

SPECIALREPORT

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Doing Business in the Broader Black Sea Region: Turkish-US Trade & Investment Perspective

Introduction

The relationship between the United States and Turkey was based primarily on defense issues for many years. The changing conjuncture in the world economy and the rising challenges and opportunities in the Black Sea region bordering Turkey and beyond are evolving this strategic alliance towards a more economic one.

The development of the business environment and enhancement of business opportunities in the region would lead to stability, peace and prosperity. The process, however, is not problem-free. The differences in developmental stages and varying degrees of economic openness of the Black Sea region countries impose serious challenges to improving business interactions.

The aim here is to identify some of the problems that might hinder promotion of private business and broader economic collaboration by considering Turkish-US companies, and offering solutions to help tackle these problems.

The first four sections present an overview of the economy and business environment in Turkey and the following Black Sea region countries: Greece, Romania, and Bulgaria (the European Union nexus of the region), and the so-called “other cluster” countries of the former Soviet Union that have all implemented economic reform packages when the Soviet Union fell apart: Russia, Ukraine, Belarus, Kazakhstan, Georgia, Armenia and Azerbaijan. These sections also assess the degree of interaction of each country with Turkey and the possibility of improving these relations.

The fifth section focuses on the degree of US-Turkish collaboration in the broader Black Sea region. The last section discusses the way forward in this regard,

The Dinu Patriciu Eurasia Center

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focusing specifically on: diversifying trade and improving businesses, legal arbitration reform, involving third countries—specifically investing in agriculture and manufacturing, developing an international financial center in Istanbul, and similarities between the United States and Turkish outflow of foreign direct investment.

The report concludes with identifying a number of emerging sectors where greater opportunities exist for US companies and their Turkish counterparts, and with how business practices can be improved with regard to other Black Sea region countries discussed in the report, based on their varying developmental stages.

Turkey in the Black Sea Region and Beyond

Turkey belongs to a number of regional and international organizations: NATO, the Organization for Economic Cooperation and Development (OECD), the Council of Europe, and the Organization for Security and Cooperation

in Europe (OSCE), as well as the United Nations, Organization of the Islamic Conference (OIC), and the World Trade Organization (WTO). In 2005, Turkey began the formal accession process with the European Union.

Turkey also has signed free trade agreements with the European Free Trade Association (EFTA), Israel, and many other countries. In 1992 Turkey and ten other regional nations formed the Black Sea Economic Cooperation (BSEC) to expand regional trade and economic cooperation.

The BSEC created a powerful regional market of 400 million people from countries bordering or near the Black Sea. This region, rich in untapped natural resources and vital industries, is one of the most difficult business activity terrains in the world. US firms can be best placed along with their Turkish partners when looking beyond the traditional Middle Eastern and North African markets to reach markets in the former Soviet Union and Eastern Europe as well as Central Asia. Turkey already acts as an important link in the East-West Southern Energy Corridor bringing Caspian, Central Asian, and Middle Eastern energy to Europe and world markets. The Baku-Tbilisi-Ceyhan pipeline, which came online in July 2006, delivers 1 million barrels of petroleum a day, and in 2007, the South Caucasus Pipeline (from Shah Deniz) started bringing natural gas from Azerbaijan to Turkey.

Turkey's connector pipeline to Greece, an important step in bringing Caspian natural gas to Europe, came online in 2007. In 2009, Turkey signed the Nabucco Intergovernmental Agreement, along with Austria, Bulgaria, Romania, and Hungary, which includes plans for a 2,000-mile natural gas pipeline running from Erzurum, Turkey, to Baumgarten, Austria, with a 31 billion cubic meter capacity. Alternative proposals to Nabucco include the Trans-Adriatic Pipeline (TAP) and the Italy-Turkey-Greece Interconnector.

The European Union Nexus in the Region: Greece, Bulgaria, Romania

Black Sea Region countries and beyond are studied hereby to highlight their differences in economic fundamentals and business practices. Some, such as Greece, Bulgaria, and Romania, are in the European Union, and are bound by its rules and regulations, despite ongoing financial problems within the EU countries. Greece in particular is at the heart of the ongoing debate about how to reform its economic

structure, which increases business opportunities for Turkey.

