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‘‘FDI and Economic Growth in Developing Countries; A Cross Comparison between Egypt and Turkey’’

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Abstract

The following paper examined the relationship between Foreign Direct Investment and Economic Growth in Developing Countries; the main focus is on Turkey and Egypt due to similarities between two countries in terms of economic, political and historical terms. An overview on FDI; types, motivations and domestic country factors is presented. Strategies attracting FDI are examined: Fiscal and Financial Incentives, Location Strategic and Marketing Strategies. The impact of FDI on host countries is discussed. Finally, the research gap discusses factors related to both Egyptian and Turkish economy.

Keywords: FDI, Economic Growth, Developing Countries

1. Introduction

International trade and international investment flows has been a main feature of the globalization era. However, international flows of goods, services, labor, and knowledge among national borders is not a recent phenomenon. Since World War II, most countries attempted to increase the rates of their international trade flows due to the increased impact of foreign firms investing on their economic performance (Tian, 2007). When firms go international, they benefit from the increased international competition, and learn from their global operations. Moreover, these firms can help their domestic economies by providing foreign currency, enhancing domestic productivity, and employment opportunities which positively affect the national trade deficit (Carlos-Pinho, 2007).

Firms can choose from many entry modes when they decide to go international. FDI is one mode of equity ownership in the host country. FDI flows have been widely growing in last couple of years. For example: In 2003, FDI flows within entire world were 560 billion dollars, while exports of goods were about 7.3 trillion dollars, and commercial services' exports were 1.8 trillion dollars. The sales of multinational corporations' subsidiaries grew between 1990 and 2001 higher than exports. Moreover, the flow of FDI in services was 950 million dollars in 1990 and increased to 4 trillion dollars in 2002 where services were about two- thirds of the FDI total flows (Helpman, 2006).

Many researchers (Jensen, 2003; Helpman, 2006; Rajan, 2004; Camilla, 2006) stated the benefits of FDI on the host country level; FDI is considered by Helpman (2006) as a feature of productive and larger companies. Jensen (2003) stated that countries especially developing ones cannot achieve economic development without being engaged in FDI; as technology, physical capital, employment, global networks, and marketing policies are all provided by FDI. Therefore, it is a helping factor for countries to realize economic growth by enhancing domestic productivity due to global competition, providing work opportunities for domestic work force, enhancing technological knowledge whether by technology transfer from developed to less developed host countries, or through transferring knowledgeable workers, internationalizing the system of research and development, or through vertical relations with local suppliers and buyers, or horizontal relations to other complementary industries within the host country (Rajan, 2004). These investing firms affect the economic growth in host countries due to their contributions to the economic performance and competition within the host country (Camilla, 2006). Jensen (2003) stated that these benefits are related to foreign currency generated for the host country, increasing employment within the host country; this increase can be direct through employing host country nationals in the firm, or indirectly through establishing local firms operating in industries complementary to the main industry of the firm (Jensen, 2003).

Some researchers (Seyoum and Manyak, 2009; Tian, 2007; Musila and Sigue´, 2006) believe that developing countries can mostly benefit from FDI; they stated that FDI for developing countries is more than just an economic tool helping them realize economic growth. FDI is a means to reduce poverty, enhance their international trade; helping them access advanced technological knowledge. Moreover, FDI is a major financing source for domestic investments in these developing countries. In addition, FDI is an accompanying feature of privatization processes occurring in developing countries (Seyoum and Manyak, 2009). Kosack and Tobin (2006) mentioned that FDI in low and middle income countries had an annual growth rate of 17% in the period between 1995 and 2000. These developing countries consider FDI as the most stable external funding source (Kosack and Tobin, 2006).

Tian (2007) mentioned that FDI has been considered by many firms to be an effective means to realize economic growth like the four Asian tigers ‘Hong Kong, Taiwan, Singapore, and Korea’ which had set some policies to attract FDI into their countries through tax reductions and rebate (Tian, 2007). Moreover, Musila and Sigue´ (2006) stated that African countries adopted FDI as a means to face the financial constraints which hinder their development. FDI refers to the process of purchasing or creating a firm in a country by foreigners (Musila and Sigue´, 2006).

The goal of this paper is to examine the impact of FDI on economic growth in developing countries; the paper attempts to discover whether FDI negatively or positively impact host countries. The paper focuses on Turkey and Egypt as special cases worth of considering. The paper consists of five main sections; the first section is the introduction which introduces basic information about the importance of international investments, trade flows among countries, and how FDI affects the host countries especially in Africa, Asia, and The Middle East. The second section; literature review introduces an overview on firms’ motives to become international, why firms might choose to engage in FDI rather than other non-equity modes. The three types of FDI are described; the factors affecting FDI are described as well. Three major strategies to attract FDI are described. The literature then reviews some country- related factors which affect the FDI like: political, economic environment and transparency levels in the host country. Then the impact of FDI on the host country in economic terms is explained. The third section of the paper is the research gap section; it lists some shortcomings in the previous literature, then the fourth section which the conclusion is providing a brief summary about the entire paper, and finally references.

2. Literature Review

The following section provides an overview on foreign entry modes; why firms can engage in exporting, licensing, or FDI. It provides an overview on FDI; motivations of firms which engage in FDI, then types of FDI are explained in details. Afterwards, some factors affecting FDI are discussed, then some strategies which attract FDI flows are discussed, and finally the impact of FDI on host countries is discussed.

2.1. Overview on Foreign Direct Investment (FDI)

Foreign market entry mode refers to the institutional arrangements taken by the firm to facilitate the movement of its resources, products, and technology into a foreign host country (Carlos-Pinho, 2007). When firms decide to go international, they have to decide which foreign market to enter, and how to enter it. Firms have three strategic choices to select from. These choices are: FDI, exporting, and licensing. The firm can keep its operating advantages internalized if it selected FDI or exporting, it can also engage in either FDI or exporting either independently or by joining other collaborative ventures. However, risk is generally high for firms engaging in FDI although the high control degree they have over foreign operations. While for licensing, the firm externalizes its operating advantages by granting the host country's firm the usage rights of its operating procedures and technical knowledge; this means lower control degrees over marketing and operational activities and higher risks (Riportella and Cazorla-Papis, 2001). The same aspect was previously discussed by Erramilli and E.D'Souza (1995) who mentioned that firms can choose either FDI or non-FDI entry modes. The decision is based on the degree of resource commitment which the firm intends to make by having fixed investment. Generally firms prefer FDI modes if uncertainty is low in the host country; when the host and home countries are culturally proximate, sharing similar cultures and languages, firms will have high levels of resource commitment in the host country (Erramilli and E.D'Souza, 1995). Moreover, resources of the firm affect its preferred entry mode; as firms with special technological knowledge and capabilities would prefer ownership modes which help them protect their knowledge from being disseminated by local host countries (Blesa and Ripolle´s, 2008).

FDI according to Jensen (2003) is a flow of private capital from a home- country firm to another host foreign country. These capital flows might be in form of reinvestment of firm's earnings, equity capital, and inter-firm debt. FDI has a long term span and that is why it is adopted by firms willing to penetrate some local markets and use their available resources. The parent company should have more than 10 percent managerial control over the subsidiary to be FDI (Jensen, 2003). About one third of FDI flows into developing countries take the form of Mergers and Acquisitions rather than Greenfield investments. This is due to the effect of government and corporate transparency which highly affect business decisions by foreign investors. However, in 2006 the FDI into Asian countries was more than 68 percent of FDI total flows into developing countries, and this reflects the fact that FDI is unevenly distributed among developing countries. The share of developing countries in global FDI in 2006 was 448 billion $. Moreover, the FDI had the largest share of total flows of resources into developing countries (Seyoum and Manyak, 2009).

