoming a finance center. Each year, global finance center index is published to consider the final situation for finance centers.

Table:3

<b>Table 18   Competitiveness Factors and their Relative Importance</b>	
<b>Competitiveness factors</b>	<b>Rank</b>
The availability of skilled personnel	1
The regulatory environment	2
Access to international financial markets	3
The availability of business infrastructure	4
Access to customers	5
A fair and just business environment	6
Government responsiveness	7
The corporate tax regime	8
Operational costs	9
Access to suppliers of professional services	10
Quality of life	11
Culture & language	12
Quality / availability of commercial property	13
The personal tax regime	14

(GFC Index 14)

The consideration framework reveal on key indicators. These key indicators are qualified laborforce, financial products, image, legal environment, political and economic stability, regulatory framework, doing business, fiscal atmosphere, infrastructure services and tax lagistion.

Turkey is the biggest economy in Eastern Europe, Middle East, Northern Africa and Middle Asia. Turkey has a realistic potential to become a finance center from these regions. Istanbul is the biggest city in all of these regions, Istanbul's population, trade volume are the initial factors for becoming a finance center. Turkey's finance transaction actualize almost %45 percent at the Istanbul(BIMY 20).

Project of Istanbul Finance Center has a great potential for Turkish Economy. Finance Center's some major effects on Turkish Economy are;

- Turkey's GDP will consist around %8 percent from Financial Service Sector at year of 2025.
- Istanbul Finance Center Project will increase about 20 Billion \$ at GDP (According to 2006 Power Purchasing Parity)
- Financial Service Sectors labor force will rise to approximately 150000 person
- Other multiplier effects at the Turkish Economy.(DPT,İstanbul Uluslararası Finans Merkezi Stratejisi ve Eylem Planı Ekim 2009)

Bourse of Istanbul is an important part of Istanbul Finance Center Project. Every investment can be considered also as an investment for future of Istanbul Finance Center Project. Bourse of Istanbul will become an attraction center and every kind of financial instruments will trade at Bourse of Istanbul. At this point, Istanbul Finance Center Project will provide extra liquidity and lots of foreign company will listing on Bourse of Istanbul(BİST, İFM).

Table:4

**Table 8 | The Middle Eastern and African Centres in GFCI 14**

	GFCI 14 rank	GFCI 14 rating	GFCI 13 rank	GFCI 13 rating	Change in rank	Change in rating
Qatar	24	672	30	661	▲ 6	▲ 11
Dubai	25	671	23	675	▼ 2	▼ 4
Tel Aviv	32	653	New	New	New	New
Abu Dhabi	42	637	39	649	▼ 3	▼ 12
<b>Istanbul</b>	<b>44</b>	<b>633</b>	<b>57</b>	<b>626</b>	<b>▲ 13</b>	<b>▲ 7</b>
Riyadh	47	627	33	656	▼ 14	▼ 29
Bahrain	52	610	64	607	▲ 12	▲ 3
Johannesburg	61	592	62	610	▲ 1	▼ 18

(GFCI 14)

Istanbul is the only improving city between other competitor centers according to the Global Finance Center Index 2014.

#### 4. Conclusion

External financing needed is a vital factor at the developing process for Turkish economy and other developing countries economies. Turkish economy has to create new areas of employment for provide to young and fast growing population. At this point funding problem is the main factor for creating new employment areas. Turkish Household sector generally canalizes their savings to residential sector, because of this incline, foreign savings is much more important for Turkish economy according to other emerging economies.

Turkey's international position can be defined as a cultural and geographical bridge between east and west and also it connects rich underground resources area with developed countries. These features influence Turkey's potential in order to become a finance center.

Table:5 2011 10 Countries With Highest Current Deficit

Rank	Country	Current Deficit (Billion \$)	Gap to GDP Ratio
1	U.S.A	493,9	-3,2%
2	France	76,5	-2,8%
3	Italy	73,5	-3,4%
4	Spain	71,0	-4,8%
5	Turkey	64,1	-8,0%
6	Brazil	62,6	-2,6%
7	India	62,5	-3,7%
8	Great Britain	60,1	-2,4%

(Türkoğlu,2013:7)

Import oriented consumption in Turkey, and the share of imported products in Turkish industry are increasing the foreign trade deficit in Turkish economy, and therefore the current account deficit every day. Turkish economy is one of the countries with the highest current account deficit, and the proportion of current deficit to GNP is high. These reveal the foreign savings need of Turkish economy for economic growth.

At this point, the provision of foreign savings is as important as how these are evaluated for Turkish economy. These investments need to stay in the country for long term, only long term investments can increase level of production and employment. Therefore Istanbul Finance Center Project can enable Istanbul to become an investment center in the Eastern Europe and Middle Asia. These effects assure with no doubt significantly fund inflow to Turkish Economy.

Istanbul Finance Center Project creates other positive externality other than economic benefits. Competition between finance centers provides to constitute much more effective and equitable Law system, effective tax regime, new managements systems, increasing number of qualified labor force, increasing urbanization level... All these externality factors can help to increase Turkey life standards.

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