THE EFFECT OF DIRECT FOREIGN CAPITAL AND CAPITAL INVESTMENTS IN ECONOMIC DEVELOPMENT IN TURKEY AFTER 2002

Türkiye'de 2002 Sonrası Dönemlerde Doğrudan Yabancı Sermaye ve Sermaye Yatırımlarının Ekonomik Kalkınmaya Etkisi

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https://doi.org/10.5281/zenodo.18131748

Anahtar Kelimeler:
Doğrudan Yabancı Yatırımlar, Ekonomik Kalkınma, Türkiye.

JEL Kodları:
A11, B11, C11, D11.

Öz

Küreselleşme süreciyle birlikte doğrudan yabancı yatırımların (DYY) teknoloji transferi, istihdam oluşturma ve üretim kapasitesini genişletme kanalları üzerinden ev sahibi ülkelerde büyüme ve refah artışına katkı sağlayabileceği yaygın biçimde kabul edilmektedir. Bu eğilimin doğal sonucu olarak ülkeler, yatırım çekme kapasitelerini artırmak amacıyla kurumsal düzenlemelerden makroekonomik istikrara, altyapı yatırımlarından yatırım ortamının öngörülebilirliğine uzanan çok boyutlu politika setleri geliştirmekte ve yoğun bir rekabet içinde hareket etmektedir.

20.yüzyıl boyunca ekonomik, sosyal, siyasal ve kültürel alanlarda yaşanan dönüşümler; küresel ölçekte kaynak kıtlığı, özel girişimin kârlılık güdüsü ve teknolojik ilerlemelerle birleşerek sermaye hareketliliğini artırmış, ekonomiler arasındaki yakınsama sürecini hızlandırmış ve içe kapalı politika yaklaşımlarının etkisini azaltmıştır. Bu çerçevede DYY, yalnızca sermaye girişini değil, aynı zamanda bilgi, yönetim pratiği ve üretim organizasyonunun taşınması yoluyla üretkenliği artırma potansiyelini de gündeme getirmektedir.

Türkiye özelinde, yabancı sermayeyi teşvik eden düzenlemeler ve bazı yapısal avantajlara rağmen, belirli dönemlerde ekonomik ve siyasal göstergelerden kaynaklanan belirsizlikler ile yatırım ortamına ilişkin öngörülebilirlik sorunlarının, DYY girişlerini arzu edilen ölçekte sınırlayabildiği değerlendirilmektedir. Bununla birlikte Türkiye'nin demografik dinamikleri, stratejik konumu ve bölgesel değer zincirlerine eklemlenme kapasitesi dikkate alındığında; kurumsal uyum, makroekonomik istikrar ve yatırım ortamının güçlendirilmesi gibi alanlarda sağlanacak ilerlemelerin, orta vadede Türkiye'nin DYY çekim gücünü artırması beklenmektedir.

Keywords:
Foreign Direct Investment, Economic Development, Türkiye

JEL Codes:
A11, B11, C11, D11.

Abstract

With the globalization process, it is widely acknowledged that foreign direct investment (FDI) can contribute to growth and rising welfare in host countries through channels such as technology transfer, job creation, and the expansion of productive capacity. As a natural consequence of this trend, countries have been developing multi-dimensional policy packages—ranging from institutional reforms and macroeconomic stability to infrastructure investment and the predictability of the business environment—to strengthen their capacity to attract investment and to compete more effectively.

Throughout the twentieth century, transformations across economic, social, political, and cultural spheres—combined with global resource scarcity, the profit motive of private enterprise, and technological progress—have increased capital mobility, accelerated convergence among economies, and reduced the influence of inward-looking policy approaches. In this context, FDI is not viewed merely as a source of capital inflows; it is also associated with the potential to raise productivity by transferring knowledge, managerial practices, and production organization into the host economy.

In the case of Türkiye, despite foreign-capital-friendly regulations and certain structural advantages, it is assessed that uncertainties arising from economic and political indicators, together with challenges related to institutional predictability, have at times constrained FDI inflows below desired levels. Nevertheless, considering Türkiye's demographic dynamics, strategic location, and capacity to integrate into regional value chains, improvements in areas such as institutional alignment, macroeconomic stability, and investment climate governance are expected to strengthen Türkiye's ability to attract FDI over the medium term.

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1. INTRODUCTION

In an increasingly integrated global economy, foreign investment has become a strategic instrument that shapes countries' development trajectories and policy agendas, particularly with respect to growth acceleration, employment creation, welfare improvement, and international competitiveness (Seyidoğlu, 2015; Karluk, 1993). For many developing and emerging economies, a persistent constraint on these objectives is the limited accumulation of domestic savings and the resulting investment gap. Within this context, inward foreign capital is frequently positioned as a complementary source of finance and capability formation. Among the various forms of cross-border capital flows, foreign direct investment (FDI) is often considered the most development-relevant channel, because it tends to be longer-term in nature and can embed production, technology, managerial know-how, and organizational capabilities within the host economy rather than merely reallocating financial assets (Seyidoğlu, 2015; Batmaz, 2021). Nonetheless, the developmental impact of FDI is not automatic. Its net contribution depends on sectoral allocation, the structure of value chains, the degree of local linkage formation, and the quality of host-country governance and regulatory capacity (Gedikli, 2011; Kuzu, 2025).

FDI is generally defined as an investment through which a firm relocates production activities beyond national borders by establishing new production facilities (greenfield investment) or acquiring existing enterprises in a foreign country, thereby obtaining a lasting interest and a degree of managerial control (Seyidoğlu, 2003, 2015). The direction and composition of FDI are shaped by a set of motives that typically include profit maximization, access to low-cost inputs (raw materials and labor), proximity to markets, and the exploitation of regulatory and exchange-rate conditions (Akyol, 2016; Seyidoğlu, 2015). In practice, FDI is undertaken by multinational enterprises (MNEs), corporate structures that coordinate and control cross-border operations under a unified strategic logic. MNEs may centralize key decisions at headquarters while influencing affiliate decision-making through ownership structures, intra-firm trade, technology standards, and internal performance targets (Yayla, 2018; Seyidoğlu, 2015). Consequently, the effects of FDI on host economies cannot be inferred solely from capital inflow volumes; they must also be evaluated through the governance arrangements, market structures, and organizational strategies that determine how value added is created and distributed across the domestic economy.