2.1.1. Motivations for FDI

Motivations for FDI include the desire of the firm to access available opportunities in the host country like lower labor costs, cheaper factors of production, less transportation costs and accessing new markets with new customers (Elli and Fausten, 2002). Rajan (2004) stated that the firm's motivations might be related to resource acquisition, market positioning, operational efficiency and strategic motives (Rajan, 2004). More specifically, the following table by Camilla (2006) summarizes the motives of firms undertaking FDI in host countries. It shows there are four objectives that each firm might be looking for; the firm might be seeking natural resources which are abundant in the host country, seeking new markets for its products and services especially if there is an opportunity to build networks, customer relations and product adaptation. Some other firms might be seeking operational efficiency which would help them cut their costs; this can be realized through hiring low wage labor, or having product mandate. And finally, there are firms which seek strategic assets such as firm-specific benefits like brand names, R&D (Camilla, 2006).

CLASSIFICATION OF MOTIVES FOR UNDERTAKING FOREIGN DIRECT INVESTMENT

Natural resource seekers	*Market seekers*	*Efficiency seekers*	*Strategic asset seekers*
Abundant raw materials Abundant raw labour Plurality of motives increase with level of economic development	Proximity to markets Customer relations Follow customers Network building Product adaptation	Relatively skilled labour at competitive wage Taking advantage of changes in external environment leading to reorganisation in • vertical integration • horizontal integration • product mandates, etc	Acquisition of firm-specific assets Associated with • networks • R&D • brands, etc

Figure 1: Motives for undertaking FDI

Source: (Camilla, 2006: 885)

2.1.2. Types of FDI

There are three major types of FDI, they are: horizontal outward FDI, vertical outward FDI, and technology seeking FDI. They are discussed below.

2.1.2.1. Horizontal Outward FDI

The horizontal outward FDI is also called market-seeking FDI which occurs when the foreign firm penetrates a foreign market by producing there and operating within many countries. This type of FDI results in replacing the domestic production by foreign production in the domestic market. However, this replacement is short term due to the fact there is no absolute horizontal production; this is because the firm might rely on its headquarters to provide it with some services or assets to operate within domestic markets although the finished product might be produced within the domestic market or within the parent country. Moreover, both foreign and home production could be integrated to achieve benefits related to cost savings for both parent and host country. This means higher revenues realized by the host country and thus domestic production increases (Herzer, 2010).

2.1.2.2. Vertical Outward FDI

Vertical outward FDI refers to an investment which is affected by the price differences in production factors; when firms relocate their production processes and stages in many locations where factors of production can be obtained at less cost. When firms restructure their chain of production and operate more efficiently, they are improving their market competitiveness and domestic production especially on the long run; the firm can realize cost savings and increase efficiency when it imports from its foreign affiliates some of intermediate goods at fewer prices (Herzer, 2010).

2.1.2.3. Technology- sourcing FDI

Technology- sourcing FDI refers to the acquisition of technology, know-how techniques, management practices, and market knowledge by foreign affiliates when the firm sources its technology base; this is achieved through either buying another foreign company or building facilities for R&D by having foreign excellence centers. When the affiliate has this knowledge, it benefits the parent country company which realizes gains in terms of increased productivity (Herzer, 2010).

2.2. Host Domestic Countries and FDI

There are some host-country related factors which affect the flows of FDI into this country; these factors are the political system, economic system, public sector transparency and private sector transparency.

2.2.1. Political System and FDI

The political environment affects the tendency of multinational firms to invest in various countries; instable countries in terms of political regimes are unattractive for foreign investors who are threatened by changing laws and declining profits in those countries as it means higher internalization costs for the foreign firm. These degrees of political risk affect the entry mode of foreign firms who prefer contractual agreements with domestic firms rather than ownership agreements when there is high political risk (Jensen, 2003).

Some researchers state that there is a positive relationship between democracy and economic growth; as democratic nations tend to consume more, also democracy is about respecting property rights which in return encourage economic growth, but democracy is also a threat to investors who fear the pressures imposed by public on the agreements (Jensen, 2003). Democracy was described by Alesina *et al* (1996) as a political system which has at least two parties represented in the free elections conducted. In a democratic system, interest groups represent a source of pressure on governments. These pressures sometimes lead to opportunistic behaviors by policy makers who attempt to increase their likelihood of being reelected (Alesina *et al,* 1996). The concept of political freedom was further described by Hann and Siermann (1998) who stated that political liberty/ freedom is evident when citizens are allowed to take part in the political process in their country; they have the rights to vote, decide who to present them in elections, and many parties are existing (Hann and Siermann, 1998).

However, democratic regimes are a source of credibility to their countries; when there is political stability, foreign investors do not fear changing policies which might make them lose their ownership and profits through events like: nationalization, expropriation of revenues, changing taxes or tariffs, and currency devaluations. On the other hand, autocracies do not respect property rights and therefore they pose a threat to investors. Meanwhile, investors might prefer to invest in authoritarian regimes as they believe they might obtain attractive agreements due to lower wages for low paid workforce. This low cost labor force is an attractive fact for investors (Jensen, 2003). This was confirmed by Verma and Brennan (2011) who stated that governmental policies highly affect the economic performance of the country and the inward and outward FDI flows; government is the main influencer of macroeconomic variables like: inflation, economic growth and trade barriers (Verma and Brennan, 2011). Political insatiability was defined by Alesina *et al* (1996) as the tendency of the executive power represented in the government to change and collapse. This change can be attributed to either unconstitutional or constitutional factors. Economic growth is negatively affected by political instability which implies uncertainty and risk to potential investors who would either invest abroad or withdraw their investments from the local unstable environment (Alesina *et al*, 1996). This instability results from the given up governmental autonomy due to the imposed contractual policies; as citizens might negatively vote while evaluating their governments' performance. This instability is due to changes in policies related to macro-policy or towards foreign investments; as host country's government might be willing to increase foreign investments to exploit them (Jensen, 2004).

2.2.2. Economic System and FDI

FDI was considered as one of necessary tools to achieve economic growth by some transition countries like Spain and Ireland which were followed by many countries from Eastern European and other developing countries. These transition countries attempted to realize an economic structural change from a socialist strict system into capitalism. These countries benefited from the flow of capital, knowledge and technology. However, these benefits are heavily depending on the host country's initial conditions at the time of investment. Developing and transition countries have few alternatives to substitute the foreign capital flows which would be generated by FDI. However, transition countries are considered relatively industrial than developing countries and this makes the case different between two groups. However, some transition industrial countries do not necessarily indicate existence of entrepreneurship and innovative activities; as most of these transition countries were based on the socialist strict system which forcefully used to transfer and exploit resources, this socialist system led to under-investing in new industries and services, and this refers to having zero innovation rates in some of these countries due to the lack of free entry and exit opportunities for firms (Camilla, 2006). Privatization is an important tool in economic transition from socialism to capitalism; it positively affects long term economic growth as it enhances the economic efficiency and property rights. Moreover, it facilitates market entry and exit for new investors due to wider absence of governmental intervention (Camilla, 2006). Hamar (1994) further mentioned that liberalizing FDI- related laws positively affects flows of capital into host countries; these capital inflows increase by a quadrant rate (Hamar, 1994).

