Policies for Business in the Mediterranean Countries

Republic of Turkey

Ivan Raffaele Silvio Pacifico

C.A.I.MED.
Centre for Administrative Innovation in the Euro-Mediterranean Region
c/o Formez - Centro Formazione Studi
Viale Campi Flegrei, 34
80072 Arco Felice (NA)
Italy
Tel +39 081 525 0211
Fax +39 081 525 0312
e-mail gpennella@formez.it
nvolpe@formez.it

Economics reforms

Introduction to the Turkish economy

In order to analyze economic incentives in Turkey and to understand the Turkish market, it is important to study the problems connected to the economic field in Turkey and the economic problems of recent years. We cannot gain an understanding of the Turkish Market or the Turkish economic future if we do not understand Turkey's economic trends and social indicators. The table below (Table. 1), shows the main social indicators that allow a complete analysis.

SOCIAL INDICATORS OF TURKEY

	1999	2000	2001	2002	2003
AREA (Km2)	774.815	774.815	774.815	774.815	774.815
POPULATION (1000 persons) (Mid-Year Population)	64.345	67.461	68.618	69.626	70.712
ANNUAL POPULATION GROWTH RATE (In thousand)	17,5	17,1	16,7	15,7	15,3
POPULATION DENSITY	83,0	87,1	88,6	89,9	91,3
ENROLLMENT RATE (%)	1998/1999	1999/2000	2000/2001	2001/2002	2002/2003
Primary education	83,6	90,5	90,7	89,8	...
Secondary education	38,2	39,1	40,4	43,2	...
University and other higher education	11,0	11,6	11,5	11,8	...
	1999	2000	2001	2002	2003
INFANT MORTALITY (İn thousand)	36,3	34,8	38,7	39,4	38,3
AVERAGE LIFE EXPECTANCY (Year)	68,3	68,5	68,6	68,5	68,7
Female	70,7	70,9	71,0	70,9	71,0
Male	66,1	66,2	66,4	66,2	66,4
POPULATION PER DOCTOR	820	834	776	744	...
LENGTH OF ROAD (Km)	60.923	61.090	61.305	62.369	...
LENGTH OF MOTORWAYS (KM)	1.749	1.773	1.851	1.851	...
RAILWAYS (Km)	8.682	8.671	8.671	8.671	...
AUTOMOBILE (Per 1000 persons)	63,3	65,2	66,1	66,1	...
TELEPHONE (Per 1000 persons)	281	271	276	272	...
TELEVISION SETS (Per 1000 persons)	419	439	459	474	...
ANNUAL CONSUMPTION OF ELECTRICITY (Per capita/Kwh)	1.417	1.505	1.415	1.479	...

(*) Covering October 1-June 15
(**) 2000-2001 / 2001-2002 education years were calculated by using the final result of General Census of Population in 2000. The eight-year compulsory education was initiated as from 1997/1998 with the law no: 4306 dated 18.8.1997.

Table 1. Social Indicators

Turkey experienced a positive trend in the annual rate of growth from 1996 to 1998 with on average 6.4%, however in 1999, the growth rate contracted by 6.1% due to policies aimed at reducing inflation and declining production because of the earthquake which took place in August of the same year. As a result of the three-year disinflation and structural adjustment program started at the end of 1999, and supported by a stand-by agreement with the International Monetary Fund (IMF), inflation fell significantly in 2000 (from 84.9% in 1996 to 32.7 % in 2000).

In the meantime, interest rates abruptly dropped below expected levels, production and domestic demand started to increase, GDP by expenditure grew by 7.1 % and as a result an annual growth rate of 6.1 % was achieved.

The financial crisis of the last months of 2000 became an economic crisis in February 2001, so a new programme for restructuring the economy and achieving stability had to be designed in April 2001. Although with the new program annual growth rates of -3.0% and 5.0% were predicted for the years 2001 and 2002 respectively, they were reduced to -8.5% and 4.0% following the September 11 events. The inflation rates for 2001 and 2002 were targeted as 65% and 35% respectively. In 2001, annual growth rate and year-end inflation were -7.4% and 68.5% respectively. The economic programme has been implemented successfully with the prospect of targets for 2002 being met by the end of the year. Growths in GDP and GNP were 8.2% and 8.8% in the second quarter of 2002. For the first six months of 2002 taken together, GDP rose by 5.2% and GNP by 4.7% year on year, and at the end of the year GNP had grown by 5.9%. Increases in exports and stocks have been the main components of growth in 2002. The year-end rate was 30 %, below the Government's target of 35 % for 2002.

We can see below how the financial and economic crisis started in the last months of 2000 affecting the sectors, agriculture, industry[1] and services in 2001. Only in 2002 the Turkish Gross national product start again to grew with a rate of 7.9%.