The academic literature has developed multiple theoretical approaches to explain why MNEs invest abroad, why certain locations are selected, and why some countries are

more successful than others in attracting and benefiting from FDI. Location-focused perspectives emphasize the attractiveness of host-country characteristics—market size, infrastructure adequacy, labor quality, institutional reliability, and policy predictability—while firm-level perspectives highlight ownership advantages (technology, brand value, managerial capabilities) and internalization incentives (the preference to internalize transactions rather than rely on arm's-length contracting) (Ekici, 2011; Yayla, 2018). Parallel to these explanations, growth-oriented frameworks highlight the potential channels through which FDI may contribute to economic performance: (i) increasing the capital stock, (ii) raising productivity via spillovers, diffusion, and competition effects, and (iii) catalyzing domestic investment through restructuring and sectoral upgrading (Bilgili, Düzgün, and Uğurlu, 2007; Şimşek and Behdioğlu, 2006). At the same time, critical strands of the literature underscore possible adverse outcomes: market dominance by foreign actors, weakened domestic competition, persistent import dependence and foreign-exchange pressures, profit repatriation, export constraints imposed by intra-firm strategies, and long-run technological dependence when R&D remains concentrated at headquarters (Seyidoğlu, 1999; Fidangül, 2014).

This duality—FDI as both an opportunity and a potential source of structural risk—has become more salient under globalization. Over the twentieth century, deepening trade integration, technological leaps, and the increased mobility of capital contributed to the erosion of inward-looking development models and strengthened policy competition among countries to attract investment. In this environment, variables such as legal predictability, macroeconomic stability, institutional quality, and infrastructure capacity have gained prominence as determinants of investment attraction and retention (Batmaz, 2021; Gedikli, 2011). Yet the same processes that facilitate capital mobility also intensify competitive pressures and can magnify vulnerabilities in economies that rely heavily on imported intermediate goods or that lack robust regulatory capacity. As a result, the question is no longer merely whether a country can attract FDI, but whether it can design governance mechanisms that ensure FDI contributes to sustainable, broad-based development rather than creating enclaves of productivity with limited domestic diffusion.

Türkiye represents a particularly instructive case for examining these issues. The country has long pursued policies to attract foreign capital and to deepen integration into global markets, especially following major shifts in its development strategy toward outward orientation. Türkiye's structural features—its sizable domestic market, demographic

dynamics, strategic geography, and potential integration into regional value chains—have often been presented as advantages for investment attraction. At the same time, earlier assessments emphasize that legal and incentive frameworks alone may be insufficient to generate the desired scale and quality of inflows when broader conditions—such as macroeconomic stability, administrative efficiency, predictability in taxation and regulation, and the strength of domestic supplier ecosystems—remain constraints (Karluk, 1993; Akdiş, 1985). Moreover, even when inflows occur, their net developmental contribution depends on how production is organized: if investments concentrate at assembly stages and maintain high import-input dependency, the balance-of-payments contribution may remain limited, and the economy may experience persistent foreign-exchange pressures despite increased output (Akdiş, 1985; Kuzu, 2025). These considerations make Türkiye a useful setting for discussing not only the channels through which FDI may support growth and welfare, but also the conditions under which such gains can be undermined by structural and governance-related factors.

Another key motivation for examining FDI in the Turkish context is the need to reconcile two policy imperatives that can be in tension: (i) maximizing growth and productivity gains and (ii) maintaining external-balance sustainability. In developing and emerging economies, growth acceleration frequently induces import growth, especially when production relies on imported capital goods and intermediate input, creating a foreign exchange gap. In this setting, FDI is often framed as a "quality" form of financing because it is non-debt creating and more stable than portfolio flows. Yet, over time, profit repatriation and imported input requirements may transform one-off inflows into recurrent outflows, complicating the current account and challenging macroeconomic stability (Göçer, 2013; Aydoğuş and Öztürkler, 2006). This dynamic implies that policy debates should shift from an exclusive focus on the *volume* of FDI to the *composition* and *governance* of FDI—specifically, whether investments generate foreign-exchange-earning capacity (exports), deepen domestic value added (local suppliers), and facilitate technology diffusion (skills and R&D linkages) (Kuzu, 2025; Batmaz, 2021).

The literature further suggests that the developmental impact of FDI is mediated by host-country absorptive capacity, particularly in education and human capital formation. While FDI can facilitate the transfer of knowledge and technology, the extent to which host economies internalize these transfers depends on the quality of educational infrastructure, labor-market capabilities, and the institutional environment supporting learning and

upgrading (Taş and Yenilmez, 2008; Akin and Vlad, 2011). This observation is especially relevant for policy design in contexts where the objective is not merely to attract investment, but to ensure that investment translates into domestic capability building—through training, supplier development, and innovation diffusion—rather than remaining confined to operational routines with limited spillover effects (Batmaz, 2021; Gedikli, 2011). In other words, the central issue becomes whether FDI is integrated into a development strategy that strengthens domestic productive capacity and resilience.

Within this broad debate, the present study adopts a comprehensive and policy-relevant perspective on FDI by synthesizing the channels through which foreign capital can shape economic outcomes in Türkiye. The study is positioned within the recognition that FDI can generate both positive effects (income, employment, technology, productivity, and export potential) and adverse effects (foreign control concerns, structural dualism, competitive displacement of domestic firms, foreign-exchange pressures, export constraints, and technological dependence) (Seyidoğlu, 1999, 2015; Fidangül, 2014). Rather than treating FDI as uniformly beneficial or uniformly harmful, the study emphasizes the conditional nature of outcomes: net effects depend on the sectoral distribution of investments, the organization of production and value chains, and the regulatory and institutional mechanisms that shape linkages and spillovers.

Methodologically, this paper is based on a narrative literature synthesis that organizes conceptual and empirical arguments around key impact channels and implementation challenges relevant to the Turkish context. The analysis integrates core theoretical perspectives and established national literature to clarify mechanisms, highlight trade-offs, and derive policy-relevant insights for designing a balanced FDI framework.

The contribution of the study is threefold. First, it provides a structured overview of the main mechanisms through which FDI can affect host economies, presenting these mechanisms in a way that directly informs policy design rather than remaining purely descriptive. Second, it highlights the central trade-off between growth ambitions and external-balance sustainability by focusing on how import dependence, profit repatriation, and value-chain positioning can limit net benefits even when gross output rises. Third, by discussing both positive and adverse channels in a unified framework, it clarifies why the quality of governance—competition policy, environmental and labor standards, supplier development instruments, and institutional predictability—plays a decisive role in shaping whether FDI contributes to broad-based development (Gedikli, 2011; Kuzu, 2025).

The remainder of the paper is organized as follows. Section 2 clarifies the concept of FDI, its determinants, and its relationship with growth, distinguishing FDI from other capital-flow types and emphasizing the mechanisms through which foreign capital may affect domestic investment and productivity. Section 3 discusses the principal positive channels of FDI in the Turkish economy, including national income, balance-of-payments effects, employment, technology, growth, regional development, savings and investment dynamics, export expansion, and human-capital outcomes. Section 4 examines adverse effects and structural risks, including foreign control concerns, economic dualism, trade-policy erosion, competitive pressures on domestic firms, foreign-exchange burdens, export constraints, and technological dependence, alongside contextual factors that historically shaped inflow patterns. The concluding section synthesizes the key findings and outlines policy-relevant considerations for maximizing developmental gains while minimizing structural vulnerabilities.