Haan and Siermann (1998) stated that economic freedom highly affected the economic growth; when individuals in a country are free to determine the supply, demand, the effective use of resources, and their property rights are well-protected, the economic growth is more likely to occur. In these terms, economic freedom is evident when there is no physical invasion for property of individuals, individuals are free to use, trade, and exchange their property without violating property of others. Therefore, the government in an economically free country is responsible for protecting property rights of individuals without restricting their voluntary exchanges. In the period between (1980- 1994), the annual growth rate of real per capita GDP in countries with high economic freedom was 2.4%, while in 27 countries with less economic freedom had an average real GDP per capita growth rate of minus 1.3% (Haan and Siermann, 1998).

2.2.3. Transparency and FDI

Transparency was defined by Seyoum and Manyak (2009) as the process by which disclosure of information related to policies, capabilities, and preferences is facilitated to both the market and outsiders. When the business environment is transparent, the essential economic and operating information is accessible by economic agents who have all awareness about potential costs and information asymmetries. There are two types of transparency:

- **Public (Government) Sector:** a public sector is believed to transparent if the decision criteria and mechanisms are accessed by outside parties; governmental decisions, regulations, and laws are clearly provided and are considered as accountable. Public sector transparency includes information and regulatory transparency. Information transparency is about the availability of timely accurate data, and allowing governmental discussions to be known by the public. While regulatory transparency refers to the availability of clear, predictable, and consistent regulations, and appeal laws; the proposed legislation should be clearly codified and understandable. The public sector transparency highly affects business decisions and performance; as when governmental policies and regulations are clear and predictable, uncertainty will be reduced as both private and public business owners will be aware of their rights and obligations (Seyoum and Manyak, 2009).

- **Private (Corporate) Sector:** refers to the reliability degree by which private firms disclose and provide clear information about their financial and accounting practices to government and external parties. This information is important in enhancing the market efficiency in developing countries due to reduction in capital costs for firms and increases the credibility of the private sector. Therefore, foreign investors are attracted to the country and flows of capital across borders are enhanced (Seyoum and Manyak, 2009).

2.2.4. Eclectic Theory/ OLI Paradigm

The OLI paradigm by Dunning stated that three advantages affect the international investment decision by firms; ownership, localization and internationalization advantages (Kok and Ersoy, 2009). Moreover, figure 2 provides a summary of three factors in the Eclectic paradigm (Galan and Gonzalez-Benito, 2001:271).

2.2.4.1. Ownership Advantage

Many researchers explained the ownership advantages of going international (Carlos-Pinho, 2007; Jensen, 2003; Floyd and Summan, 2008). Ownership advantage rises when the foreign firm has specific skills and is willing to transfer it to other countries. There might be management or technological skills which it is willing to use in penetrating foreign markets and compete with domestic firms in host countries. Moreover, the foreign firm might have an advantage in terms of its marketing; this refers to product variety which might not exist in some eastern countries. Ownership advantages also include the flow of foreign investments and currencies among countries; these investments are source of income through taxes to the host countries' governments. Ownership advantage was further explained by Jensen (2003) who stated that the parent firm goes internationally to access some resources and advantages; these advantages might be intangible such as the global brand name, or tangible such as production facilities or processes (Jensen, 2003). It was mentioned by Carlos-Pinho (2007) that the firm should be able to benefit from its competitive advantage in the foreign market it enters. Ownership advantages are firm-specific and mainly relate to the intangible assets of the firm like its patent, trade name, the degree of international experience, firm's size, and degree of products' differentiability; the firm is likely to prefer ownership entry modes that enable it to exert full control on its ownership advantages if they can be transferred without being disseminated; this enables the firm to protect and manage its operations (Carlos-Pinho, 2007; Jensen, 2003; Floyd and Summan, 2008).

2.2.4.2. Location Advantages

Location advantages were explained by many researchers (Floyd and Summan, 2008; Carlos-Pinho, 2007). These advantages are related to cost of work force and market size. Some governments offer some financial and fiscal incentives for investors to enhance the investment environment. The market accessibility depends on level of income and size of population. Moreover, these advantages are related to less transportation and shipping costs incurred by the firm when directly producing in this foreign market rather than directly exporting. These cost savings might be related to tariffs and quotas imposed on exports, or they might be due to the nature of the good which is better to be produced domestically in the host country, this host country might provide production factors and inputs with low costs and therefore the parent firm is willing to operate in this host country (Floyd and Summan, 2008; Carlos-Pinho, 2007).

2.2.4.3. Internationalization Advantages

Jensen (2003) mentioned that Internalization is explaining the motives of the firm to be fully independently operating in the host country (Jensen, 2003). While according to Floyd and Summan (2008), Internationalization advantages are related to the entry mode into the host country. Other views believe that entry modes depend on resources availability; for examples; in the Eastern countries resources are various, and therefore many foreign investors have their own Greenfields there to make use of available resources (Floyd and Summan, 2008). However, some other disadvantages exist like the time span taken for the firm to adapt to host country's conditions including laws, regulations, and various policies. The firm might be faced with low quality labor so it incurs higher costs. However, if the firm decided to delay its entry into the domestic market, it would incur less entry costs due to available information which it can obtain about other early entrants into this domestic market, and the possibility of improvements in infrastructure and human capital increased (Elli and Fausten, 2002).

Figure 2: Model of determinant factors in the key decisions in the internationalization process

Source: (Galan and Gonzalez-Benito, 2001:271)

2.3. Strategies to attract FDI

There are some strategies to attract FDI flows; these strategies are widely implemented by countries willing to host foreign investments.

2.3.1. Investment Promotion Policies

Some countries should promote their countries to foreign investors through investment promotion strategies. Investment promotion can be defined as the processes by which some information about investment sites and available services is shared and communicated to prospect investors. That is why some countries establish a one- stop investment promotion agency to allow for smoother procedures and implementation of FDI by controlling administrative red tape and overruns costs. There are four main functions for the IPA to achieve; they are: image- building, investor facilitation and services, investment generation, and policy advocacy; image building activities are about enhancing the country's image through promoting its states, operations, and investment incentives, while investor facilities and services are about targeting those investors who operate in specific industries or sectors and attempting to reach them and meet their needs by offering suitable services, investment generation is about raising the ration of realization which refers to the FDI approvals' percentages which are turned into real investment flows, and finally policy advocacy which refers to processes to enhance the investment atmosphere and clarify aspects of the private sector, and then it is followed by services which facilitate investments. However, there are some conditions which should be met in order for the IPA to perform; it should be politically recognized and linked to governmental offices, to have involvement of private sector in its IPA board, the macro-environment for investment should be stable. However, the role of IPA is not such productive in generating investments which relate to certain sectors. The enhancement policies should not be biased towards certain sectors; they should aim at enhancing the entire investment environment to make best usage of FDIs. This can be achieved through having better educated and qualified work force, improving the country's infrastructure, enhance local technological knowledge, and enhancing the investment environment (Rajan, 2004).

2.3.2. Fiscal and Financial Incentives

Incentives are defined by Rajan (2004) as policies aiming at helping firms realize less tax burdens like accelerated depreciation rates. Incentives are considered a means to reflect attitudes of host country's government towards foreign investors. There are two types of incentives by which countries attract FDIs; there are financial incentives which are directly provided by the government to the firms which are subsidized through dedicated infrastructure or loans. While fiscal incentives are about using tax treatments like less income tax, allowances for investment, processing export zones, indirect taxes exemption. These incentives should be offered wisely by governments to avoid fiscal wars at large countries. For example: Singapore supports foreign investors through subsidies which expand to include costs related to trainings, and land acquisition; these policies positively affect both domestic and foreign firms (Rajan, 2004).