Greece

Greece has been in deep economic crisis since late 2009. Its international debt rating has been downgraded. Under intense pressure from the European Union and international market participants, the Greek government has adopted a medium-term austerity program that includes cutting government spending, reducing the size of the public sector, decreasing tax evasion, reforming the health care and pension systems, and improving competitiveness through structural reforms to the labor and product markets.

These unpopular reforms have been presented more recently to a public referendum, probably to thwart a political crisis, as the government faces a vocal opposition from the country's powerful labor unions and the general public. Greek labor unions are launching protest demonstrations and striking over new austerity measures, but these so far have had only a limited impact on the government's push for austerity measures. However, the jury is still out in this regard and the government's ability to implement reforms and meet budget targets can still be undermined.

In May 2011, after Greece's credit rating downgraded to the lowest possible grade, the International Monetary Fund (IMF) and Euro-zone governments provided Greece with emergency short and medium term loans so that the country could meet its short term debt obligations. In exchange for the largest bailout ever assembled, the government announced combined spending cuts and tax increases totaling \$40 billion over three years, on top of the tough austerity measures already taken. Greece's lenders have already written off 50 percent of its total debt but are calling on Athens to step up efforts in 2011 to increase tax collection, shore up public enterprises, and reduce healthcare spending. Greece was also given more time to repay its EU-IMF loan.

But investors still question whether Greece can sustain fiscal efforts in the face of a bleak economic outlook and public discontent. To start a business in Greece it takes ten days, far too long for a country that is in need of foreign capital. Greece is a low-inflation country (2.5 percent) but this can change.

Despite facing economic misfortunes, Greece is a market-based democracy and a natural ally of Turkey. More

recently, Turkish companies have been expanding in Greece and Greek companies are entering the Turkish market. Furthermore, they partner for opportunities in the region. The growth of the cross-border activity also reinforces US investors' interest in the region. Improving relations between Turkey and Greece comes from the improvement of macro-economic stability rather than enhancing the legal and business environment, although this should not be ruled out.

Bulgaria

Bulgaria, an EU member since 2007, had on average 6 percent annual growth rate between 2004–2008. This was driven by significant amounts of foreign direct investment (FDI) and consumption, as successive governments were committed to economic reforms and responsible fiscal planning. The global downturn reduced domestic demand, exports, capital inflows, and industrial production. Gross Domestic Product (GDP) contracted by approximately 5 percent in 2009, and stagnated in 2010, despite a significant recovery in exports. The economy is expected to grow modestly in 2011, however.

Corruption in the public administration, a weak judiciary, and the presence of organized crime remain significant challenges. 18 days are required to start a business in Bulgaria. A low inflation, deficit country receiving modest FDI (\$2.1 billion) with 64 percent of GDP coming from services, while agriculture's contribution is 5 percent.

The presence of Turkish companies in Bulgaria is vast and the operations of these firms cover a wide range of sectors, from food production to banking. This is facilitated by the presence of large indigenous ethnic Turks.

Romania

Romania is another Black Sea country that has joined the European Union ranks in 2007. A deficit country, Romania achieved strong GDP growth in recent years thanks to domestic consumption and investment. Romania is one of the poorest countries in the European Union, and has benefited from the membership, as it recently began to realize macroeconomic gains, spurring the creation of a middle class.

Corruption and red tape continue to handicap its business environment. Inflation increased in 2007-2008, due to stronger consumer demand, high wage growth, and rising energy costs. In this time period, Romania experienced a

nation-wide drought that affected food prices and led to the relaxation of fiscal discipline.

Romania's GDP contracted markedly in the last quarter of 2008 due to the effects of a global downturn in financial markets and trade. GDP fell more than 7 percent in 2009, at which time the government began a search for a \$26 billion emergency assistance package from the International Monetary Fund, the European Union, and other international lenders. Drastic austerity measures were introduced as part of Romania's IMF-led agreement led to a further 1.9 percent GDP contraction in 2010. The economy is expected to return to positive growth in 2011.

14 days are required to start a business in Romania, that received a \$3.4 billion FDI inflow with strong Turkish backing. Turkish businesses there also vary in the sectors as wide as food, textiles and banking.