ECONOMIC INDICATORS OF TURKEY

	1999	2000	2001	2002	2003 (1)	2004 (1)
GROSS NATIONAL PRODUCT (GNP) (2)						
At current prices (TL Billion)	78.282.967	125.596.129	176.483.953	275.032.359	356.680.888	
At current prices ($ Million)	185.267	200.002	145.693	180.892	239.235	
At 1987 prices (TL Billion)	112.044	119.144	107.783	116.338	123.165	
GNP Per capita (TL Thousand)	1.216.609	1.861.759	2.571.978	3.950.139	5.044.135	
GNP Per capita ($)	2.879	2.965	2.123	2.598	3.383	
Deflator	55,8	50,9	57,8	44,4	22,5	
Gross domestic product per capita - At current prices and						
current purchasing power parity ($)	6.135	6.730	6.046	6.448	6.718	
GNP - RATE OF GROWTH BY SECTORS (%)						
Agriculture	-5,6	3,8	-6,0	7,4	-2,4	
Industry	-5,1	5,6	-7,4	7,9	7,3	
Services	-3,9	6,5	-6,1	6,0	5,1	
GNP	-6,1	6,3	-9,5	7,9	5,9	
GDP COMPOSITION BY SECTORS (%)						
Agriculture	16,0	15,4	12,8	13,0	13,4	
Industry	19,0	20,0	21,1	19,7	18,5	
Services	64,9	64,6	66,1	67,3	68,2	
FIXED INVESTMENTS (TL Billion) (Programme, 2004)	16.863.755	27.688.468	32.408.981	46.031.221	61.179.859	76.737.211
Public (TL Billion)	4.435.215	7.983.004	10.047.332	15.880.805	14.969.350	17.914.349
Private (TL Billion)	12.428.540	19.705.464	22.361.649	30.150.416	46.210.509	58.822.862
EMPLOYMENT (2000-2003 Q4)						
Civilian labour force (1000 persons)	22.925	22.031	22.269	24.347	23.206	
Civilian employment (1000 persons)	21.236	20.579	20.367	21.658	20.811	
Agriculture	8.595	7.103	7.217	7.618	6.799	
Industry	3.664	3.738	3.734	3.953	3.836	
Services	8.976	9.738	9.416	10.086	10.176	
Unemployment rate (%)	7,4	6,6	8,5	11,0	10,3	
Number of workers abroad **(January-September, 2003) (Februa**	1.206.067	1.170.226	1.178.412	1.200.725	1.197.968	1.197.964

(1) Provisional

(2) The new series in producers' price

Table 2

[1] For further details, see Industry Employers' Union. (http://www.ieis.org/eng/yayin/index2.htm), Istanbul, 2004 (accessed June 2004);

In August 2002, the High Planning Council, approved the economic programme of Turkey for 2002-2005, and in the year 2003 economic performance was even better.

The program covers economic targets for meeting the EU accession criteria. An average growth rate of 5.2 % and an inflation rate of 8 % are targeted by the programme. It aims to reach a sustainable growth rate and the EU average in the ratio of public debt stock to GNP, and to strengthen the free market economy. It is expectd that an increase in the growth rate will be mainly achieved by increasing investments and exports. Expected increase in investments and exports are calculated at 14.2% and 6.6% respectively. Due to the recent macroeconomic program, Turkey has gone through a large number of structural reforms. The aim of these reforms is defined as increasing the efficiency of growth and production factors in the country in order to meet the requirements of both globalization and growth based on human capital and technology. Legislative measures taken in that respect are categorized as: a) financial sector restructuring; b) increasing transparency in the State and strengthening of public finances; c) enhancing of competition and efficiency in the economy; d) strengthening of social solidarity.

Actions taken to adopt the EU *acquis*, are to a large extent contributary to these efforts.

1 Foreign investments and development of Free Zones [2]

1.1 Foreign Investments

There are two ways to develop the country in this moment. The first one is linked to the capability of gaining the interest of the foreign investors in Turkey and the second is to enforce industry and services in the country through investments and incentives. [3]

The foreign direct investment (FDI) has a number of benefits for Turkey: it creates opportunities for employment and income growth, transfers technology and management skills to Turkey, helps to address poverty and underdevelopment in Turkey's inland regions, and furthers the integration of Turkey into the global community. Turkey's large internal market, skilled and cost-effective labour force, strategic location, customs union with the EU, and regional trading relationships seemingly position it to attract significant FDI. Yet during the 1990's, FDI inflows averaged less than 0.5% of GDP in Turkey, while such regional competitors for FDI as Hungary and Poland averaged inflows of 4% and over 2%, respectively. Turkey's historically poor

[2] For further details, http://www.dtm.gov.tr/English/doing/iginvest/invest.htm; (Accessed April 2004).