2. FOREIGN DIRECT INVESTMENT (FDI)

This section provides a narrative synthesis of key studies on foreign direct investment (FDI) to clarify its conceptual foundations, main determinants, and growth-related mechanisms, and to establish a policy-relevant framework for the subsequent analysis.

2.1. The Concept and Significance of Foreign Direct Investment

Foreign direct investment (FDI) occurs when firms extend production activities beyond their home country by establishing new facilities abroad (greenfield investment), acquiring existing enterprises, or reorganizing operations through mergers and acquisitions. Unlike portfolio investment, FDI involves ownership stakes that grant the foreign investor a degree of managerial control over overseas production units. It is typically planned and implemented to serve long-term objectives (Seyidoğlu, 2015).

FDI flows are shaped by a balance of interests between investing firms and host economies. The primary motivation of FDI is to maximize commercial returns rather than to provide direct assistance to, or automatically ensure the development of, the host country. Therefore, host-country policy design must identify an optimal equilibrium in which investor profitability intersects with domestic development gains. Otherwise, economies that rely on external finance as a safeguard for their own interests may, as an outcome, become dependent on capital-exporting countries (Batmaz, 2021).

2.2. Determinants of Foreign Direct Investment

Since World War II, FDI has become a principal component of growth and development dynamics in both advanced and developing economies. Developing countries often seek to internalize the positive externalities associated with foreign capitals such as technology transfer, financing, workforce training, and access to global markets—to modernize domestic production structures and enhance competitiveness through productivity gains (Akyol, 2016). Within this context, the present study discusses the local-level implications of FDI and highlights practical challenges observed in implementation (Akyol, 2016).

FDI decisions reflect multiple motives on the part of multinational enterprises (MNEs) and investing countries. Common economic drivers include access to low-cost inputs or resource-proximate raw materials, reductions in production costs, direct entry into target markets, and the exploitation of regulatory and exchange-rate conditions. Firms may also prefer direct investment to strengthen control over supply and production chains and to protect brand value. The potential local development effects are commonly discussed along the following axes (Akyol, 2016):

1. Employment opportunities: FDI may create new jobs, increase household income, and improve living standards.
2. Technology and knowledge transfer: Training and capability-building can strengthen human capital, while managerial knowledge and innovation may diffuse into the local economy.
3. Infrastructure development: Investment may accelerate improvements in transport, energy, and telecommunications, enhancing public and private service provision.
4. Economic diversification: Reduced dependence on single sectors can diversify production, increase resilience to shocks, and mitigate macroeconomic imbalances.
5. Access to international markets: Partnerships and production networks may support local firms' access to export markets and improve competitiveness.

However, FDI can also generate adverse local externalities. Competitive pressure on domestic firms, limited spillovers, or weak enforcement of environmental standards may reduce net benefits. Accordingly, maximizing the developmental contribution of FDI

requires a balanced and effective regulatory framework, in which competition, environmental, and labor-market policies are implemented in coordination (Gedikli, 2011).

Beyond purely economic outcomes, the quality of governance and the participation of local governments and communities in decision-making are decisive for whether the gains from FDI are broadly shared. Aligning investments with local needs and institutionalizing benefit diffusion through appropriate policy instruments remain central to sustainable development strategies (Kuzu, 2025).

2.3. Benefits and Risks of Foreign Direct Investment

Countries aim to maximize the benefits of foreign capital when designing policy frameworks, yet potential risks and negative externalities should not be overlooked. While advanced economies compete intensely to attract FDI, developing economies—despite their stronger need for external resources—often raise concerns regarding sovereignty erosion, net foreign-exchange outflows, and the weakening of domestic firms' market positions (Kuzu, 2025).

When deeply integrated into host economies, FDI may yield multiple gains beyond the direct effects of job creation, income growth, and additional capital. These gains may include expanded production capacity, transfers of technological and managerial knowledge, foreign-exchange inflows, export expansion, and stronger competitive pressure in domestic markets (Kuzu, 2025). The potential positive effects are commonly summarized as follows (Seyidoğlu, 2007):

- In economies with insufficient capital accumulation, FDI can reinforce production infrastructure through initial financing and reinvested profits.
- By expanding output and employment, FDI may enlarge economic scale and broaden labor-market opportunities.
- The transfer of technology and modern management practices can strengthen institutional capabilities in host countries.
- Foreign exchange inflows may support the balance of payments through import substitution and export channels, thereby reducing vulnerabilities.
- Global experience and marketing networks may accelerate export capacity.
- In concentrated or monopolistic markets, FDI may increase competition, improve allocative efficiency, and place downward pressure on prices.

- Under an effective tax architecture, profits generated by foreign capital may contribute to public revenues (Seyidoğlu, 2007).

Nevertheless, integration of foreign capital can also create economic and political challenges. Potential risks include increased market dominance by foreign actors, deteriorating competitive conditions for domestic firms, monopolistic tendencies, weakened effectiveness of trade policies, pressure on foreign-exchange reserves, limited export potential, concentration of inflows through mergers and acquisitions, and technological dependence (Fidangül, 2014). Key vulnerabilities are often discussed on both economic and political grounds (Seyidoğlu, 2007):

- If FDI concentrates on strategic sectors, foreign firms may gain influence over economic decision-making, potentially constraining national autonomy.
- Foreign firms with superior technology and capital may create an asymmetric competitive environment for domestic SMEs, reinforcing long-run concentration.
- Foreign-capital-driven production structures may reduce the effectiveness of trade-policy tools such as tariffs and quotas.
- Imported inputs and profit repatriation may adversely affect the balance of payments and intensify exchange-rate volatility.
- Strategies that limit intra-firm competition may compress host-country export potential.
- If R&D remains at headquarters, the host economy may face persistent dependence on imported technologies.
- Entry via acquisitions rather than greenfield investments may limit employment and innovation effects.

Debates over foreign capital typically reflect political and economic value judgments. In general, however, benefits are more likely to outweigh costs when FDI is governed within a transparent and predictable framework aligned with national development priorities (Fidangül, 2014).

2.4. The Effect of Foreign Direct Investment on Economic Growth

Economic growth may be defined broadly as sustained increases in macroeconomic indicators—such as production, investment, imports, and exports—associated with

employment and productive capacity; in a narrower sense, it refers to real period-to-period increases in a country's gross national product (GNP) (Kula, 2003). Investment is widely recognized as a key driver of growth.

New investment requires savings. In developing countries where per capita income is low, domestic savings may be insufficient to finance the desired pace of growth. The gap may be partially bridged through external savings, including FDI inflows (Fidangül, 2014).

FDI is expected to increase host-country output, yet its net contribution depends on the structure of production. If foreign-invested firms substitute imported inputs for domestic ones, net value added is limited after deducting the cost of imported inputs. Profit remittances transferred to home countries must also be excluded when assessing net contributions. Opportunity costs of domestic input should be considered; if domestic inputs are idle, opportunity costs may be close to zero, increasing the measured contribution. For a more robust assessment, indirect effects such as spillovers and tax payments should be evaluated alongside direct effects. When value added generated relative to imported inputs exceeds unity, the benefit–cost outcome can be considered favorable (Karluk, 1996).