2.3.3. Location Strategic Marketing Strategies

According to Musila and Sigue´ (2006), place marketing is about how to make a certain country an attractive investment location for foreigners, there should be a strategic marketing approach followed by FDI marketers in the country. This approach should be based on primary understanding of three main issues which are: the important role played by FDI in the country development, the location-specific advantages, and the appropriate marketing strategy to implement. Some Asian countries used location's strategic marketing to attract FDI, this strategic marketing had occurred through three generations.

- The first generation was based on undifferentiated production and mass marketing. This strategy attracted investors seeking operational and organizational efficiency through cost reductions. Some financial incentives and customs were used to attract FDI especially in manufacturing sectors (Musila and Sigue´, 2006).

- The second generation was about positioning and competitive analysis. This strategy emerged because of the fierce competition among potential investment locations and the ultimate need for another competitive advantage beside operational cost savings. Therefore, competing offers were analyzed, needs of specific industries were determined, and the offers meeting those needs were proposed. Moreover, there was great consideration for the potential costs of each location along with life quality there. The positioning strategy targeted investors who had already established initial investments and are willing to invest more (Musila and Sigue´, 2006).

- The final strategy was based on prospective approach. Local clusters and synergies were formed between old and new businesses considering exploiting airports, and roads. Moreover, firms were encouraged to conduct training and research in their areas of interest. There was high consideration for quality of both life and human resources to guarantee development at cultural and intellectual levels (Musila and Sigue´, 2006).

2.4. The Impact of FDI on Host Country

FDI has some effects on host countries; it affects the host-country trade balance, domestic productivity, and the domestic economy as a whole. These effects are discussed below.

2.4.1. Horizontal and Vertical Productivity Spillovers

FDI is believed to increase the productivity if host country due to some reasons; it helps local firms in being more efficient and productive to cope with increased competitive pressures imposed on them when competing with foreign investors, also the direct transfer of knowledge helps in achieving better performance for the industry level in the host country. For example: in the 1980s, the American automotive industry improved during the initial periods of Japanese FDI in the American auto market; this improvement occurred because of the competitive pressures from Japanese firms. Moreover, the American local suppliers with low productivity sold their products to Japanese assemblers, and this improved the entire auto sector. The impact of FDI on host country productivity is reflected wither directly or indirectly; these benefits are realized through labor training and knowledge transfer into host countries. Moreover, host countries can better utilize their resources and achieve efficient allocation of resources in existing industries, there could be also less dispersion among various firms which produce similar products due to best practices adopted by both local and foreign firms (Chung *et al*, 2003). Hamar (1994) mentioned that enhanced efficiency of firms occurs after couple of years, and that is why host governments offer tax reductions and exemptions to new foreign investments during their initial operating years (Hamar, 1994).

- **Vertical Productivity Spillovers**

Vertical productivity spillovers are about forward and backward links in the markets for inputs which result in financial transactions; as it is related to the relations among industries. For example: if a trade transaction occurs between local suppliers, customers and the foreign firm which result in technology and knowledge transfer and thus leads to improvement in the local production. Moreover, if domestic manufacturers bought intermediate goods from the foreign firm, this is considered a forward linkage which improves the local productivity. A vertical spillover is called inter- industry spillovers because it involves many industries (Uttama and Peridy, 2010).

- **Horizontal Productivity Spillovers**

Horizontal Productivity spillovers occur when productivity within certain industrial sector increases due to transferred technology or technical knowledge; these spillovers are called intra- industry spillovers as the improvements are just including one single industrial sector (Uttama and Peridy, 2010).

2.4.2. FDI and Domestic Economy

Herzer (2010) stated that positive impact of FDI on domestic economies depends on the investing firm. However, it stated that local market and producers also affect the degree of positivism. These aspects relate to fierce competition between foreign and local firms. Moreover, local firms can learn from foreign firms some business practices and new technologies and therefore they increase their efficiency and productivity. The foreign firm might also produce intermediate goods at lower prices to other home country firms and this generates higher income for host countries. These positive spillovers help host countries to realize economic growth. However, if domestic consumers preferred the foreign products, then it would reduce domestic production and negatively affect the economy (Herzer, 2010). These aspects were further mentioned by Kosack and Tobin (2006); they stated that through positive externalities, FDI can indirectly enhance growth by providing up-to date technology, management practices, technically-skilled labor, and quality- control techniques. However, these positive effects highly depend on levels of human capital, existing technology, and labor wages in host countries. This human capital affects the degree to which foreign enhanced technology and management practices would be domestically absorbed (Kosack and Tobin, 2006). However, the welfare of domestic country is negatively affected. The question is evolving around the fact that these positive spillovers are realized when countries support and promote foreign investment or when they restrict these foreign investments temporarily. Some authors stated that the liberalization process should be gradual to enable the FDI to achieve positive spillovers in the economy.

Therefore, they believed that early liberalization stages require taxing the FDI for realizing increase in capital stock and enhancements in the technology by allowing time for the host country to absorb the new capital and the new technology transferred into; as the process of positive impacts depends on the country's absorptive capacity. For example: china gradually liberalized its market through step wise strategy; it began by letting FDI into some of coastal areas where Chinese government believed they need and are able to absorb the transferred technology. Chinese government allowed time for this transferred technology to be diffused into other areas and cities inland which began to be ready for further FDI through improved absorptive capacity. This explains the fact that absorptive capacity of the host country is highly affecting the positive spillovers of FDI, and that is why there are benefits for gradual entry of FDI into host markets because it allows for better technological and knowledge transfer by time passage. This means that a country can divide the FDI into some periods rather than being limited by its capacity when receiving all foreign investments one time, and this leads to higher abilities to absorb transferred technologies which in return will generate higher returns and capital stock to the host country. Moreover, the host country should set some restrictions at the beginning of allowing FDI to guarantee optimal performance and outcomes. This means there is a trade- off between short- term fast growth and short- term slower growth. The fast growth takes less time but provides less capital stock and less technological benefits. On the other hand, slow growth allows for time to increase capital stock and technological advancement. This means that governments should interfere and set some restrictions on the FDI into their lands to allow for future economy- wide learning externalities (Desmet *et al*, 2008).

FDI is a source of wealth creating assets both tangible and intangible. The host country can use these assets for production in associated industries, also skill levels are believed to improve and productivity increases as well. In addition, technology is transferred to wholly owned subsidiaries and positively affects the domestic market. For example: the total factor productivity growth of Indian firms increased when FDI inflows increased in Indian economy (Rashmi, 2004).

Moreover, Kosack and Tobin (2006) mentioned that FDI could act the same as domestic savings; reinvested profits, and equity purchased by foreign investors increase the available funds for new fixed investments. Therefore, the productive capacity of a country increases (Kosack and Tobin, 2006). However, FDI is believed to cause host countries to lose their economic control over operations which would mainly be managed by foreign firms. Moreover, the governmental subsidies and grants give foreign firms unfair advantage over local firms. In addition, the overcapacity in declining domestic demand is another negative impact of FDI in host countries. However, FDI is believed to increase the domestic market competitiveness and efficiency; as the higher the entrants into an industry are, the higher is the market competitiveness, service quality, and the lower are the prices. Moreover, IEJVs create some benefits related to risk diversification, reduced capital commitments, and less costs for firms to start up their business (Williams, 1997).