[3] For further information see, Report of the Subcommittee on Turkey, presented to "The Advisory Committee on International Economic Policy" (ACIEP), November, 2003.

performance in attracting FDI was because there was a sense of policy and economic instability, which had various consequences, including chronic inflation. In the face of these impediments to foreign direct investment, it is important to specify that Turkey's climate for FDI is determined not only by its formal policy, as embodied in its constitution, legislation, and public statements, but also by its practice in putting policy into effect, and the perception of policy and practice by the investing community. In order for Turkey to attract a level of FDI commensurate with its size, population, and advantageous trading relationships, Turkey must have appropriate policies in place, but just as importantly, those policies must be clearly manifested in bureaucratic and judicial practice, and investors must perceive that Turkey is firmly committed to the continuation of those policies. There are three main channels through which Turkey will enforce the foreign direct investments: 1) policy; 2) practice; 3) perception.[4]

1.2 Policy

In last years Turkey has recognized the importance of FDI and has made several reforms to guarantee a favourable climate to new investment. The government has recently supported the creation of a General Directorate on Foreign Investment within the Department of the Treasury, and has approved of the new law on Foreign Direct Investment. The law was passed only a year so it is difficult to judge the results or the effects of this law, but it is possible to make some considerations about it.

1.2.1. New Law on Foreign Direct Investment

The Foreign Direct Investment Act (Law No. 4875) took effect on June 5, 2003. It replaces legislation that governed foreign direct investment practices in Turkey since 1954 and takes significant steps forward in harmonizing Turkey's legal framework for FDI with international standards.

The new FDI law and other reforms resulted at least in part from a study by the Foreign Investment Advisory Service of the World Bank (FIAS) begun in 2001 at the invitation of the Turkish Government. One of the key recommendations of the FIAS was for an improved legal framework for FDI, and the resulting legislation has been characterized by FIAS as "close to best practice." The law, and revisions to the Turkish Commercial Code passed separately, make the following provisions: 1) Remove legal restrictions on foreign direct investment; 2) Guarantee national treatment and equal rights and obligations for foreign and domestic investors; 3) Simplify the steps and procedures required to facilitate foreign investments; 4) Permit the transfer of profits, dividends, fees and royalties without any restrictions; 5) Prohibit

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[4] For further information, see Levent Bosut, *Private equity and venture capital in Turkey*, PDF Corporate Finance, Istanbul, 2004.

expropriation and nationalization of foreign investments without prompt, adequate and effective compensation; 6)Eliminate any kind of restrictions on the sector in which investments can be made.

Real improvement in the climate for FDI will occur only if reforms called for by the new law are put into practice by the Turkish government in an effective manner, and the international investor community perceives that there has been a significant change in the investment environment that represents commitment to a stable policy favouring FDI. To ensure these results it will be important to strengthen collaboration between public and private sector in developing strategies and planning objectives to obtain more foreign direct investments in Turkey. For this reason was the Coordination Council for the Improvement of the Investment Environment (CCIIE) was created, with a memberhship that includes representatives of the Turkish private sector and the foreign investment community. All the actors (i.e. stakeholders, *foreign investment community, etc)* must be considered in a transparent process.

1.3 Practice

It is important to encourage the new policies favourable to FDI, like national treatment, transparency, and freedom of economic action. These include the areas of dispute resolution, regulatory approvals and tax policy.

Starting from dispute resolution, the new law regulate disputes regarding investment agreements subject to private law, disputes arising from exclusive public service provisions and concession agreements made between foreign investors and the Turkish state. The new FDI law states that investors may apply to national or international arbitration, as well as to local courts, for dispute resolution, provided that the conditions in the related regulations are fulfilled and the parties agree thereon. At the same time nothing is said about commercial disputes between local companies and foreign investors.

It is very important to compare figures with other states: according to 2003 World Bank data, in order to resolve a dispute in Turkey, 18 procedures (requiring interaction between the litigants and/or the officers of the court) are required, 105 days elapse before the dispute is resolved, and the cost of disputes resolution is 5.4% of Gross National Income per capita. These figures compare favourably to Hungary (17 procedures, 365 days, 5.4% GNI per capita) and the U.S. (17 procedures, 163 days, .4% GNI per capita). But if the numbers are so good it is also important to understand that there is really a problem of image, because the foreign investors don't believe that the government can assure that local courts will provide swift and impartial justice in line with the need to attractive foreign investors.

Another important point of the reforms concern the approvals needed to start a business in Turkey. Also in this case, according to 2002 World Bank data, 13 procedures were required to begin a business in Turkey, taking 53 days and costing US $1,222. In this area, Turkey compared well in terms of time and cost with Hungary, generally viewed as one of the most successful East European economies in attracting investment (65 days and US $3,048), but poorly in terms of number of procedures (Hungary required only 5). Also in this case there is a problem of image because Turkey is less expensive and is faster than Hungary in giving possibilities to create a new business and, at the same time, it has more procedures. More procedures in less time!!!!

In trying to simplify the procedures, the new law has changed some rules: 1) It is not necessary to obtain permission or authorization from administrative authorities in order to invest; 2) Foreign investors are free to make direct investments in Turkey and are subject to equal treatment with Turkish investors; 3) Restrictions on changing the shareholder percentages of foreign investors have been eliminated; 4) Amendments made separately from the Turkish Commercial Code reduce the number of steps required for forming companies in Turkey.