Other Countries Cluster

The other cluster of countries which includes Russia, Ukraine, Belarus, and Kazakhstan, on the one hand, and Georgia, Armenia and Azerbaijan on the other, have all implemented economic reform packages since the collapse of the Soviet Union. Although these reforms did not produce expected outcomes as cronyism and corruption have become rampant in most of the region, they signaled a commitment to a more market-based approach to economic affairs. The reforms have produced varying degrees success amongst the clustered economies which are the focus of the next two sections.

The Hostile Fraternity: Armenia, Azerbaijan, Georgia

Armenia and Azerbaijan

Armenia, facing an acute trade deficit, has managed to bring down its rate of inflation to 10.5 percent as of 2010. The country receives a meager amount of FDI. Trade deficit is financed extensively from foreign aid and large loans from multilateral institutions. After several years of double-digit economic growth, Armenia faced a severe economic recession with GDP declining more than 14 percent in 2009. Sharp declines in the construction sector and workers' remittances, particularly from Russia, were the main reasons for the downturn.

The economy began to recover in 2010 with nearly 5 percent growth. The refinancing rate (7.25 percent)

is the key monetary policy instrument of the Armenian National Bank. Neighboring Azerbaijan is an oil rich surplus economy with high growth rates. However, some non-export sectors such as construction, banking, and real estate also reflect a double digit growth. In 2009, economic growth remained above 9 percent even as oil prices moderated and growth in the construction sector cooled.

In 2010, economic growth has slowed to 3.7 percent, although the impact of the global financial crisis was less severe than in many other countries in the region. The current global economic slowdown presents some challenges for the Azerbaijani economy as oil prices remain below their mid-2008 highs. While Turkey and Azerbaijan have close ties, Armenia keeps a distance from the two. Resolving political disputes would lead to enhanced trade and economic collaboration between the three countries. Starting a business in Azerbaijan and Armenia takes eight days while in Belarus it takes five days.

Georgia

Georgia's main economic activities include the cultivation of agricultural products such as grapes, citrus fruits, and hazelnuts; mining of manganese and copper; and output of a small industrial sector producing alcoholic and nonalcoholic beverages, metals, machinery, aircraft and chemicals. Areas of recent improvement include growth in the construction, banking services, and mining sectors, but reduced availability of external investment and the slowing regional economy are emerging risks. The country imports nearly all its needed supplies of natural gas and oil products. Railroads are part of a strategy to capitalize on Georgia's strategic location between Europe and Asia and develop its role as a transit point for gas, oil and other goods.

Georgia has historically suffered from a chronic failure to collect tax revenues; however, the government, since coming to power in 2004, has simplified the tax code, improved tax administration, increased tax enforcement, and cracked down on petty corruption. However, the economic downturn of 2008-2009 eroded the tax base and led to a decline in the budget surplus and an increase in public borrowing needs. Two days are required to start a business. Georgia is a deficit economy, patching up its current account from an inflow of FDI and foreign aid.

Belarus, Kazakhstan, Ukraine, and Russia

Belarus

Belarus on the other hand has seen limited structural reform since 1995, when President Lukashenka launched the country on the path of "market socialism." In keeping with this policy, administrative controls over prices and currency exchange rates were re-imposed. The state established its right to intervene in the management of private enterprises. Since 2005, the government has re-nationalized a number of private companies. In addition, businesses have been subjected to pressure by central and local governments, including arbitrary changes in regulations, numerous rigorous inspections, retroactive application of new business regulations, and arrests of "disruptive" businessmen and factory owners.

In Belarus, continued state control over economic operations hampers market entry for businesses, both domestic and foreign. Government statistics indicate GDP growth in 2008 was strong, surpassing 10 percent, despite a high rate of inflation and a low rate of unemployment. However, the global crisis pushed the country into recession in 2009, and GDP grew only 0.2 percent for the year. The industrial sector was hit badly by slumping foreign demand. A stand-by agreement with the International Monetary Fund was signed to assist with balance of payments deficit. In line with IMF conditions, in 2009, Belarus devalued the ruble more than 40 percent and tightened some fiscal and monetary policies.