The impact of FDI on domestic industries is positive due to three reasons; competition effect: it is argued that domestic firms when competing with foreign investment enterprises they are most probably to enhance their domestic managerial operations. Linkage effect is about the observation of foreign firms by domestic counterparts which benefit from technological support and their position within the supply chain. And finally the employment effect refers to employees who work in the foreign firm then move to a domestic one with their learnt competencies. However, foreign firms can negatively affect domestic firms by both a market stealing effect, and a skill stealing effect. Market stealing effect occurs by stealing their domestic demand and sweeping them away of market due to lower costs incurred by the foreign firm and the inability of domestic counterparts to compete. In addition, there could be negative employment effect when skilled workers quit their domestic positions and work for the foreign firm, and this negatively affect the quality of domestic production. Three sources which are the capital, product, and employment affect the competition effect which can be either positive or negative, while the linkage effect is always positive. Moreover, the tangible and intangible assets of foreign invested enterprises affect the technology spillovers through capital; as the tangible assets like facilities and equipment are hard to protect within host countries as they could be instated by local competitors, and therefore they can highly impact technological spillovers, while intangible assets like patent, trade name, and copyrights are easy to protect and therefore they do not have much effect on technology spillovers. While technology spillovers through products are dependent on domestic consumption and exported goods of the foreign invested enterprise, and both its existing and recently developed goods. This is because the domestically sold products of the FIE could be imitated by domestic competitors who are positively affected. On the other hand, if the FIE exports its products to various markets, it will be hard to imitate its products so there are relatively low spillovers. In addition, if the FIE is developing a new product, it is hard to access the details and imitate it, while for existing products it is possible to imitate them by local competitors, and hence positive spillovers can be evident. And finally, the technology spillovers through labor which depend on the average salary range paid by FIE; if the salaries range are high, domestic skilled employees shift to the FIE and this negatively affect the host country through skill- stealing effect firms (Tian, 2007).

2.4.3. FDI and Domestic Trade Balance

Firms can either have FDI in either developing countries, or in advanced industrial nations. This indicates that firms might have various motives according to the host country they invest in. firms invest in AINs for accessing and penetrating markets which would raise the imports in of the host country, while they invest in developing countries to obtain low cost raw materials which would increase exports and the trade surplus. According to the market imperfection approach, FDI is preferred by firms for two main motives which are: market seeking, and factor seeking motives. Factor seeking motives include the motive for obtaining raw materials and low cost production. Factor seeking investment: is about acquiring either raw materials or production factors at lower costs. Raw material seeking investment is made by firms willing to produce goods which require raw materials relatively rare at their home country. This investment positively impacts the host country's trade balance as it creates higher exports of its raw materials (Brouthers *et al*, 1996).

In Hungary for example, the foreign debt was improved due to the inflow of foreign capital to the country. Therefore, Hungary was able to pay its interests on foreign debts without reducing the domestic financial resources (Hamar, 1994). While low cost production seeking is made by firms which globally outsource its production to access low cost production factors (Brouthers *et al*, 1996).

Market seeking investment is made by firms willing to maintain their market share certain existing exporting market it has. The firm might lose its market share if the host country has protectionist policies; host countries impose trade barriers to allow importing of items needed in final assembly at lower dollar amounts. Moreover, these barriers are a sign reflecting the inability of local firms in the host country to compete with foreign imported products, and this encourages foreign investing firms to increase their resource commitments in these host countries. In addition, most service providers and suppliers might follow the firm into the host country and establish their own FDI to gain access to their clients and take share in the market (Brouthers *et al*, 1996). This type of investment negatively affects the host country trade balance as it leads to having higher imports in the host country as most of activities undertaken by foreign investors in these host countries are import- intensive ones. For example: USA and some AINs in the European Union have high GNP per capita. However, they have trade balance deficits due to the high resource commitment by foreign firms there. For example: Japan has about 60 percent of its FDI in USA and EU (Brouthers *et al*, 1996). The countries in Central and Eastern Europe believed FDI is one of major tools helping them in transition into market economy. For example: the sales of foreign affiliates in Hungary increased by 47% in years 1992 and 1993 (Williams, 1997). Camilla (2006) mentioned that that FDI is not proved to have such positive impact on economic growth in developing countries. This is due to the fact that some countries rely solely on FDI and thus become over dependent on foreign capital in maintaining the economic desired growth. Transition countries and developing countries have different focuses on their consideration for FDI (Camilla, 2006).

3. Research Gap

While examining the literature on the relationship between FDI and economic growth, a wide lack of consideration for some developing countries like Egypt and Turkey was noticed. Although knowing that Egypt and Turkey are developing countries with similar cultural and historical trends. Both countries attempted to be economically and politically free through seeking aid of foreign international institutions such as: UN, UNICEF, IMF, WB and WTO. Both countries implemented programs for economic reforms and structural adjustments. Moreover, both countries opened their economies to attract foreign direct investments. However, neither Egypt nor Turkey achieved the expected levels of foreign direct investments.

Another important factor to consider when considering economic growth is corruption. Hayakawa *et al* (2013) mentioned that low level of corruption is related to higher inflows of foreign investments. This is due to the negative relation between political risk and FDI inflows. Corruption, internal conflicts and bureaucracy are negatively related to FDI inflows. Therefore, it means political stability, low availability of information, red tape and higher sunk costs for foreign investors. Other factors related to corruption include external conflict, lack law and rule, low levels of governmental accountability and low performing institutions. (Hayakawa *et al*, 2013).

According to some theorists, similar structural and institutional problems in developing countries led to failing efforts to liberalize their economies; these problems created maintained inequalities and imbalanced economic systems. In Turkish case, it had the military, economic and legislative powerful institutions. However, it lacked the transparency and accountability which led to its democratic gap. Moreover, its uncontrolled financial liberalization, lack of funds, differences between lending and borrowing interest rates and strict rationing of credit deferred long-run investments. Turkish asset market was unstable because of capital rough flows. Moreover, the public sector debt records went to highest levels. Therefore, Turkish economy faced many crises in years 1994, 1999 and 2001. The IMF provided its help through rescuing packages to stabilize the collapsing economy. This deregulated financial markets and goods market which were globally integrated through international trade did not lead to increased investments or enhanced macroeconomic performance; inflation rates kept increasing and economic growth rates were unstable. The widening social conflict between Turkish and Kurdish, Secularism and Islamism, urban and rural groups was also a factor in deteriorating economic performance. Moreover, military and political social classes were isolated from other classes. This led to granting them special power in terms of unquestionable conduct (Demir, 2005).

Through history, economic liberalization and free trade had its proponents who call for self-regulating markets and long run equilibrium through efficient allocation of resources. They believed that on political side, trade liberalization will lead to democratization and liberalized political system especially in developing countries. However, this transition process for developing countries into free market system was not achieved in the linear smooth mode; rates of successful transition differed from country to country. Therefore, according to proponents of liberalized markets, economic and political liberalization go parallel together. For example: Turkey as developing country implemented a new economic paradigm in terms of economic neo-liberalization. However, political system was characterized by social, ethnic, and ideological conflicts. The political and institutional environment affected the outcome of economic reform (Demir, 2005).

3.1. Overview on Egyptian Economy

Egypt attempts to realize political stability which would help it enhance its economic development. Life quality of Egyptians did not improve as the ultimate focus was like most developing countries which focused on pure economic indicators like GDP to reflect life quality. In 2007, Egypt was rated by the IMF as one of largest countries passing by an economic reform process. At the same year, it was expected that Egypt will be the highest recipient of FDI more than South Africa. While in 2006, FDI into Egypt was more than $ 6 billion (Farid, and Lazarus, 2008). As mentioned by Bonaglia and Goldstein (2006), in the period between 1995 and 2000, Egypt was the largest recipient of FDI in North Africa; total FDI into Egypt was 41 percent of total inflows into Africa. However, in 2000 and 2001, these inflows dropped by 70 percent. In June 2001, Egypt signed the association agreement with EU, and the agreement came into practice in June 2004. This agreement was expected to help Egypt enhance its international trade and FDI. However, the results were not as expected due to distortions and incomplete implemented reforms in both labor and financial markets (Bonaglia and Goldstein, 2006).