More transparency is needed; a World bank study shows that 62% of foreign-invested enterprises must pay an illicit fees to obtain the licences and permits. The need to make such payments is considered an obstacle to development of foreign investments in Turkey. The recommendation of the World Bank is to create an Ombudsman at high level to monitor the functioning of the regulatory approval process as it applies to foreign-invested-enterprises in regard to speed, efficiency, fairness and transparency .

1.4 With which measures can Turkey demonstrate its policy stability?

As has been indicated above, the conditions to develop foreign investments in Turkey do exist but there isn't enough confidence in the Turkish market. Considering the need for long term investments by the foreign investors, Turkey must give the sense of during stability in which democratic reforms, economic reforms can build a new state in the next 15/20 years. In the past, lack of policy stability in Turkey has often been cited as an important impediment to FDI.

The Under-Secretariat is a new agency for realizing the reforms heralded by the new Turkish laws and regulations on FDI. This new agency has the objectives of: ensuring that each economic reform or change in Turkish law is compatible with foreign investment targets; evaluating the effects of the reforms or changes on the FDI climate and suggesting the acceptable alternative policies that are more favourable to the attraction of FDI. If the Under-Secretariat works effectively, the faith of investors will grew quickly because it will signify that Turkey has chosen an enduring policy to in support of foreign investment.

In the next few years Turkey has to demonstrate its will to enter the European union through more reforms. Until Turkey becomes a formal member of the European Union, it will be important to demonstrate in each international agreement, the will to develop an environment supportive of the growth of the FDI. Maybe in the next few years we will see reforms that will transform their FDI commitments towards WTO obligations. The World Bank suggest, for example, that even if the GATS only covers services, it provides an opportunity to assure investors that national treatment will be given to foreign-invested entities with a commercial presence in a variety of areas, such as distribution services and product servicing, that are relevant to a wide range of investments. It will be better if Turkey sends a strong signal by taking an aggressive leadership role in calling for strong measures to protect investors' rights in appropriate international, regional, and bilateral agreements. The international investors must have confidence in Turkey not only in coming months but in the coming years. The Turkish Government has taken steps to promote foreign direct investment in Turkey, including the establishment of the General Directorate on Foreign Investment within the Secretariat of the Treasury.

1.5 Foreign investment in Turkey

The Turkish Government strongly believes in foreign investment and therefore grants the same rights and obligations as for local capital, while guaranteeing the transfer of profits, fees and royalties and the repatriation of capital. While the cumulative foreign capital approvals between 1954-1980 was 280 million US $, this amount reached 23.8 billion US $ at the end of 1998. The leading investors in Turkey are France, USA, Netherlands, Germany, Switzerland, United Kingdom, Italy and Japan.

In this moment, in accordance with the indications of the Word bank, the General Directorate of Foreign Investments (GDFI) is authorized to offer several services to foreign enterprises in Turkey.

What are the main important points of foreign investment policies in Turkey? First of all we must remember that real persons and legal entities residing abroad may engage in all types of industrial, commercial, agricultural and other fields aimed at the production of goods and services, which are also open to the Turkish private sector. These new activities can be developed in Turkey through the use of several forms of capital (Cash - Machinery, equipment, etc.- Assets – Intellectual property). If it is requested, the foreign capital transferred from abroad can be kept in banks in foreign exchange deposit accounts without being converted into Turkish Lira, to be opened in the name of the company to be established or the shareholders who transfers his/her shares, or the company which increases its capital, and can be paid to the beneficiary as foreign partner's capital share. At the same time there are no limitations to participation ratios of local and foreign partners: a company can be 100% foreign owned. There is substantial freedom in portfolio participation: all the legal entities residing abroad including investment trusts and investment funds, who want to purchase and sell securities and other capital market instruments through banks and intermediary institutions authorised by the Capital Market Legislation in Turkey can do it without any need for further permission from the GDFI. But at the same time, if there is a person living abroad who owns 10% or more equity of a company established in Turkey, and he wishes to participate in a directors or shareholders meeting of that company, the GDFI must be informed of the participation. It is important to make clear that public and private sector enterprises shall liaise with the GDFI for matters regarding: the registration of licenses, know-how, technical assistance, management and franchising agreements to be made with persons and legal entities residing abroad. If there is an agreement that it is not approved by the GDFI, that agreement cannot become effective.

There are no limits to the transfer of earnings abroad. After the deduction of taxes in accordance with current tax laws, from the profits and dividends deriving from the shares of foreign shareholders of foreign capital entities, the net amount can be transferred abroad. In order to create a good climate for foreign direct investment, Turkey has signed more than 50 Protection and Promotion of Investment Agreements and 34 of them have entered into force. Avoidance of double taxation Agreements has been made a legal provision with 39 countries.