The impact of FDI on growth is commonly explained through three channels. First, FDI expands the capital stock. Second, productivity may rise through positive externalities and spillovers associated with the presence of foreign firms. Third, FDI can exert a catalytic effect on domestic investment by inducing competitive restructuring and encouraging investment in previously underdeveloped sectors. Many studies argue that FDI and domestic investment can be complementary, and the empirical literature frequently reports evidence that foreign capital supports domestic investment (Bilgili, Düzgün, and Uğurlu, 2007).

One of the primary constraints faced by emerging economies is inadequate domestic capital accumulation. Increasing FDI inflows is therefore often considered a key policy approach to narrowing this gap. A considerable body of research reports a positive association between FDI and growth (Şimşek and Behdioğlu, 2006).

FDI is also typically viewed as less volatile than portfolio investment. Portfolio flows ("hot money"), often directed toward securities markets, may amplify macroeconomic instability. For this reason, policymakers frequently prefer FDI as a more stable form of external financing (Yayla, 2018).

3. POSITIVE EFFECTS OF FOREIGN DIRECT INVESTMENT ON THE TURKISH ECONOMY

This section presents a narrative synthesis of the main channels through which foreign direct investment (FDI) can affect the Turkish economy. The discussion is structured around income, balance-of-payments, employment, and technology effects, and highlights policy-relevant implications for maximizing domestic value added and spillovers.

3.1. Income Effect

A central channel through which foreign direct investment (FDI) affects host economies is its net contribution to national income. If production associated with the investment is conducted domestically, national income is expected to increase. The magnitude of this effect depends critically on whether the inputs used in production are sourced domestically or imported (Güvercin, 2010).

Once foreign-capital operations begin, output is produced within the host country and economic value is created. However, the net contribution should be evaluated by deducting the value of intermediate inputs from the value of output generated by the investment. In addition, opportunity costs—particularly for domestic factors of production such as labor—should be considered to assess the net national-income effect more accurately (Akdiş, 1985).

In simplified form, the contribution can be expressed as (Karluk, 1993):

$$C = H - G \tag{1}$$

Where C denotes contribution, H denotes output, and G denotes the total value of inputs used.

When factor incomes and transfers are taken into account, the expression can be extended as (Karluk, 1993):

$$C = H - G = F + R \tag{2}$$

Where F represents factor incomes (wages, interest, rent, and profits), and R denotes transfers made in return for entrepreneurial services.

Importantly, foreign capital may also generate indirect income effects. Competitive pressure can raise productivity in domestic firms and stimulate entrepreneurial dynamism, generating positive external economies; conversely, if domestic firms lose competitiveness, negative externalities may emerge (Karluk, 1993). From a policy perspective, maximizing the income effect requires strengthening domestic supplier capabilities so that a larger share of value added is created locally.

3.2. Balance-of-Payments Effect

FDI has multi-dimensional effects on the host country's balance of payments.

Positive effects. The initial capital inflow may improve the balance of payments on impact. Once operations begin, further positive effects can materialize through import substitution and export channels.

Negative effects. Foreign-invested firms may import capital goods and intermediate inputs required for production. In addition, factor income remittances—such as profit repatriation, interest payments, management fees, and royalty/license payments—can generate foreign-exchange outflows and weaken the external balance.

A formal representation in the literature expresses the balance-of-payments "benefit" and "cost" components as follows (Karluk, 1993):

$$BPE = K + X + S \tag{3}$$

Where BPE is the balance-of-payments benefit, K is initial capital inflow, X is exports by affiliated/subsidiary firms, and S imports substitution.

$$BPC = (R_2 + F_1) + (M_1 + M_2) + D \tag{4}$$

Where BPC is the balance-of-payments cost, R_2 is profit remittances leaving the country, F_1 denotes other payments to foreign factors (e.g., royalties/fees/interest), $M_1 + M_2$ represent imports associated with operations and induced import demand, and D denotes disinvestment or capital withdrawal.

Based on these, the Net Benefit–Cost Ratio is defined as (Karluk, 1993):

$$NBCR = \frac{K + X + S}{(R_2 + F_1) + (M_1 + M_2) + D} \tag{5}$$

In the short run, limited factor mobility may constrain the host economy's ability to shift rapidly toward export-oriented production or strong import substitution. As a result, operations of foreign-invested firms may increase imports, potentially offsetting the one-off positive impact recorded now of capital inflow. In the Turkish context, earlier assessments emphasize that an assembly-oriented production structure and high import-input dependency may limit sustained positive contributions to the balance of payments (Akdiş, 1985). For a durable improvement, FDI must retain a foreign-exchange-generating character over the long term; otherwise, if import dependence and transfer payments exceed the initially brought-in capital, adverse effects may arise (Akdiş, 1985).

Policy implication. To strengthen the external-balance contribution, FDI policy should prioritize (i) export orientation, (ii) domestic supplier development, and (iii) reductions in structural import-input dependency in key production chains.

3.3. Employment Effect

The employment impact of FDI depends strongly on the mode of entry, the sectoral profile of investment, and the technology intensity of production.

When foreign firms establish new facilities through greenfield investment, they are more likely to create additional employment by expanding production capacity (Çolak and Alakbarov, 2017). In contrast, FDI realized through mergers and acquisitions may generate limited or even negative short-run employment effects, particularly when acquired firms undergo restructuring and labor costs—often a major cost component—are reduced (Bülbül and Emirmahmutoğlu, 2010). Nevertheless, acquisitions may preserve employment if ownership change prevents firm closure and ensures continuity of operations.

Beyond direct job creation, FDI can generate indirect employment effects through supply-chain linkages, subcontracting, and local procurement. When foreign firms source inputs domestically or when their outputs serve as intermediate goods for local industries, employment effects may spread across related sectors. Empirical studies suggest that indirect effects vary by sector, with stronger effects observed in some industries (e.g., food processing, automotive) and more limited effects in others (e.g., machinery, electronics, textiles) in developing-economy contexts (Kuzu, 2025).

For Türkiye, policy discussions often emphasize increasing employment and improving regional income distribution. The extent to which FDI supports these goals depends on whether investments flow to employment-intensive sectors and whether

production techniques are labor- or capital-intensive. Existing assessments indicate that the employment contribution of foreign-capital enterprises may remain limited when capital-intensive technologies dominate (Akdiş, 1985).

Policy implication. Employment gains are more likely when incentive schemes target greenfield projects, local procurement, and training commitments, and when sector selection is aligned with labor-absorption capacity.

3.4. Technology Effect

Technology has become a strategic determinant of competitiveness due to structural transformations in industry: larger scales, the shift from consumer goods toward intermediate and capital goods, stronger export pressures, and intensified competition on quality and costs in domestic and global markets.