3.1.1. Factors affecting Egyptian Economy

Based on data from the Economist Intelligence Unit, Egypt has a large growing population; this poses some pressures on the government to provide job opportunities for youth. Egypt has low domestic savings rate; this is due to the large inflation rates, low interest rates. The Egyptian human capital In terms of managerial and technical talents is relatively poor. That is why investments in fields which facilitate the transfer of technical, managerial, and technological knowledge are encouraged. In 1993, the World Bank ranked Egypt as one of low income countries; it had annual per capita income of $ 635. While in 1998, the per capita income increased to $790. Therefore, Egypt moved to the category of middle income countries (Zohny, 2001). Bonaglia and Goldstein (2006) stated that FDI into Egypt is limited due to the poor investment climate and geopolitical aspects; there are two major multinational corporations which are Orascom and Oriental Weavers (OW); Egypt is a home for both MNCs (Bonaglia and Goldstein, 2006).

Bonaglia and Goldstein (2006) stated that in the period between 1996 and 2003, there was a total of 17 M&A were made by Egyptian companies; the MENA region had a total of 6 deals, Asia had 3 deals, and Gulf area had only 1 deal; that is why they mentioned that most of Egyptian Mergers and Acquisitions are done in other Islamic nations (Bonaglia and Goldstein, 2006). While for the MENA region; in 2008, FDI flows in MENA region reached $104,777, this increase was attributed to the increasing number of construction and energy projects. These FDI flows positively affected the region in terms of economic growth, job opportunities, and reduced poverty. Moreover, FDI flows reduced the strict regulations and created competitive investment markets (Fereidouni *et al*, 2011).

Although Egypt has an economic reform to liberalize the market, its political system does not catch up with this liberalization; Egypt has a bureaucratic centralized governmental system, this prevents the country from realizing economic freedom although it privatized many firms to facilitate the transition into free market system. In 2004, the Prime Minister Ahmad Nazeef stated the Egyptian government commitment to market liberalization and privatization of firms ("World investment prospects," 2011).

The country privatized many governmental owned firms; for example: the bank of Alexandria sold 80 percent share to Sanpaolo which is an Italian financial institution in 2006 in return for $1.6billion. In addition, there had been some efforts to make tax reforms, investment incentives, and efficient business practices. The government also promised to commit to free trade deal with USA. In 2006, the real GDP rose by 6.8% ("World investment prospects," 2011). However, the reform did not achieve the expected outcomes; due to the governmental corruption and bureaucracy in Egypt. Egyptian oil sector is a main sector which attracts foreign investors; it had many US firms that accounted for 65% of the total foreign investments in the oil sector. Moreover, other Arab investors from the Gulf area, and European investors from the EU invest in Egyptian oil sector. For example: BP, BG, and Royal Dutch Shell. The following graph shows the inflows of FDI in the period ranging from 2002 to 2011 in Egypt ("World investment prospects," 2011). Same aspects were further explained by Bonaglia and Goldstein (2006) who stated that Egyptian economy tends to heavily rely on Suez Canal navigation revenues, and oil exports. While more than one third of Egyptian GDP is generated by services sector including transportation and communication. The industrial sector generates about 20 percent mainly from textiles and processing food. Egyptian exports are concentrated in three major commodities which are: cotton fibers, textiles, and clothes which constitute 5 percent of total exports, oil and petroleum exports constituting 32 percent, and metals constituting 4 percent. These three items combined are 40 percent of total Egyptian exports (Bonaglia and Goldstein, 2006). The following two tables show GDP, Imports and Exports growth in Egypt for period between 2000- 2012, along with the annual FDI Inflows growth for same period.

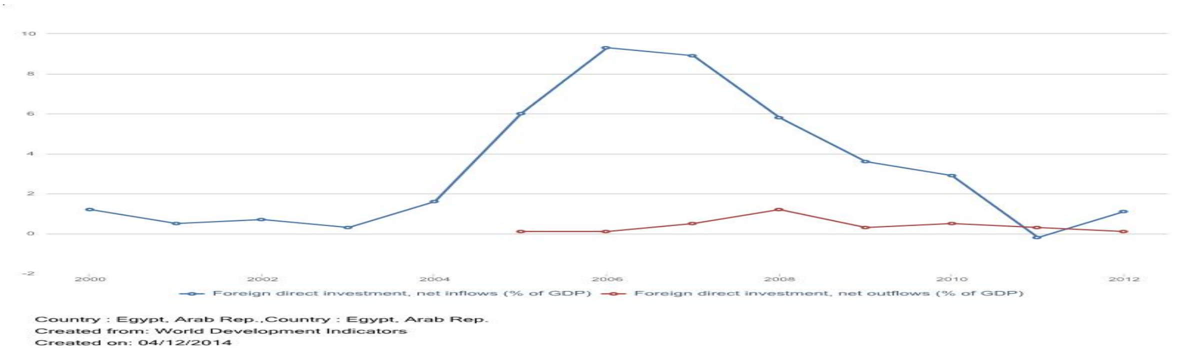

Table 3: GDP, FDI Inflows Growth in Egypt.

Source: ‘‘World Development Indicators, 2013’’

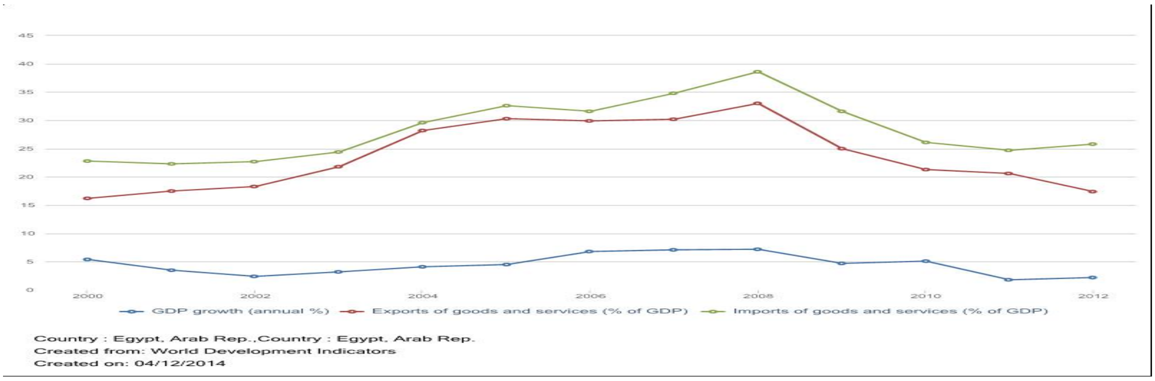

Table 4: GDP, Imports and Exports Growth in Egypt.

Source: ‘‘World Development Indicators, 2013’’

3.2. *Overview on Turkish Economy*

Turkey is the number thirteenth candidate for EU membership. It applied for the EU membership since 1987. Since December 2002, in Copenhagen the Council is promising a decision on whether Turkey fulfills the political criteria of Copenhagen which was designed in 1993. The criteria mainly relate to institutional stability, democracy, rule of law and protected minorities. In 1995, Turkey joined a Customs Union with EU in services and manufacturing and removed its tariffs and trade barriers. These efforts were a result of trade liberalization and integration with international economy. This Custom Union is covering areas related to market power, monopoly and intellectual property. So far, many European countries reject accepting Turkey in the EU. Reasons for rejecting it revolve around being different in terms of culture and religion. Moreover, it is argued that political stability criteria have not been totally fulfilled. Other reasons relate to the big geographic size of Turkey which indicates that it will be the largest country in the EU as it is estimated that by 2020, Turkish population will exceed German one. Therefore, its decision making power will be ultimate. Other countries fear that EU most funds will be targeted towards Turkey. The structure of Turkish economy is also different from European countries in terms to openness degree and welfare levels (A. de Mooij & M. Lejour, 2005).