Turkey has been party to OECD Codes of Capital Movements and Invisible Transactions, to the convention on ICSID (International Center for Settlement of Disputes) and to investment-related agreements on WTO platform like TRIMs (Trade Related Investment Measures) and TRIPs (Trade Related Intellectual Property Rights). To promote investment in Turkey the current legislation concerning investment incentives is shaped by the decree published on 25 March 1998, and its related communique published on 6 May, 1998. According to this legislation, the incentive tools granted to investors are: 1)**Exemption from customs duties and fund levies.** The imported machinery and equipment for the investment can be brought to the country with the exemption of customs duties and fund levies. 2)**Investment allowance.** All expenditure relating to buildings, machinery, equipment, freight and installation are entitled to benefit from the investment allowance. The current allowance rate is 100%. Therefore an amount equal to the fixed investment cost can be deducted from the future taxable profits. 3) **VAT (Value Added Tax) exemption for imported and locally purchased machinery and equipment**. Value added tax, paid on imported and locally purchased machinery and equipment, can be exempted by this incentive measure. 4) **Exemption from taxes, duties and fees.** Investors who commit to realize 10,000 USD of exports upon the completion of the investment are granted exemption from the taxes, duties and fees related to: a)establishing a company; b)increasing capital within the investment period; c) receiving investment credits whose terms are at least one year ; d) Registration of land and properties as capital-in-kind.

In Turkey there is also the general incentive regime which is applied depending on the location, scale and subject of investments. In terms of application of general incentives, Turkey is divided into three types of regions:

1. Developed Regions: The city boundaries Istanbul and Kocaeli; and the municipality boundaries of Ankara, Izmir, Bursa, Adana and Antalya);
2. First priority regions: 50 cities determined by the Council of Ministers
3. Normal Regions: The remaining cities

The above incentive measures are applicable for all types of investments in the normal and first priority regions, but only the following investments can qualified for incentives in the developed regions: 1) electricity production (including auto-producers); 2) infrastructure investments; 3) investments under the BOT and/or BOO scheme; 4) investments related to R&D, design and producing new products or models; 5) investments for environmental protection; 6) priority technology investments determined by the Higher Council of Science and Technology; 7) electronic sector investments; etc.

2. Free Zones

The Free Zones are defined as special sites within the country but deemed to be outside of the customs territory. They are regions where the current regulations related to foreign trade and other financial and economic areas are not applicable, are partly applicable or are where new regulations are tested in.[5] At the same time the free zones are also regions in which exists the most convenient business climate to increase trade volume and export for some industrial and commercial activities.[6]

Recently, with Law No. 5084 on the Encouragement of Investments and Employment and Amendment of Certain Acts, published in the Official Gazette dated 06.02.2004, No. 25365, and coming into effect on the same date, there have been some new directives regarding tax incentives in the Free Zones Law No. 3218, dated 15.06.1985.

Now there are more than twenty zones in the entire country in which it is possible to develop all kind of activities such as manufacturing, storing, etc.

According to new provisions called for by the law n. 5084, mentioned above:

1. The real or legal persons who obtained the operating licences before the Law No. 5084 (6.2.2004) came into effect: a) shall continue to benefit from the exemptions of income or corporate taxes within the limits of the period specified in their operating licences, b) shall not pay income tax on the wages they pay to their workers until 2009; c) shall be

[5] For further information http://www.dtm.gov.tr/sb/english/freezone1.htm (Accessed April 2004).

[6] For further details, http://lnweb18.worldbank.org (Accessed march 2004).

exempted from all taxes, levies and duties generated from activities related to their free zone operations until 2009.

2. Only earnings generated from the sales of the goods produced in the zones by the real or legal persons who obtained a production licence on 6.2.2004 or after, are exempted from income or corporate taxes until the end of the taxation period of the year Turkey becomes full member of the European Union. At the same time it is important to remember that the law specifies the limits of the operations in Turkish free zones.

In the light of this, it can be said that that operating in free zones can be more advantageous for firms that: 1) require minimum bureaucracy; 2) sell the goods abroad produced with imported inputs; 3) engage in labour intensive sectors; 4) engage in transit trade, re-export and barter activities; 5) prefer to use foreign currency in all transactions (wholesalers, banks, insurance companies, manufacturers) 6)demand modern office and working spaces with good and ready infrastructure.

It is important to understand that growth in the free zones in recent years is near 40% per year (table 3). But maybe in 2004 we will see a growth approaching 70%, the same growth that the Turkey had before the financial crisis of 2000.

ANNUAL TRADE VOLUME OF FREE ZONES (US$ 1000)