Kazakhstan

In Kazakhstan, the global financial meltdown and the loss of capital inflows to the banks caused a credit crunch in 2007. The subsequent and sharp fall of oil prices in 2008 worsened the economic situation. Kazakhstan, entering an economic recession, responded by devaluing its currency, the *tenge*. In order to stabilize market pressures it injected \$19 billion in economic stimulus. Rising commodity prices also have helped revive Kazakhstan's economy, which registered 7 percent growth in 2010.

The country's undiversified economy, with heavy presence of non-tradable, despite a dramatic decline in oil prices, is expected to continue growth in 2011. Despite solid macroeconomic indicators, the government realizes that its economy suffers from an overreliance on oil and extractive industries, the so-called "Dutch disease."

In response, Kazakhstan has embarked on an ambitious diversification program, aimed at developing targeted sectors, such as transport, pharmaceuticals, telecommunications, petrochemicals and food processing. It is a high growing (7 percent) surplus economy, receiving nearly \$10 billion in FDI. Nineteen days are required to start a business.

Ukraine

Ukraine is known as the bread basket of the former Soviet Union. It also has a diversified heavy industry with integrated market structures to the other regions of the former USSR. Although Ukraine is dependent for its energy supplies on Russia, it is one of the most important economies in the region. Since its independence in 1991, Ukraine has set forth a program of liberalization with a legal framework for privatization as an important component of the reform. The liberalization effort has failed as Ukraine experienced a contraction.

Ukraine is strategically an important country, as it has been proven by a two week dispute that saw gas supplies cut-off to Europe in the recent past. Ukraine has ended up with a ten year gas supply agreement and transit contract with Russia.

The resistance to economic reform in Ukraine renders the government weak in dealing with tax and customs privileges and the large shadow economy. Corruption is rampant with weak law enforcement.

The country is a steel producer and exporter, which also contributed to real GDP growth of 7 percent in 2006-2007. Ukraine reached an agreement with the International Monetary Fund for a \$16.4 billion Stand-By Arrangement in November 2008 to deal with the economic crisis. The drop in steel prices and Ukraine's exposure to external impact lowered growth in 2008 and the economy contracted more than 15 percent in 2009.

The government asked the International Monetary Fund to postpone the controversial increase of gas and heating tariffs, as the Yanukovych administration is confident about cash stripped Naftogaz' deficit even without these increases. The number of days required to start a business in Ukraine is twenty-four.

Russia

The Russian economy was one of the hardest hit by the 2008-2009 global economic crisis as oil prices plummeted

and the foreign credits that Russian banks and firms relied on dried up. The Russian Central Bank spent one-third of its \$600 billion international reserves, the world's third largest, in late 2008, to slow the devaluation of the ruble. The government also devoted \$200 billion in a rescue plan to increase liquidity in the banking sector and aid Russian firms unable to roll over large foreign debts coming due.

The economic decline bottomed out in mid-2009 and the economy began to grow in the first quarter of 2010. However, a severe drought and fires in central Russia reduced agricultural output, prompting a ban on grain exports for part of the year, and slowed growth in other sectors such as manufacturing and retail trade.

High oil prices buoyed Russian growth in the first quarter of 2011 and could help Russia reduce the budget deficit inherited from the lean years of 2008 to 2009, but inflation and increased government expenditures may limit the positive impact of these revenues. Russia's long-term challenges include a shrinking workforce, a high level of corruption, difficulty in accessing capital for smaller, non-energy companies, and poor infrastructure in need of large investments.

Russia is a surplus economy by \$71 billion and a growth rate of 4 percent. It still receives a record high FDI inflow of \$43 billion. GDP grew 4.8 percent in 2010, in part, on the strength of renewed export growth.

On January 1, 2010, Russia, Kazakhstan and Belarus launched a customs union, with unified trade regulations and customs codes still under negotiation. In late January, Russia and Belarus amended their 2007 oil supply agreement. The new terms raised prices for above quota purchases, increasing Belarus' current account deficit. In December 2010, Belarus, Russia and Kazakhstan signed an agreement to form a Common Economic Space and Russia removed all Belarusian oil duties.

The Scope of US-Turkish Business Collaboration in the Broader Black Sea Region

This section focuses on the US-Turkish perspective with respect to improving business co-operation in the Black Sea Region, particularly on similarities in domestic country business set-up and their forward looking prospects on collaboration in the region. The US and Turkish business collaboration in the region should take into account

differences of institutional and market development stages in target economies and promote a more flexible approach based on bilateral interactions.