Meyersson (2014) stated that major political, economic and social changes occurred in Turkey by 1994. These changes were fueled by the rising urbanization and deregulation. Before this date, White Turks dominated cities. White Turks are those educated, wealthy and secular people. On the other hand, Black Turks are those less educated citizens who represented the working class. They were suffering from unemployment and poverty (Meyersson, 2014).

3.2.1. <u>Factors affecting Turkish Economy</u>

There are some factors which affected the Turkish economic performance and the speed by which Turkey succeeded to reach some of its development goals. These factors such as Turkish party system and terroristic incidents greatly affected how Turkish economy performs and how social justice in terms of income distribution and education is accessed by Turkish citizens.

- *Turkish Party System*

Turkish political system received much attention due to the fact that Turkey lies in critical area surrounded by many countries politically unstable. Moreover, Turkey represents a unique case of a country achieved radical transformation in economy, while at the same time it is facing the increasing ethnic and religious based tensions. Çarkoğlu (1998) therefore focused on Turkish party system due to the fact that Turkish politics is based on dominated party systems. Çarkoğlu (1998) believed that Turkish party system was rather an intra-elite conflict based rather than societal role in national politics. It means a rise of opportunistic behaviors among voters who switch their votes among parties with similar ideologies. Therefore, the volatility in elections' results in Turkey was highest especially in some areas. This was in the following table showing the geographical distribution of Turkish local elections in years 1991, 1994 and 1995. The table reflects the fact that in Eastern and Southeastern areas the higher mean of volatility exists. Moreover, repeated military interventions attempted to implement new constitutional amendments which received no consensus among parties. Moreover, the military leadership helped create more fragmentation in the party system and interrupted the political life. This conflict represents a source for lacked ordinary political system. Therefore, these parties ought to cooperate together. However, elite domination prevents this cooperative effort (Çarkoğlu, 1998).

TABLE 1. Regional Electoral Volatility and Fractionalization in Turkey 1991–1995

Volatility index	Central Anatolia	Marmara	Eastern Anatolia	Southeastern Anatolia	Black Sea	Aegean	Mediterranean	Mean for Turkey	Explained (%) variation across regions
1991–1995	21.7	18.7	37.0	46.8	19.1	21.5	25.1	26.1	66.4
1994–1995	15.0	16.3	28.2	33.4	17.2	15.0	20.8	20.2	39.5
1991–1994	14.8	12.5	23.9	34.1	15.5	1.7	17.5	17.8	51.9

Table 5: Regional Electoral Volatility and Fractionalization in Turkey 1992-1995

Source: (Çarkoğlu, A: 1998, 549).

- *Terrorism and Turkish Economy*

Another challenge which faced Turkey in maintaining steady growth rates was terrorism. For decades, Turkish institutions, tourists and business firms were attacked and around 35,000 lives were lost. These attacks were undertaken by separatist group called KADEK which refers to Partiya Karekeren Kurdistan; this group alleged the intention of re-directing Turkey again from secular, democratic government into a religious based state. These attacks harmed the economy through levied production and transaction costs, increased military spending to face terrorists by increasing security measures. It also led to decreased in revenues from tourism and less tourism FDI. The Turkish economy suffered directly on short-run, confidence medium-term effects and long-term productivity effects. On short-run, victims' families receive living support and compensations for damaged property and infrastructure. Individuals and consumers had declining motivation to consume. Therefore, the consumption decreased and economic productivity declined. Moreover, other factors helped in increasing the instability on social and economic levels such as: high rates of unemployment, increasing urban population, and rise of leftist radical movements led by students. In the period between 1978- 1982, the Ministry of Foreign Affairs reported a total of 43,000 lost lives. The major troubles were caused by Kurds who believed there is economic disparity between their less developed ignored areas in South Eastern Turkey, and developed Western areas. The Turkish tourism sector was largely harmed due to the incidents which targeted foreign tourists who were kidnapped. Moreover, touristic places like St Sophia Mosque, the Blue Mosque, the Covered Bazaar, and Taksim Square were attacked in years 1994 and 1995. While, in 1984-2006 a total of 73 terroristic attacks were targeting transportation facilities, business firms and providers of telecommunications service. These incidents led to a declining activity and output levels. Moreover, when foreign based firms are attacked, foreign investors are much reluctant to invest more in such instable country (Öcal & Jülide, 2010).

The first two following tables show the annual GDP, Exports and Imports growth in Turkey for period ranging from years 2000- 2012. The other table shows inflows of FDI into Turkey during the same period.

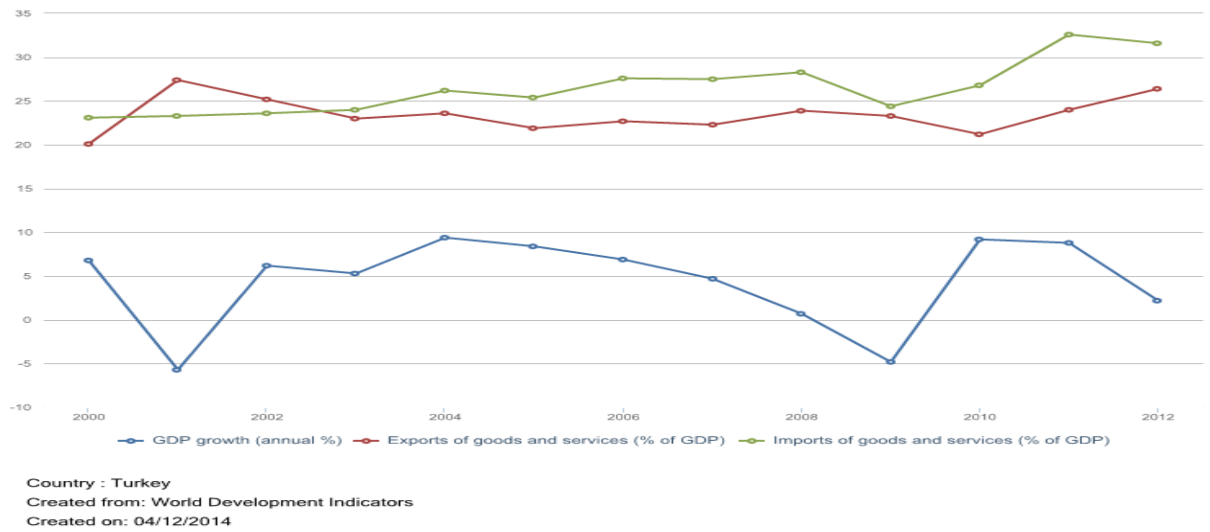

Table 6: GDP, Imports and Exports Growth in Turkey.