ZONES	2000	% 00/99	2001	% 01/00	2003	% 03/02	2003-III	2004-III	% 04/03
İST-DERİ	4.059.383	63,3	2.324.919	-42,7	4.076.782	44,2	704.939	1.208.224	71,4
MERSİN	1.767.854	17,5	1.337.790	-24,3	2.766.312	68,4	499.073	779.551	56,2
İST-AHL	2.893.199	31,7	2.193.739	-24,2	3.022.789	22,1	614.722	750.012	22,0
EGE	1.662.598	39,8	1.291.910	-22,3	2.642.599	44,5	544.733	719.651	32,1
BURSA			82.294		1.108.768	147,4	135.303	488.933	261,4
İST. TRAKYA	181.535	149,4	237.939	31,1	1.145.646	73,8	204.701	342.129	67,1
AVRUPA	105.655	723,2	212.865	101,5	570.498	66,3	102.247	200.206	95,8
ANTALYA	215.132	22,1	185.019	-14,0	359.183	46,0	52.922	83.414	57,6
MENEMEN	240.262	33,0	251.479	4,7	301.562	8,7	76.521	83.048	8,5
KAYSERİ	22.554	3.336,3	27.071	20,0	157.184	87,9	28.670	41.430	44,5
GAZİANTEP	35.671	126,5	54.355	52,4	207.261	89,1	17.852	35.109	96,7
SAMSUN	16.845	284,2	12.329	-26,8	17.244	44,8	7.202	32.289	348,3
DENİZLİ					41.030	1.058,0	5.636	21.152	275,3
ADANA-YUMURTALIK	60.864	2.664,5	59.267	-2,6	74.852	59,8	14.621	18.838	28,8
KOCAELİ					29.180	215,5	3.323	16.635	400,6
RİZE	15.816	31,9	16.447	4,0	10.986	-3,2	1.334	7.831	487,1
MARDİN	5.522	4,8	5.284	-4,3	19.597	-17,1	3.486	5.597	60,6
TRABZON	15.914	-40,3	36.661	130,4	46.956	-3,2	11.769	4.034	-65,7
TUBİTAK-MAM TECH.					9.555	85,2	1.028	1.725	67,8
D. ANADOLU	1.789	191,5	1.881	5,1	83	-53,0	83	-	
İMBK(*)	-		-		-		-	-	
TOTAL	11.300.593	43,3	8.331.246	-26,3	16.608.066	49,6	3.030.165	4.839.805	59,7

Table 3

2.1 Necessary steps for operation in the free zones.

To engage in operations in the free zones it is necessary to obtain an operating licence from the Under-Secretariat for Foreign Trade, Directorate General of Free Zones. An application form for the Operating Licence can be obtained from Directorate General of Free Zones, Zone Directorates or Zone Operator, Founder/Operator Companies and has to be completed. At the same time all the documents indicated below must be attached to the form:

1. Descriptive information about the applicant and its free zone operation;
2. Authorization document and specimen signature of the signatory and power of attorney and specimen signature of the representative of the firm (if any);
3. Turkish Trade Registration Gazette announcing the establishment of the Applicant Firm, showing its current capital

composition. For foreign firms Trade Registration Document ratified by the related Turkish Consulate;
4. Last three years' balance sheets and income statements;
5. The original receipt of application fee deposited in the Central Bank of Turkey, and its copy;
6. Documents related to the foreign currency brought into Turkey in the last three years, (If any);

All the documents signed until now have to be sent to the Under-Secretariat for Foreign Trade, Directorate General of Free Zones through Zone Operator or Founder/Operator Firms.

The Directorate General of Free Zones was founded in 1983 within the organization of the Prime Minister's office, on the basis of Statutory Decree Nr. 151. Later in 1984 it was merged into the State Planning Organization as the Directorate of Free Zones on the basis of Statutory Decree Nr. 223 and in 1991 it became part of the Under-Secretariat of Treasury and Foreign Trade of the Prime Ministry as the Directorate General of Free Zones on the basis of Statutory Decree Nr. 438. In 1994, the Directorate General of Free Zones was included in the organization of the Under-secretariat of Foreign Trade of the Prime Ministry since the Under-Secretariat of Treasury and Foreign Trade was divided into two on the basis of Statutory Decree Nr. 534. However, this Decree was cancelled. Thereafter, as the result of the reorganization of two Under-Secretariats as the Under-Secretariat of Foreign Trade and the Under-Secretariat of the Treasury, with Law Nr. 4059, in 1994, the Directorate General of Free Zones began to carry out its activities within the structure of the Under-Secretariat of Foreign trade.

2.1.1The Operating Licence

In order to obtain an Operating Licence, the Turkish Trade Registration Gazette announces the establishment of the domestic firm or a certificate indicating the registration of the foreign firm is required in addition to other related documents. This requires trade registration either in the Chamber of Commerce or/and Industry for operation in free zones. It is important to make clear that:

1. Real persons or legal entities residing in Turkey, holding a trade registration may engage in free zone activities in offices they have constructed or rented by obtaining an Operating Licence from the Under-secretariat for Foreign Trade Directorate General of Free Zones.
2. Turkish residents who intend to establish a firm for operation in a free zone must apply to the Under-Secretariat for Foreign Trade, Directorate General of Free Zones, submitting the draft of their contract to substitute the document mentioned above along with other documents. Only after that their application is approved they may go along with the procedures to establish their firms. After the firm is established, the

application is made by this firm to the Under-secretariat for Foreign Trade General Directorate of Free Zones along with the Trade Registration Gazette advertising the establishment of the firm together with the rental contract to obtain an Operating Licence.