Degree of Turkish-US Interaction

This section establishes the degree of Turkish–US interaction with a focus on the so-called “third countries” in the region.

Turkey’s importance to the US comes from its geographic location at the junction of the turbulent Middle East, Caucasus, Central Asia, the Balkans and the Black Sea region that include Ukraine and Russia. Recently, crisis dynamics and energy concerns in the globalized world economy drove such geo-strategically inspired relationship towards the economic sphere. In fact, Turkey already has become an important market for US businesses in terms of both trade and foreign investments, but this importance now has grown to such an extent to act as a bridgehead towards the third countries, particularly in the Middle East and the Black Sea Region.

More recently, as observed from a variety of interactions between US-Turkey economic councils, a stronger emphasis to work together to overcome obstacles and to seek out new ways to pursue mutual goals in the ex-Soviet countries and Central Asia. Authorities in the two countries search for mechanisms for expanding shared priorities in third countries by promoting support for small and medium sized exporters. The steps taken to enhance investment climate include regulatory and intellectual property support for innovative industries, energy, biotechnology, pharmaceuticals, and government procurement. These steps are expected to deepen ties between the US and Turkish private sectors.

Given Turkey’s economic growth and development over the last ten years, the United States decided to shift its emphasis from short-term technical assistance projects to longer-term business linkages between the US and Turkish firms. Turkey applies the European Union’s common external customs tariff to third-country imports, including from the United States, non-agricultural imports and imposes no duty on non-agricultural items from European Union and European Free Trade Association (EFTA) countries.

The United States Commerce Department has designated Turkey as one of the ten Big Emerging Markets, forecasting

great potential commercial opportunities. In 1993 the number of American firms operating in Turkey was eighty. In 2011 this number reached 1,000. The US-Turkish Bilateral Investment Treaty went into effect in April 1990. The two countries signed a double-taxation agreement, initialed in 1986. The US-Turkish Bilateral Tax Treaty was ratified by the Council of Ministers of Republic of Turkey in 1997.

In 2009 the United States and Turkey launched the Framework for Strategic Economic and Commercial Cooperation, a new cabinet-level initiative focused on boosting trade and investment ties. The inaugural Framework for Strategic Economic and Commercial Cooperation meeting was held in Washington in October 2010. The Framework aims to reduce barriers to bilateral trade and investment, create opportunities for US workers, farmers, and firms, and otherwise enhance bilateral economic ties. The Framework includes greater involvement of the private sector in both countries in dialogue and deliberations between the two governments. This new engagement on economic matters will give momentum to bilateral commercial transactions and mutual investment flows. The Framework will help the business communities in both countries explore new business partnerships and execute commercial transactions. In addition to the new framework, the US and Turkey hold annual meetings of the Trade and Investment Framework Agreement (TIFA) Council, which met in Washington in July 2010, and the Economic Partnership Commission (EPC), which met in March 2011. The US-Turkish Business Council was established to enable private sector leaders from both markets to provide joint recommendations for improving the commercial relationship.

Two-way trade (exports plus imports) between the US and Turkey was valued at \$14.8 billion during 2010. While US-Turkish trade was sharply impacted by the economic downturn in 2009, US exports to Turkey increased in 2010. Leading US exports to Turkey include aircraft, iron, steel, machinery and fabric, in addition to a wide range of agricultural products. Turkey predominantly exports vehicles, machinery, cement, and tobacco to the United States. Turkey is the 27th largest export market for US goods, with \$10.5 billion in 2010. US exports to Turkey are led by commercial aircraft sales, steel-making products, telecommunications equipment, foodstuff, chemicals and plastics, and cotton. US goods represent only about 7 percent of Turkey’s total global imports. Total US goods

imports from Turkey were \$4.2 billion in 2010 which is led by iron and steel mill products, stone and cement products, apparel and cotton goods, industrial machinery and aircraft parts. The US goods trade surplus with Turkey was \$6.3 billion in 2010. The stock of US foreign direct investment (FDI) in Turkey was \$4.9 billion in 2007, and amounted to \$6.3 billion in 2009, mostly concentrated in the wholesale trade and manufacturing sectors, while Turkish FDI in the United States was \$218 million. US FDI in Turkey is concentrated largely in the banking and manufacturing sectors. Almost all economic sectors open to investment by the Turkish private sector are fully open to foreign participation without screening or prior approval, although establishment in Turkey's financial and petroleum sectors requires permission. Foreign equity ownership is limited to 25 percent in broadcasting and 49 percent in maritime transportation. Turkey's parliament is considering draft legislation easing restrictions on foreign ownership in the media sector.