For less developed countries, adopting modern technologies is essential to expand output and compete internationally. Yet, limited domestic innovation capacity often places such economies as persistent technology importers, making technology an “external” factor in production (Kazgan, 1988). If the technology introduced by foreign firms merely replaces technology that would otherwise be imported, the incremental national benefit may be limited.

A critical challenge therefore lies in selecting, adapting, and absorbing technology. Technology transfer occurs not only through FDI but also through licensing agreements, technical assistance arrangements, and machinery imports. Strengthening the institutional capacity to choose appropriate technologies and ensuring compatibility with domestic industrial strategy are key to overcoming the technology bottleneck in development (Kazgan, 1988). If imported technologies are ill-suited to local conditions, indirect adverse effects may arise over time (Akdiş, 1985).

Policy implication. To maximize spillovers, FDI governance should focus on absorptive capacity (skills, R&D, supplier upgrading), performance-oriented incentives (local R&D, training, and technology diffusion), and monitoring mechanisms that evaluate realized—not promised—technology transfer outcomes.

3.5. Effect on Growth

Assessing the impact of foreign capital on economic growth requires emphasizing that—in joint management arrangements—the choice of sector and technology is among the

principal determinants shaping growth dynamics. Beyond cyclical fluctuations, growth can be understood as an increase in the economy's productive capacity. In this respect, net additions to fixed capital formation and the scale and efficiency of new investments are central drivers of long-run growth.

To understand the investment–growth relationship more accurately, it is necessary to examine the sectoral composition of investment. In economies where high investment ratios coincide with rapid growth, investment tends to be concentrated on machinery and equipment. By contrast, in economies where investment ratios are high, but growth remains modest, construction investment often predominates. The key reason behind these divergent outcomes lies in differences in sectoral productivity dynamics. Empirical observations indicate that productivity gains in services tend to be more limited than in goods-producing sectors. Since construction investment is strongly associated with services, slower productivity growth in this domain can constrain its contribution to aggregate growth. Conversely, machinery and equipment investment is more linked to goods production and productivity improvements, thereby strengthening its growth effect.

Accordingly, for foreign-capital investment to exert a substantial and sustained impact on growth, it is commonly viewed as desirable that such investments be channeled primarily into manufacturing and productivity-enhancing activities.

Incentive frameworks should prioritize FDI projects that raise productivity (technology upgrading, machinery/equipment deepening) and expand tradable-sector capacity, rather than projects that primarily inflate low-productivity investment components.

3.6. Effect on Regional Development

Reducing economic and social disparities across geographic regions remains one of the most persistent challenges for developing economies. Interregional development differences are observed not only in developing countries but also in advanced economies. Even when incentives for lagging regions are strengthened, directing foreign capital to these areas may remain difficult. In this regard, underdeveloped regions within advanced economies—often offering higher baseline infrastructure and lower uncertainty—may appear more attractive to investors than lagging regions in developing countries (Akdiş, 1985).

The determinants foreign firms consider when selecting a host country—such as infrastructure quality, access to inputs, and market size—also shape their intra-national

location decisions. The foreign investor typically seeks regions that minimize production and transaction costs. By contrast, host governments often aim to steer investments toward lagging regions through fiscal and economic incentives to maximize social returns. The key issue, therefore, is whether incentive packages can credibly compensate not only for regional cost disadvantages but also for uncertainty costs that may materialize over time.

The effectiveness of incentives varies across investment types. For example, in capital-intensive projects, foreign firms may be more responsive to instruments that directly reduce the cost of capital (e.g., investment allowances) than to other tools. In practice, it is observed that the likelihood of channeling foreign investment into lagging regions is often higher in advanced economies than in less developed countries; this difference is attributed less to the generosity of incentives and more to the weaker bargaining power of less developed countries vis-à-vis multinational enterprises (Akdiş, 1985).

Policy implication. Regional FDI policies should combine incentives with credible improvements in infrastructure, institutional capacity, and risk reduction mechanisms; otherwise, incentive packages alone may have limited power to redirect location choices.

3.7. Effect on Savings and Investment

Per capita national income is widely used as an indicator of development level. A sustained increase in real per capita income is typically associated with expanding the volume of investment and, consequently, enlarging productive capacity (Karluk, 1993).

Raising the investment level on a continuing basis requires that part of domestic savings be redirected from consumption toward investment. At the same time, industrialization demands innovative technologies and additional capital. For developing countries facing persistent savings and capital gaps, recourse to foreign capital emerges as an important financing channel.

The contribution of FDI to investment should be maximized by policies that encourage reinvestment of earnings, support domestic savings mobilization, and promote linkages that crowd in—not crowd out—domestic investment.

3.8. Effects on Export Expansion, Foreign-Exchange Inflows, and the Closure of Current Account Deficits

In many developing countries, a structural tension exists between rapid growth ambitions and a persistent tendency for imports to rise. This dynamic produces a foreign-

exchange gap that exports struggle to cover, thereby shaping the need for external financing. Foreign capital influences the current account through multiple channels. Through foreign direct investment, production capacity can expand and firms can leverage accumulated experience, technology, and networks to strengthen exports. In addition, import substitution may be achieved by producing domestically certain goods previously sourced from abroad, yielding favorable repercussions for the balance of payments.

Foreign-capital enterprises may, in principle, offset adverse balance-of-payments effects arising from profit remittances and the importation of capital and intermediate goods through their own production and export capacity. Realizing this potential depends on channeling foreign capital into sustainable, foreign-exchange-earning activities aligned with host-country interests.

In Türkiye's case, it is observed that following 1980, the country adopted an outward-oriented development strategy and sought deeper integration into global markets by encouraging foreign-capital inflows and expanding exports.

To improve current-account outcomes, FDI attraction policies should prioritize export-oriented projects, deepen domestic supplier capacity, and reduce import dependency in key value chains, while ensuring that transfer payments do not dominate the external balance over time.

3.9. Effects on National Income and Growth

Gross domestic product (GDP)—the principal indicator of national income—measures the market value of goods and services produced within a country's borders by both domestic and foreign agents. In its narrow sense, growth is often described as an increase in national income. In developing economies, capital is scarce compared to labor. Insufficient capital accumulation can therefore constrain growth, especially when low income and savings rates perpetuate a capital gap. This gap is frequently addressed through external financing channels, including foreign direct investment (FDI).

FDI is often viewed as a tool for alleviating shortfalls in income and savings by expanding investment volume and, in turn, raising national income. Higher national income can enlarge productive capacity and may also increase employment. Proponents of FDI emphasize that new investments and advanced technologies can raise employment and improve labor quality. Improvements in skills and learning-by-doing mechanisms can

enhance productivity, and rising productivity is expected to support higher growth rates. It is also argued that skill upgrading can spill over to domestic firms, amplifying the effect.