2.1.2 Rules for setting up firms in Turkey or free zones by individuals or legal entities residing abroad

Legal entities that wish to establish firms in Turkey or free zones need:

a) A certificate of activity;
b) An Activity Report for the previous year (including balance sheet and field of Activity for the previous year);

Individuals residing abroad can establish firms in Turkey by giving a passport copy, a detailed description of the commercial and industrial background, the verification documents, a letter of intention from the individual or legal entity residing abroad, stating that the required capital for the desired activity to be realized in Turkey shall be transferred into the country, a draft contract of the company to be established, an application form, etc. The Certificate of Activity and a passport copy shall be certified by either the relevant Turkish Consulate or in accordance with the provisions of the Convention Abolishing the Requirement of Legalization for Foreign Public Documents, prepared on the basis of the Hague Conference on International Private Law. The passport can be certified by a Public Notary in Turkey, and in this case no other certification is required.

BREAKDOWN OF THE TRADE VOLUME BY SECTORS (1000 US $)

2004 March

Sectors	Domestic market to Zones	%	Zones to Domestic Market	%	Abroad to Zones	%	Zones to Abroad	%	Total	%
I.AGRICULTURE	36.094	5,8	67.305	4,2	95.519	5,7	37.734	4,0	236.651	4,9
A-VEGETABLE PRODUCTS	*24.977*	*4,0*	*58.476*	*3,6*	*79.550*	*4,7*	*35.406*	*3,8*	198.409	*4,1*
B-LIVESTOCK PRODUCTS	*10.202*	*1,7*	*8.819*	*0,5*	*14.749*	*0,9*	*1.207*	*0,1*	34.977	*0,7*
C-FISHERY PRODUCTS	*667*	*0,1*		*0,0*	*1.176*	*0,1*	*837*	*0,1*	2.680	*0,1*
D-FORESTRY PRODUCTS	*248*	*0,0*	*11*	*0,0*	*43*	*0,0*	*284*	*0,0*	586	*0,0*
II. MINING&QUARRY	2.569	*0,4*	647	*0,0*	649	*0,0*	3.645	*0,4*	7.510	*0,2*
III.INDUSTRY	579.131	*93,7*	1.545.211	*95,8*	1.580.123	*94,3*	891.179	*95,6*	4.595.644	*95,0*
A-PROCESSED AGRICULTURAL PRO.	*15.759*	*2,6*	*22.603*	*1,4*	*77.271*	*4,6*	*81.386*	*8,7*	197.020	*4,1*
B-PROCESSED PETROLEUM PRO.	*1.251*	*0,2*	*139.708*	*8,7*	*133.087*	*7,9*	*301*	*0,0*	274.347	*5,7*
C-INDUSTRIAL PRODUCTS	*562.120*	*91,0*	*1.382.900*	*85,7*	*1.369.765*	*81,7*	*809.491*	*86,8*	4.124.277	*85,2*
TOTAL	617.794	*100*	1.613.163	*100*	1.676.291	*100*	932.558	100	4.839.805	*100*

Table 4

It is possible to note from the tables which industry is the simplest sector to invest in and maybe which companies have most benefits (table 4).
Table 5

BREAKDOWN OF THE TRADE VOLUME BY COUNTRIES (US$ 1000)
2004 March

Countries	Inflow to Zones	%	Outflow from Zones	%	Total	%
I. OECD COUNTRIES	**1.110.779**	***48,4***	**620.319**	***24,4***	**1.731.098**	***35,8***
A.EU COUNTRIES	*901.570*	*39,3*	*557.443*	*21,9*	1.459.013	*30,1*
B. OTHER OECD COUNTRIES	*209.209*	*9,1*	*62.875*	*2,5*	272.085	*5,6*
II. OTHER EUROPEAN COUNTRIES	**56.245**	***2,5***	**21.832**	***0,9***	**78.078**	***1,6***
III.TURKIC REPUBLICS	**47.569**	***2,1***	**42.050**	***1,7***	**89.619**	***1,9***
IV.FORMER USSR	**81.150**	***3,5***	**46.224**	***1,8***	**127.375**	***2,6***
V.ISLAMIC COUNTRIES	**80.311**	***3,5***	**113.517**	***4,5***	**193.828**	***4,0***
VI.OTHER COUNTRIES	**300.236**	***13,1***	**88.615**	***3,5***	**388.851**	***8,0***
VII.TURKEY	**617.794**	***26,9***	**1.613.163**	***63,4***	**2.230.957**	***46,1***
TOTAL	**2.294.084**	***100***	**2.545.721**	***100***	**4.839.805**	***100***

On the other hand it must be understood that the companies which have main interests to develop and to use in the free zones are the European countries as shown in table n. 5.

The companies from the EU countries are those that could be most damaged by the elimination of the free zones in Turkey.

2.1.3. Evaluation and granting of Operating Licences by the Directorate General

Firms intending to rent a closed area must sign a rental contract with one of the users, holding a Renting Operating Licence within 30 days of being notified. Only after a copy of the rental contract is approved by the related Zone Directorate and is sent to General Directorate of Free Zones, can the Operating Licence be obtained. Those who are not found eligible for an Operating Licence shall have their application fee returned. The term of the Operating Licence is 10 years for tenant users who intend to rent a completed office, and 20 years for investor users who intend to build their own offices.