Source: ‘‘World Development Indicators, 2013’’

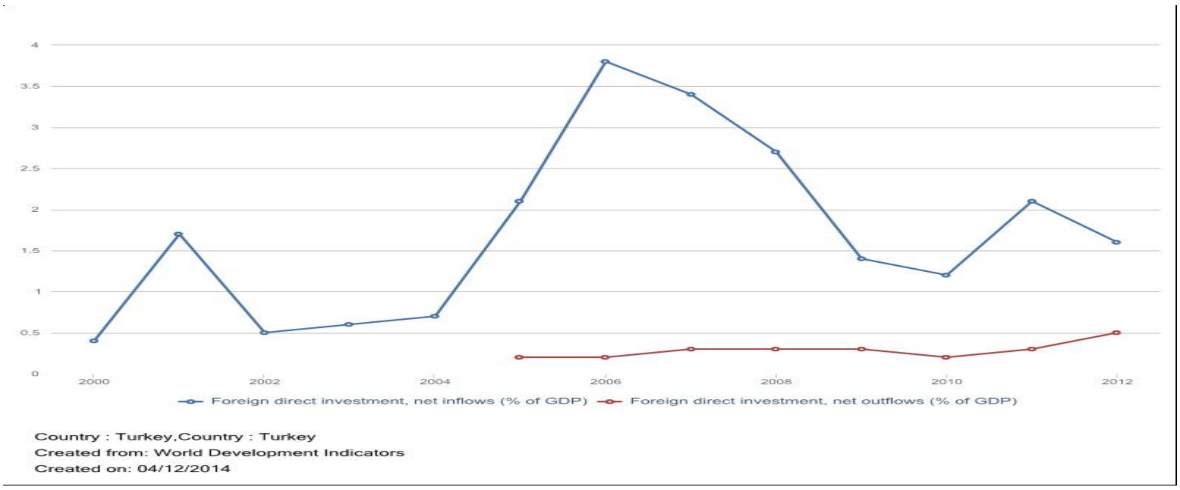

Table 7: FDI Inflows Growth in Turkey.

Source: ‘‘World Development Indicators, 2013’’

Trade Policy in Turkey

In the period from 1950s to 1970s, foreign trade policy in Turkey was based on import substituting industrialization (ISI). This policy included overvaluation of exchange rates, rationing of credit and exchange markets, strict quantitative barriers and controls on international trade. The bureaucratic state was providing subsidies to entrepreneurs;

rent seeking behavior in business environment was common, the incentive for business makers was mainly to access cheap credit and foreign exchange, and to import final and intermediate goods. Therefore, a form of distributional coalition emerged between state and business makers. The balance of payment crisis in 1970s led Turkey to adopt set of state and economic restructuring policies. These policies aimed at shrinking role of government in economic performance and democratizing the political system. However, the economic reform was based on neo-liberalism and rationality assumptions. Whereas, the political reform was based on irrationality assumption; people were assumed to be unable to determine their fate and that they are not ready for free democratic elections. This assumption led the military government at that time to adopt restrictions targeting trade unions and labor bargaining power, political parties were banned and purchasing power declined because of decreasing real wages. Therefore, outward-oriented market based growth in Turkey did not achieve the expected results (Demir, 2005).

Turkey as other countries, it adapted its economic system to international trade and economic openness requirements through signing many trade agreements. Moreover, Turkey attempted through international financial crisis to have flexible policies. This crisis was an uncontrollable external shock to Turkish economy; this was due to the fact that Turkey has mainly its trade relations with EU countries. Therefore, Turkish exporters suffered from low demand from European market with which it has a customs union. For example: Turkey was using safeguards, countervailing duties and anti-dumping policies to increase its flexibility and international trade share. Turkish trade policies were having high change rates. Therefore, high degree of uncertainty existed about access to Turkish market by foreign investors. Turkey has a duty free two-way trade with EU except in agricultural products. Moreover, Turkey mainly trades with countries with which it has free trade agreements (Bown, 2014).

In Turkey, business organizations focused on human resources management to maintain their competitive advantage. HRM is considered a developing field in a developing nation. Business environment is affected by political and economic factors. Turkish economy heavily relied on agriculture in 1920s. Nowadays, agriculture represents

around 14.5 percent of GDP with 57.8 percent devoted to service expanding sector. Therefore, the focus shifted from produced output to the human factor (Aycan, 2001).
In response to major changes occurring in the country since 1980s, Turkey is ranked as World's highly industrialized and populated country. In 1996, Turkey entered into customs union with EU which considered it as one candidate for EU membership since 1999. Human capital in Turkey received much attention through know-how, knowledge and business practices imported from EU trade partners (Aycan, 2001).

EU Membership and Turkish Economy

In October 2005, negotiations with EU began to let Turkey access EU. These negotiations were open-ended due to the uncertainty about consequences of allowing Turkey into EU. However, the economic integration through Customs Union including processed agricultural goods and manufactured goods eliminated trade barriers. For example: Mutual trade between Turkey and EU reached Euro 100 billion per annum in 2008. However, the debate on free movement of labor was maintained; Turkey is highly populated country, so inflow of Turkish migrants to EU is source of worry. In 1963, Turkey and EU signed the Association Agreement; it guaranteed the free movement of persons who are economically active. In 1970, the Additional Protocol to this Agreement led to mutual commitment to workers' free movement by 1986. However, the lack of political consensus on this free movement led to stagnation in this area. Therefore, Turkish people cannot go work or reside in EU unless they satisfy AP with EU (Wiesbrock, 2013).

In 1963, Turkey and EU signed the EC-Turkey (Ankara Agreement 'AA') which anticipated establishing customs union; aligned tax structure, integrating Turkey through three stages into the Common Agriculture Policy. These three stages were: preparatory, transitional and final stage. The agreement had trade and financial focus; the freedom of workers' movement, empowering trade and economic mutual relations, freedom of services providing and nondiscrimination between Turkish citizens or workers and other EU nationals in terms of working conditions or salary payments (Wiesbrock, 2013).

During oil crisis in 1970s, Turkey had some difficulties; global recession, political crises in terms of Cyprus issue, abused Kurdish minority and lacked democracy. All of these reasons led to rejection of first application for EU membership in 1989. Moreover, the single market objective was not completed. In 1997, European Council in Luxemburg excluded Turkey from the list of prospective candidates for EU membership. Therefore, Turkish government stopped its diplomatic dialogue with EU. However, in 1999, Turkey was listed as candidate for EU membership. This led to many amendments in Turkish constitution. Therefore in 2004, Turkey was declared to have met the Copenhagen political criteria. This was recognition for Turkey's efforts for democratization and improvement in minority rights and cancellation of death penalty. The fulfillment of Copenhagen criteria is the main condition allowing Turkey to join EU. Moreover, the framework of negotiations states that EU may entail transition long periods, certain safeguard phases or arrangements on Turkey. Moreover, the accession negotiations can be suspended in case if democracy violations, disrespect for human rights or fundamental freedoms and rule of law. Turkey also signed a protocol in which it commits itself to keep good relations with its neighbors in terms of border disputes (Wiesbrock, 2013).

4. Conclusion

The current research aims at examining the impact of FDI on economic growth in developing countries. The specification of developing countries as the focus of the research was explained, and how it was due to the traditional debate which did not result in a definite answer to the question whether FDI negatively or positively affected developing host countries. The paper started by an overview on FDI. Moreover, some motivations for firms to engage in FDI were discussed; it was clear how firms have various motives related to cost savings, operational efficiency, market seeking, and strategic assets. Furthermore, three types of FDI were described in details. Then some factors which affect FDI like the political and economic environments were discussed; it was clear how political regimes especially democratic ones have positive relationship to FDI inflows to host countries. While it was clear how economic freedom and policies are highly related to FDI inflows. Then some strategies which are used by some countries to attract FDI were discussed; Investment promotion policies are implemented by some countries to provide investment-related information to foreign investors. Other countries implement some fiscal and financial incentives to attract foreign investors through introducing tax reductions, allowances, and subsidies. Moreover, some countries follow some strategic location marketing policies to enhance the popularity of their countries as potential investment locations. Afterwards, the impact of FDI on host country was discussed. And finally the research gap was discussed; it was discussed how a wide lack of consideration for developing countries was noticed in the previous literature on the relationship between FDI and economic growth.

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