Beyond capital formation and employment, FDI is also highlighted as a channel for technology transfer. Multinational corporations often undertake substantial R&D expenditures and may transfer advanced technologies into production processes. When technology-intensive firms enter developing economies through FDI, host countries may benefit from externalities even without directly conducting R&D. Such mechanisms are expected to strengthen human capital via learning-by-doing and to support growth through improved resource allocation, infrastructure investment, manufacturing development, and technological progress (Batmaz, 2021).

From a theoretical perspective, investment is positioned as a key determinant of growth in classical growth models such as Solow and Harrod–Domar (Acaravcı, Erdoğan, and Akalın, 2018). In the neoclassical framework, where technology is treated as exogenous, FDI is often discussed as a channel through which capital and technology enter the economy, generating potential externalities and raising per capita income by increasing capital accumulation per worker. In endogenous growth approaches, FDI may accelerate growth more persistently through technology transfer and knowledge diffusion. Technological progress may raise production and exports, while export expansion together with FDI inflows may reduce exchange-rate pressures and support macroeconomic stability (Gocer, Bulut, and Dam, 2012).

A frequently cited illustration of FDI's contribution to growth and export performance is the experience of the East Asian Tigers. Multinational firms combined advanced technologies with cost advantages to expand product variety and strengthen international competitiveness, contributing to rapid export growth. Over time, production structures evolved from subcontracting toward higher value-added activities and branding, suggesting that FDI can support both export upgrading and growth under conducive conditions (Gocer, Bulut, and Dam, 2012).

Realizing growth and income gains from FDI requires policy coherence: incentives should be tied to productivity-enhancing investment, measurable spillovers (training, local R&D, supplier upgrading), and export capacity, while governance mechanisms should monitor whether promised gains are realized in practice.

3.10. Effects on Education and Human Capital

In a broad sense, education can be defined as a planned set of activities through which individuals develop cognitive and physical competencies and undergo behavioral change in line with predetermined objectives. While classical economics conceptualized capital as a physical input, the growing role of knowledge and skills in production elevated the concept of human capital, which stands at the core of endogenous growth theories. Human capital refers to the aggregate of individuals' and societies' knowledge, skills, experience, abilities, health status, and educational attainment—i.e., the accumulated capabilities acquired through schooling and work experience. By strengthening the skills and productivity of the labor force, education raises output and national income through productivity gains (Taş and Yenilmez, 2008).

Two overarching perspectives are frequently used to explain persistent poverty in developing countries: (i) a physical-assets gap (scarcity of factories, infrastructure, and productive resources) and (ii) an ideas gap (limited access to economically valuable knowledge and organizational practices). These perspectives can coexist. From either angle, a functioning legal order, stable macroeconomic policy, and effective education systems emerge as common policy objectives because they help narrow both gaps—by enabling accumulation and by facilitating interaction, learning, and diffusion of ideas (Batmaz, 2021).

Multinational enterprises can contribute to human capital formation through training and technical support provided to local suppliers, subcontractors, and customers. Such backward and forward linkages create externalities, and labor markets become a key diffusion channel when trained workers move to domestic firms or establish new businesses. In this sense, multinationals not only introduce innovative ideas but can also strengthen the human-capital base required to adapt those ideas to local conditions (Batmaz, 2021).

However, the extent to which host countries internalize knowledge and technology transfers depends on educational infrastructure and absorptive capacity. In Romer-type frameworks, benefiting from imported or transferred technology is intricately linked to the economy's capabilities, and therefore to its level of education (Akin and Vlad, 2011; Güler, 2017). Cross-country evidence further suggests that human capital is a critical determinant for efficiency-seeking inward FDI (where productivity and skills are central), whereas it may be less decisive for market-seeking or resource-seeking investments. Cases in Southeast Asia—where skill formation and upgrading institutions were limited prior to large FDI

inflows—and in parts of Africa—where FDI has often been driven by natural resources and market access and accompanied by weak human-capital progress—support this distinction (Miyamoto, 2003; Strat, 2015). Therefore, different FDI types attach different weights to the presence of well-educated and qualified human capital in prospective host countries.

To maximize FDI-related human-capital gains, policies should link incentives to measurable training commitments, supplier upgrading, and local skill formation, while strengthening education and vocational systems that increase absorptive capacity.

3.11. Health Effect

FDI is increasingly viewed as an instrument for reducing poverty and supporting growth in developing economies. Beyond employment and capital inflows, FDI may facilitate transfers of technology and capabilities and potentially expand access to global markets (Francis, 2020). While the empirical literature has traditionally focused on growth and wages, the effects of FDI on quality-of-life components such as health have received comparatively less attention (Herzer and Nunnenkamp, 2012).

Health is a fundamental component of human capital that improves productivity at both individual and national levels. Healthy workers tend to have higher physical and cognitive capacity, lower absenteeism, and longer working lives. Children's good health supports learning and reduces school absenteeism, which can translate into improved educational outcomes and earnings prospects overall (Francis, 2020).

The World Health Organization's Commission on Macroeconomics and Health (2001) emphasizes that a healthy workforce is important for attracting investment due to its productivity effects. Foreign investors may also avoid regions with high disease prevalence and limited access to health services to reduce risks to employees (Batmaz, 2021).

Complementary health investments (primary care access, workplace safety, and public-health capacity) can improve investment attractiveness while amplifying the productivity channel through which FDI contributes to growth.

3.12. Environmental Impact

Over the past decades, the environmental consequences of carbon dioxide emissions from fossil-fuel consumption—particularly air quality deterioration and global warming—have gained increasing prominence in policy and research debates (Zeren, 2015). International governance frameworks have expanded accordingly. Following the 1992

United Nations Conference on Environment and Development (Rio), the UN Framework Convention on Climate Change entered into force in 1994, aiming to reduce human-driven greenhouse-gas emissions across key sectors such as energy, industry, transportation, and agriculture. The 1997 Kyoto Protocol introduced commitments to limit greenhouse-gas emissions, while subsequent global agendas also included environmental objectives (Batmaz, 2021).

The pollution hypothesis (Walter and Ugelow, 1979) argues that pollution-intensive industries may relocate from developed to developing countries as environmental regulations tighten in advanced economies, thereby increasing investment in jurisdictions with weaker standards. In this view, multinationals facing higher compliance costs may seek locations with more lenient regulation to preserve competitiveness, potentially making developing economies more exposed to high-pollution activities and associated CO_2 emissions (Sat, 2017; Işık and Işık, 2018).

This hypothesis is often discussed alongside comparative advantage and factor endowment arguments. Since highly polluting sectors are frequently capital-intensive, relocating production can increase environmental degradation in host countries. As income and output rise, demand for a cleaner environment may strengthen, leading to tighter regulation; firms seeking cost advantages may then shift toward countries where standards are lax or poorly enforced (Tamboğa, 2019). Additional claims link environmental neglect to international debt dynamics, suggesting that fiscal and foreign-exchange pressures can incentivize overexploitation of natural resources or tolerance of environmentally harmful activities (Batmaz, 2021).