All areas that are open to the Turkish private sector are now open to US participation and investment. Turkey grants US businesses the same rights, incentives, exemptions and privileges that Turkish businesses receive. US firms can participate in government-financed and/or subsidized research and development programs. Investment incentives include subsidized credit facilities and exemptions on corporate and value-added tax, customs fees, and duties. Such openness makes Turkish-US ventures more attractive to act together in third countries.

Existing US-Turkish Collaboration and the Way Forward

In fact, American and Turkish companies are already engaged in major energy projects. ExxonMobil and Turkish Petroleum are exploring deep-water areas in the Black Sea for gas and oil, as are Chevron and Turkish Petroleum. Chevron, Conoco Phillips and Hess were partners in and own a share of the Baku-Tbilisi-Ceyhan oil pipeline. Edison Mission and Doğa Enerji are partners in the Doğa Power Plant that supplies electricity to Istanbul. AES and Koç Holdings formed AES-Entek which will be one of the largest independent power producers in Turkey. And, perhaps as an example of opportunities for the future, General Electric and GAMA Enerji have partnered on a 400-megawatt power plant in Galway, Ireland.

In order to create and improve opportunities for Turkish-US partnership in energy, both governments are working on financing projects for renewable energy instruments as well as traditional energy exports such as gas turbines through the United States Export-Import Bank and the Overseas Private Investment Corporation. The US Trade and Development Agency is supporting feasibility studies for waste-to-energy and geothermal projects in Turkey, as well as electricity transmission smart grid systems. The US Department of Energy is collaborating with the Ministry of Energy and Natural Resources, and other Turkish government agencies on the "Near Zero Zone," a pilot industrial energy efficiency project in Izmir. The US Department of Commerce has brought a business development mission of top US companies in the oil and gas service sector, as well as renewable energy and energy efficiency, to Turkey in 2011. US and Turkish companies have already built strong relationships. However, this is far from sufficient to grow into true innovative partnerships involving third countries. What is needed is the expansion of research and investment in new technologies by building innovative partnerships that can enhance prosperity and growth for both countries.

Diversifying Trade and Improving Business

Turkey is an important strategic partner of the United States on areas such as security, regional peace and stability, and counter-terrorism. Despite strong political and military ties, trade relations between the two countries have not yet reached their full potential. The level of bilateral trade is inadequate, as 25 percent of US imports in Turkey are military goods. The establishment of market-driven democracies in the Black Sea Region can only survive with comparable economic transformation. The opportunities for US-Turkish co-operation in the Black Sea Region can be enhanced if based on a strategically designed model that helps strong reforms to integrate the region to the global economic order. Design of such model towards the region needs new ideas to improve the balance in trade and investment between Turkish and American businesses. The growth of such co-operation however cannot be possible without the United States' realizing and recognizing Turkey's capacity. The business community in both countries ought to bridge the divide of modus operandi in both countries. Entrepreneurs should find incentives to promote collaboration. The Black Sea Region has huge potential. However, job creation in the countries of the

region is unlikely to be endogenous, but instead will need foreign and external input, providing the opportunity for Turkish-US business collaboration. By combining the strengths of both Turkish and US businesses, the high level of risk can be reduced since Turkey has experience in the Turkic countries of the former -Soviet Union while US firms provide credibility.

Turkish-US trade relations should be diversified. This follows the implications of recent regional changes and new opportunities and challenges in working with third countries. Aligning both Turkish and US business practices would bring about substantial opportunities between Turkish and US business as this might enhance co-operation and collaboration. However, certain problem areas should be improved for better business environment and economics co-operation. For instance, in addition to energy sector where innovative partnerships can happen, US-based pharmaceutical companies could also invest in Turkey which would bring into Turkey an international investment of about \$1 billion. This would create spillovers to the third countries in the region.