However, this term is 15 years for tenant users and 30 years for investor users who are engaged in production activities. If the investor users engaged in production activities intend to operate in other fields of activities, then the term of the Operating Licence is 20 years on the condition that they operate in their same offices. If the investor users holding an Operating Licence in activities other than production, then the term of the Operating Licence is also 20 years. Tenant users may start to operate when they receive their Operating Licences, but when investor users receive their Operating Licence, they must obtain another licence, the "construction licence" to go ahead with their construction projects. After they have finished their construction project they must obtain a permission to start their activities. At the same time during the construction period they can start their activity renting a closed area during the construction period.

2.2 A case study: the technological development zones

Following the example of the results of the Turkish free zones, an important law was recently approved concerning the development of technological investments in Turkey: the Technological Development zones (TDZ) Law numbered 4691, enacted in July 2000. The objective of the law, through the cooperation of universities, research institutions and the production sector, is to create technological information in order to give the industry of the nation a structure fit for international competition and exportation; to introduce innovations in products and production methods, to raise the quality or standard of products, to increase productivity, to decrease the costs of production, to market technological knowledge, to help the transfer of technology, to provide the technological infrastructure which will quicken the entry of the foreign capital which, in turn, will provide high/advanced technology, etc.[7]

After the enactment of the Law, twelve new science and technology parks were approved by the Ministry of Trade and Industry. These TDZs are established in four different Turkish cities, but only five of them are operative while the remaining ones are still at initial construction phase. As the Law enforces involvement of universities for establishment of TDZ, each of these science and technology parks are linked with at least one university. All science and technology parks are situated within university grounds, in order to create close relationships with the university community.

The increasing demand from companies and entrepreneurs encourage universities to invest in the establishment of TDZs. One of the main reasons behind the demand of the companies is the tax incentives provided by Law.

2.2.1. The tax incentives

The Law provides two types of tax incentives to the companies. First is the income tax exemption for research personnel, including academics. With this incentive, companies are able to pay more salaries to their staff and they can have also more money to spend on research. The second type is corporate tax exemption for the portion of profit generated through research and software development activities. Also, with these incentives the companies can spend and invest more in research projects.

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[7] For further information about ICT in Turkey, see Contribution of Turkey to E-Europe 2003, Progress Report, State planning Organization Information society department, January, 2004

METU-Technopolis is the first and the biggest science and technology park in Turkey. Opened in 2000, it hosts around 120 companies employing over 1000 researchers. The majority of the companies are technology based and develop software products and services.

Between 1999 and 2004, the number of companies has increased from 13 to 120. The majority of existing companies are operating in ICT and software development sectors. Almost 75 percent of companies deal with the ICT and software industry. These companies supply much of the knowledge based products and services. In 2003, METUTECH companies have exported 7,5 Million USD of technological products and services. The export markets of the companies are countries like US, Singapore, Hong Kong, Dubai, Holland, Russia, Germany England, etc.

2.2.2 The results of TDZ.

The importance of the Technological Development Zones is strictly connected to the results of these zones. Even if in Turkey the role of innovation and entrepreneurship has always been culturally important, there wasn't a scientific framework in the country. With these experiments, new possibilities have opened up for collaboration between industries, universities and scientific work groups. Many companies are trying to contact universities to develop new products and services through the use of Information and Communication Technologies. The existing 35 project collaborations between academics and companies are important but not sufficient compared to the number of projects running. Especially, university needs to change its attitude towards joint projects and must develop innovative alternatives.

At the same time many managers have understood that new technologies are the keys to be able compete throughout the world.

We must consider that there are also a lot of benefits from the use of the incentives because although in the short term there are less earnings from the taxes, in the long term the industries grow in the international market and the country benefits from its new role on the international market.

On the other hand, the tax incentives granted by the Law have become a significant facilitator for the companies. The cash savings stemming from tax incentives are canalized to new research and innovation projects. Since the income tax incentives provided by the Law have a positive cash flow effect on companies' financial statements, the desire of companies to move into TDZ has significantly increased. Furthermore, the corporate tax incentive has caused more capital to be invested in software development and research activities.

Encouraged by these results, the policy makers are planning to expand the level of incentives for innovation and research activities. The successful results have also spurred attention for strategic planning for the knowledge economy. At this moment there are no government resources in TDZ; so far the government has not allocated any funds for helping the technological parks.

For example, METUTECH has used a different approach in order to overcome this obstacle. The existing funding facilities are used for infrastructure development while upstream investments are realized through several fund raising models. First, eligible companies have been encouraged to lease the land and construct their own buildings. Second, advance payment schemes with promotional conditions areproposed to companies. And an income sharing build-operate-transfer model was implemented. The results were successful in all aspects. Over 10 million USD upstream investments were developed. Maybe the same models can be used in other parts of the country.