From a sustainable development perspective, the integration of environmental protection with economic growth is central. The World Commission on Environment and Development's 1987 report *Our Common Future* (Brundtland Report) defined sustainable development as meeting present needs without compromising future generations' ability to meet theirs, highlighting the importance of environmental protection for intergenerational welfare (Işıldar, 2011).

To avoid "race-to-the-bottom" dynamics, FDI attraction strategies should embed environmental standards, monitoring, and enforcement capacity, and use incentive conditionality to encourage cleaner technologies and measurable emission reductions.

3.13. Balance-of-Payments Impact

The balance of payments (BoP) records a country's transactions with the rest of the world in foreign currency. It consists of four main components: the Current Account, the Financial Account, Net Errors and Omissions, and Official Reserves. Trade in goods and services and income flows (including profit repatriations and interest payments) are recorded in the Current Account, while cross-border capital movements—such as FDI equity flows and portfolio investments—are captured in the Financial Account. Recording discrepancies appear under Net Errors and Omissions, and reserve assets (gold, foreign exchange, and Special Drawing Rights—SDRs) are included in Official Reserves (Göçer, 2013).

Policies aimed at increasing FDI often pursue macro-objectives such as revitalizing economic activity and supporting sustainable growth. In many developing countries, however, foreign capital movements also play a decisive role in financing current-account deficits. A current-account deficit is typically financed through the Financial Account; if insufficient, other balancing items and, as a last resort, reserves may be used (Göçer, 2013). Compared to volatile portfolio flows, FDI is frequently regarded as a higher-quality, more sustainable financing source because it is non-debt creating and less prone to sudden reversals (Aydoğuş and Öztürkler, 2006).

FDI can affect the current account both directly and indirectly. While the initial equity inflow is recorded in the Financial Account, its operational phase influences the Current Account through exports, imports, and income transfers. On one hand, FDI may support exports and import substitution, contributing positively to the external balance (Kuzu, 2025). On the other hand, fragmented cross-border production and reliance on imported intermediate inputs may increase import demand and exert pressure on the BoP, especially in import-dependent export structures (Kuzu, 2025).

Profit repatriation constitutes another key determinant of the current account. Over time, profits generated by foreign-invested firms may be transferred abroad, generating foreign-exchange outflows and potentially worsening the current account balance (Göçer, Bulut, and Dam, 2012). Evidence cited for Türkiye suggests that profit transfers accounted for a non-negligible share of the current-account deficit in certain years (Göçer, Bulut, and Dam, 2012). Moreover, as some studies emphasize, one-off capital inflows associated with FDI can transform into recurrent outflows through profit repatriation; therefore, policies that

encourage the reinvestment of profits within the host country are often highlighted (Kuzu, 2025).

To improve the net external-balance contribution of FDI, policy design should (i) reduce import-input dependency, (ii) strengthen export capacity and added domestic value, and (iii) promote profit reinvestment through predictable, performance-based incentive mechanisms.

4. ADVERSE EFFECTS OF FOREIGN CAPITAL INVESTMENTS ON THE TURKISH ECONOMY

This section examines the adverse effects of foreign capital investments on the Turkish economy by mapping the main risk transmission channels through which costs may outweigh benefits. The focus is on how foreign capital can reshape economic autonomy, structural coherence, trade-policy effectiveness, market competition, external-balance dynamics, export capacity, and technological capability formation. The aim is analytical rather than ideological: foreign capital is not treated as inherently harmful, but as an instrument whose outcomes depend on sectoral allocation, governance quality, and the strength of domestic institutions. Clarifying these mechanisms is essential for understanding why inward investment may fail to generate broad-based development gains—and for identifying the conditions under which foreign capital can be aligned with national development objectives.

4.1. Increasing Foreign Control over the Economy

A distinctive feature of foreign capital investment, particularly foreign direct investment (FDI), is that they may confer decision-making authority and managerial control over enterprise operations. When foreign capital enters without a coherent strategy and adequate regulatory capacity, it may become concentrated in strategic sectors and increase foreign influence over key economic decisions. In such cases, concerns may arise regarding economic and political autonomy, including constraints on the independent pursuit of monetary, fiscal, and trade policies and a reduced capacity to implement autonomous industrial strategies. As the share of foreign capital expands, the potential magnitude of these risks may also increase (Seyidoğlu, 1999).

4.2. Erosion of Economic Coherence

Beyond questions of control, foreign capital may also affect the internal coherence of the economic structure. In less developed economies, a dualistic pattern can emerge when

foreign-owned firms operate with advanced technologies and modern organizational practices while large parts of the domestic economy remain reliant on traditional production modes. This divergence may create a bipolar production structure that limits broad-based diffusion of productivity gains and weakens integration across sectors (Seyidoğlu, 1999).

4.3. Circumvention of Trade Restrictions

Such structural fragmentation can be reinforced when foreign-invested production reduces the effectiveness of protective trade measures. Tariffs and import prohibitions are often designed to curb consumption of imported goods and encourage domestic production; however, once the relevant goods begin to be produced domestically by foreign-invested firms, compressing consumption becomes more difficult. Moreover, production rarely becomes fully "national" in input structure: in many cases, only final assembly or late stages of production take place domestically, while key raw materials and intermediate inputs continue to be imported from parent facilities abroad. As a result, domestic production may remain dependent on foreign inputs, intensifying pressure on foreign-exchange reserves despite the appearance of import substitution (Seyidoğlu, 1999).

4.4. Unfair Competitive Advantage over Domestic Firms

Import dependence and market protection can interact with competitive dynamics in ways that weaken domestic firm resilience. Foreign-owned enterprises often possess superior access to finance, advanced technology, and managerial knowledge, which may create asymmetric competition vis-à-vis small and medium-sized domestic firms. When domestic enterprises cannot compete effectively, market exit may follow; in protected markets, foreign firms may gradually obtain dominant positions, raising concerns about market power, reduced entry opportunities, and the contraction of domestic entrepreneurial space (Seyidoğlu, 1999).

4.5. Foreign Exchange Expenditure

These competitive outcomes become particularly consequential when foreign-invested firms are not export-oriented and rely heavily on imported inputs. Contrary to common expectations, foreign firms may prioritize the domestic market, procure a significant share of inputs from abroad, and remit profits overseas. Under such conditions, foreign-exchange outflows can rise and the net effect on the balance of payments may become adverse, especially when transfer payments and import requirements persist over time (Seyidoğlu, 1999).

4.6. Constraining Exports

Beyond external-balance pressures, export performance may be constrained by internal corporate strategies. Multinational enterprises may restrict the export activities of their foreign subsidiaries to avoid intra-firm competition with parent companies or other affiliates. When subsidiaries are prevented from entering certain markets—either the parent's domestic market or third-country markets under corporate control—the host country's export potential can be artificially limited, weakening the possibility that foreign investment translates into sustained foreign-exchange generation (Seyidoğlu, 1999).