However, the Turkish regulatory framework deters such investment. US businesses often view the Turkish regulatory environment as inconsistent and non-transparent. Although the Office of the United States Trade Representative recognized the improvement of Turkey's Intellectual Property Rights regime (IPR), Turkey is also on the US piracy watch list. US firms want Turkey to do more to safeguard intellectual property rights, though Turkey has made improvements in their enforcement, including an increased number of raids, arrests, prosecutions, and issuance of deterrent sentences for IPR infringers. A recent OECD report stated that Turkey's overall corporate governance outlook is positive because authorities have already adopted, or are introducing, high quality corporate governance standards (including audit standards) and because transparency has improved significantly.

Legal Arbitration Reform

Globalization had a significant impact on the legal sphere as much as on all other sectors. International investors and investments resulted in mechanisms that provide for rapid settlement of many disputes independently of national adjudication, especially in the energy sector. It is crucially important that possible disputes are minimized. Indeed, some protection mechanisms, from which companies

registered in Turkey and investing abroad may benefit, are applicable to foreign companies investing in Turkey.

At this stage, Turkey set a strategy by establishing necessary legal regulations and properly using administrative mechanisms on the path of European Union accession by generating several rapid, transparent, and new legal resolution alternatives to governmental arbitration. Energy companies frequently prefer arbitration for settling their disputes as multinational companies invest in this sector by taking certain risks and mostly face reliability challenges with regards to the legal system of the country where investments take place.

The arbitration method has found its field of practice in the Turkish legal system as a result of some essential legal and constitutional changes in the past decade in Turkey. The legal base of arbitration is established for ensuring that some public services to be given by foreigners through special legal contracts in Turkey. There are still long-unresolved cases of legal actions brought against the Government of Republic of Turkey before the ICSID (International Center for the Settlement of investment Disputes).

Involving Third Countries: Investing in Agriculture and Manufacturing

Hence, some of the problematic issues between Turkey-US economic partnerships are related to trade, investment, and entrepreneurship. Third country and sectoral cooperation can be dealt with by enhancing business-to-business ties while promoting cooperation in agricultural sector and developing policies that encourage bilateral trade in agricultural goods.

There are mutual impediments to improving agricultural trade. This is important for both sides, as many US agricultural exports to Turkey are inputs for Turkish industrial exports. The machine manufacturing industry also holds strategic significance for development by defining the productive skills of other sectors through investment, intermediate goods and the services it offers. A developed machine manufacturing industry provides a critical competitive edge over other countries in the manufacturing industry.

The machinery industry sector in Turkey has been growing at a rate of nearly 20 percent per year since 1990. This growth is backed by highly competitive and adaptable small and medium-sized businesses (SMEs), which form

the bulk of the industrial production in the country. As the drivers of growth in machinery and major contributors to the industrialization of the country, Turkish SMEs distinguish themselves from their peers in other countries by their utilization of the low-cost and highly skilled work force Turkey offers.

Another indicator of the advanced level of Turkish machinery industry is the rate of domestic input in the production stage. Around 85 percent of domestic input not only reduces the dependency on foreign sources, but also helps other local industries. The combined advantage of the engineering capability required to compete in the international market with reasonable labor costs enable the Turkish machinery industry to offer a range of products and components that are both high-quality and affordable.

The machinery industry in Turkey is labor intensive rather than capital intensive, and is expected to remain so in the near future. In this regard, the industry's advantage lies in the accumulation of companies with different capabilities, strategies, and products, so that this clustering provides a technological edge to the overall industry. The harmonization of EU legislation in accordance with Turkey's accession process has made it compulsory to obtain the necessary safety and compatibility certifications. As of July 2010, four Turkish national institutions have been authorized as notified bodies to ensure the compliance of local machinery producers with EU standards. Turkey's machinery industry has been given ambitious export targets for the country's 100th anniversary in 2023 to reach \$100 billion with a share of 2.3 percent of the global market. This is one area where US and Turkish companies can cooperate with some spillover effects to the third countries.