4.7. Technological Dependence

Export constraints and input dependence also relate to the technological dimension. Foreign enterprises commonly concentrate research and development (R&D) activities at headquarters rather than in host countries. This can limit host-country participation in innovation processes and perpetuate dependence on externally sourced technologies. Moreover, when technological standards and production routines are externally determined, domestic learning may remain confined to operational adaptation rather than genuine capability building, potentially slowing the development of a national innovation ecosystem. Foreign capital has therefore long been debated in the economics literature: while proponents emphasize market mechanisms and efficiency gains, critics stress the need for stronger public oversight and strategic governance of multinational activities. In practice, assessments—positive or negative—often reflect political value judgments; nonetheless, a recurring analytical point is that beneficial outcomes are more likely when multinational incentives are aligned with host-country development priorities through transparent and predictable governance (Seyidoğlu, 1999).

4.8. Reasons for the Absence of Foreign Capital Inflows to Türkiye

Despite the Foreign Capital Encouragement Law No. 6224 (in force since 1954) and its liberal provisions, Türkiye historically did not attract foreign direct investment at the expected scale. This suggests that incentive-oriented regulation alone is insufficient and that broader institutional, macroeconomic, and operational conditions materially shape investment decisions. The literature highlights several factors behind historically limited inflows, including episodes of political and economic instability; bureaucratic obstacles and delays despite pro-investment rhetoric; adverse historical experiences shaping perceptions; weak coordination among public authorities in certain periods; periodic

nationalization/expropriation rhetoric; the absence of a clear and predictable practice regarding double taxation; foreign-exchange constraints that affected the importation of inputs and shaped perceptions regarding profit repatriation; infrastructure deficiencies in transport, communications, and energy; frictions surrounding the employment and remuneration of foreign personnel; limited capital-market depth; weakened market growth momentum in downturns; and frequent regulatory changes that undermined credibility (Karluk, 1993). In addition, domestic and global shocks affected inflows: the contraction following the 2001 crisis coincided with declines in private fixed capital investment, and global uncertainty in the early 2000s further reduced FDI volumes; yet attributing limited inflows solely to cyclical conditions would be incomplete, as the structural constraints enumerated above point to a need for a more coherent and comprehensive foreign capital strategy (Karluk, 1993). Source-country patterns also indicate that OECD countries have historically been the dominant origin of inflows; within the OECD, European Union member states account for a substantial share, and in the early 2000s the United Kingdom, the United States, the Netherlands, Germany, and Switzerland were frequently cited among leading source countries (Karluk, 1993), a profile that underscores the role of institutional predictability, regulatory clarity, and credible governance in shaping investor confidence and the net developmental impact of foreign capital in the Turkish case.

5.CONCLUSION

Globalization has intensified competitive pressures among countries and amplified the urgency of rapid development and adaptation to contemporary production and governance requirements. In this environment, many developing economies increasingly prioritize policy mixes designed to attract foreign direct investment (FDI) as part of broader strategies to expand productive capacity, deepen integration into global markets, and strengthen long-run growth performance. The appeal of FDI stems not only from its long-term character compared to more volatile capital flows, but also from its potential to embed production, technology, managerial knowledge, and organizational capabilities in the host economy. For this reason, inward FDI has become a core component of development visions across a wide range of developing countries.

The analysis in this study underscores that the developmental contribution of FDI is best understood through a set of interrelated channels rather than a single outcome metric. First, FDI can support macroeconomic performance by contributing to output and income generation, enlarging the tax base, and—under favorable conditions—improving the

foreign-exchange position through export expansion or import substitution. Second, it can enhance productivity and technological progress through technology transfer, the diffusion of modern management practices, and competitive pressures that encourage efficiency improvements. Third, it can expand employment opportunities and, in some cases, improve workforce quality through training, learning-by-doing, and the upgrading of skills in modern sectors. Taken together, these mechanisms explain why FDI is frequently viewed as a development-relevant form of foreign capital.

At the same time, the findings also highlight a crucial point: positive outcomes are not automatic and depend heavily on the composition of investment, the structure of value chains, and the quality of governance in the host country. The same mechanisms that can generate gains may also produce vulnerabilities when domestic linkages remain weak or when the institutional environment does not effectively steer investment toward nationally beneficial objectives. Potential adverse outcomes include heightened foreign influence in strategic sectors, dualistic production structures with limited spillovers to domestic firms, asymmetric competition that displaces local enterprises, persistent import-input dependence that increases foreign-exchange pressures, profit repatriation that transforms one-off inflows into recurrent outflows, constraints on export expansion stemming from intra-firm strategies, and technological dependence when R&D activities remain concentrated in parent-country headquarters. These risks imply that FDI, by itself, is not a sufficient instrument for accelerating growth and reducing poverty; rather, it becomes development-enhancing primarily when complemented by coherent, consistently implemented policy sets.

International experience suggests that countries that managed to translate increased foreign investment into sustained development gains typically combined openness with strong complementary conditions. Beyond liberalization, factors such as macroeconomic and political stability, predictable and transparent regulation, credible competition and privatization frameworks, effective social-policy instruments, alignment with international trade rules, participation in regional integration arrangements, targeted tax facilitation, and well-designed incentive schemes can influence both the volume and the quality of FDI. Cultural and institutional context further shapes how investors perceive risk and how effectively host economies absorb and diffuse the benefits of foreign investment. In this sense, the key distinction is not simply whether a country attracts FDI, but whether it attracts the kinds of investment that generates durable productivity gains, deepen domestic value added, and strengthen external-balance sustainability.

In the Turkish context, sectoral patterns reported in earlier assessments indicate that foreign-capitalized firms have tended to concentrate in selected manufacturing branches—such as chemicals and pharmaceuticals, electronics and machinery, and food and beverages—alongside services domains including tourism and banking. Additionally, a notable portion of FDI inflows have been associated with joint ventures, mergers, and acquisitions, which may generate different employment and innovation outcomes compared to greenfield investments. Such patterns matter because the net developmental impact of FDI depends on whether investments expand productive capacity, foster domestic supplier ecosystems, and support export upgrading, or whether they remain concentrated in activities characterized by limited spillovers and high import dependence.

Based on the mechanisms discussed throughout the paper, increasing both the scale and developmental quality of FDI in Türkiye requires a coordinated, country-level approach that strengthens institutional specialization and presents investment opportunities within a systematic, comparative, and data-driven framework. More importantly, a holistic investment-attractiveness agenda should be grounded in policy coherence, regulatory predictability, and credible implementation capacity. When these conditions are met, FDI is more likely to support sustainable development through productivity upgrading, human-capital formation, and expanded export capacity; when they are weak, foreign investment may increase output while simultaneously deepening external vulnerabilities and limiting long-run capability building. The central policy challenge, therefore, is to design governance arrangements that attract investment while ensuring that value added, learning, and competitiveness gains diffuse widely across the domestic economy.

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