Developing an International Financial Center and Logistics: Istanbul

One of the areas which would enhance Turkey's role as a bridgehead to the US firms in the Black Sea Region comes from the creation of an international financial center (IFC) in Istanbul. This would require progress on the IFC action plan, determination of specific areas of cooperation, including exchanges of regulatory and policy experts, and potential cooperation on measures to make Turkey more attractive for foreign investment in the financial sector. There are also opportunities for cooperation in the energy

sector, including efficiency and renewables and nuclear policy.

In both countries the vital role in promoting cooperation in energy and innovative industries the private sector needs to be involved through global entrepreneurship programs. Cooperation on entrepreneurship includes supporting similar programs for the third countries, particularly those in the Black Sea Region, North Africa and sub-Saharan Africa. Facilitating cooperation between the two governments and private sectors requires leveraging new business opportunities in the third markets. In addition, the promotion of such ventures in the third countries can be facilitated by creating logistics centers in Turkey to manufacture and increase both Turkish and US exports to third countries.

Similarities between US and Turkish Outflow FDI

Turkey's remarkable 10 percent economic growth percent is actually accompanied by a process of deeper transformation of the economy, which can be best captured in view of Turkey's fledgling Outward Foreign Direct Investment (OFDI). It is now solidly established that Turkey has joined the ranks of capital exporting developing countries, alongside Brazil, Russia, India, China, and others. This follows the rise in Turkey's productive capacity, foreign trade performance and increased domestic demand. Studying similarities between Turkish OFDI and US business interests can provide ground for furthering cooperation particularly towards the third countries in the Black Sea Region.

The opening up of the Turkish economy in 1980 and the deregulation, trade liberalization, and privatization that followed, led to a slow growth in inward FDI. This was strengthened by the signing of a Customs Union treaty with the European Union² that came into force in 1996. Inward FDI helped outward FDI growth in several ways—for example, by making Turkish firms more competitive through knowledge spillovers and by giving them an incentive to explore foreign markets by increasing competition in the domestic market. On the one hand, Turkish firms wanted to access technology and skills in the European Union while on the other hand, they desired to gain access to low-cost labor in Africa and Asia. They have also sought natural resources in the newly independent Turkic countries

²The customs union agreement was restricted to industrial and processed agricultural products.

of Central Asia and responded to growing demand in the emerging markets of Asia and Africa.

After years of low FDI levels, Turkey succeeded in attracting \$18.3 billion in net FDI in 2008. Global market conditions reduced foreign capital inflows in 2009, and Turkey attracted \$7.7 billion in net FDI in 2009. This amount was expected to fall to around \$5 billion in 2010. A series of large privatizations, the stability fostered by the start of Turkey's European Union accession negotiations, strong and stable growth, and structural changes in the banking, retail, and telecommunications sectors contributed to the 2008 rise in foreign investment. Turkey has taken steps to improve its investment climate through administrative streamlining, an end to foreign investment screening, and strengthened intellectual property legislation. However, a number of disputes involving foreign investors in Turkey and certain policies, such as high taxation and continuing gaps in the intellectual property regime, inhibit investment.

Conclusion

Several industry clusters can be identified as the emerging sectors: information technology, environmental technology, transportation, energy technology, health care technology, and financial services. Opportunities for US companies together with their Turkish counterparts in these sectors are significant and expanding rapidly. The lucrative business sectors also include electrical power systems, telecommunications (equipment and services), industrial chemicals, pollution control equipment, computers, medical equipment, and major infrastructure projects.

The possibilities of collaboration between Turkish and US companies that would also help development of business environment in the Black Sea Region are great. Stemming from the very nature of their developmental stages and the way in which they have integrated into the global economy, improving business practices with the countries in the region ought to differ. Developing business interactions with Greece, Bulgaria and Romania would require alignment of business practices along the European Union lines while business interaction with Armenia, Azerbaijan and Georgia would follow political priorities. In the latter case, bilateral deals with each one of the countries in that cluster would yield more beneficial business interactions. Russia, Belarus and Kazakhstan would be much more difficult

markets to penetrate because of the size, scope and depth of their economies. In this case, adopting a more flexible business approach might be required. Ukraine, due its IMF straightjacket and its history of liberalization, might be a different case. The areas of business opportunities for Turkish–US companies in Ukraine are diverse, but banking, pension and insurance are likely sectors to be considered for investments.

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