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Uluslararası Yatırımcılar Derneği
International Investors Association

INTERNATIONAL DIRECT INVESTMENTS 2018 YEAR-END EVALUATION REPORT

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Contents

Charts and Tables

Charts

Tables

EXECUTIVE SUMMARY

2018 was the year of changes for Turkey. The Parliamentary system was transformed to the New Presidential System by the end of June. Following this change in the government system, in the second half of the year was a period of intense market volatility and rising economic stress due to the slump in Turkish Lira that was precipitated by political tensions with the US. The New Economic Program, which was announced in September, provides a good foundation for gradually restoring macroeconomic stability by the implementation of visionary fiscal policies.

Global economic growth in 2018 remained strong despite the Trump government expediting trade tension in the global market. Whilst the US government continuously stressed the global economy during the year, US economy has been expanding rapidly thanks to procyclical fiscal policy and the protectionist measures taken; unemployment falling to 3.7 percent in September, its lowest level since 1969. The stronger dollar and the interest rate decision of Fed had notable impact on the other economies outside of US. In particular concern, this expansion is likely to impact emerging markets, especially if capital outflows accelerate and money rapidly returns to the US. Growth in the Euro area on the other hand moderated in 2018, slowest pace since 2014. China and many other Emerging Market and Developing Economies are exhibiting signs of slowdown, too.

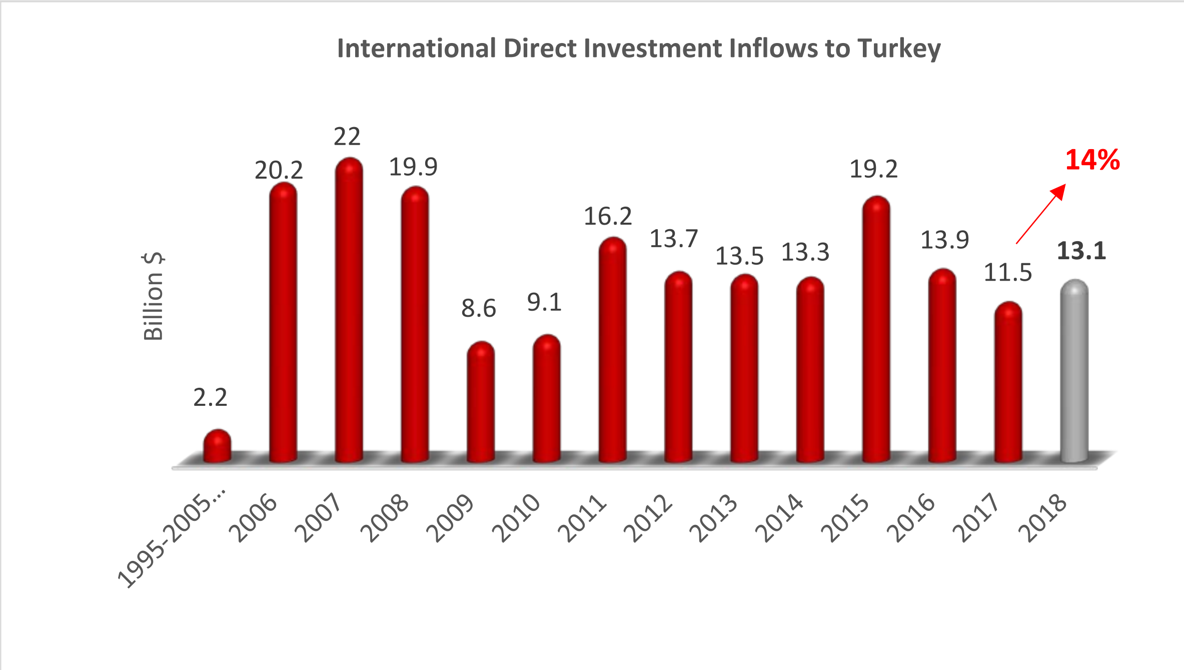
As a result of slowdown in global economy and mainly in the developed economies, global FDI inflows in 2018 are expected to fall by 19%. Regarding the source of FDI inflows to Turkey, the main FDI sourcing countries are historically from the European region and yet was the same in 2018. Whilst the slowdown in capital flows to Turkey was significant, it did not technically amount to a sudden stop. In political history of Turkey, the country experienced two sudden stop episodes in the past 20 years, namely during the 2000-2001 domestic financial crisis and 2008-2009 global financial crisis. The decline in capital inflows in 2018 was milder than those earlier episodes and the capital flow shocks in 2014 and 2016. The decisive steps which will be taken by the government under the New Economic Program with the implementation of visionary fiscal policies, are expected to accelerate FDI inflows and the enlargement of the existing investors.

In this report “International Direct Investments 2018 Year-End Evaluation Report”, FDI inflows to Turkey in 2018 and disclosed number and value of M&As were analyzed in detail. The predictions of international organizations and non-governmental organizations for global economic outlook of 2018 and forthcoming years along with the rankings of Turkey on the global indexes were provided.

INTERNATIONAL DIRECT INVESTMENT INFLOWS TO TURKEY

International Direct Investment Inflows to Turkey Reached $13.1 billion in 2018

International Direct Investment (FDI) inflows to Turkey reached **$13.163 million** by the end of 2018 **with an increase of 14%** compared to 2017.



Source: Central Bank of Turkey *(incl. real estate purchased by non-residents)*

The total FDI inflow in 2018 ($13.1 billion) consisted of $6 billion net capital, $1.1 billion other capital and $5.9 billion real estate purchased by non-residents.

Regarding the FDI Inflow in 2018 ($6.534 million), it fell by 12% compared to the previous year (2017: $7.401) million). However, real estate purchased by non-residents had an important share of 45% in the total inflows and increased by 27% compared to last year.

Distribution of International Direct Investment Inflows to Turkey

(Million $)	2013	2014	2015	2016	2017	2018
Capital (Net)	9.936	8.371	11.729	6.904	5.532	6.064
Inflow	**10.523**	**8.632**	**12.093**	**7.534**	**7.401**	**6.534**
Outflow	**587**	**261**	**364**	**621**	**1.869**	**470**
Other Capital (Net)	578	645	3.389	3.156	1.371	1.184
Real Estate (Net)*	3.049	4.321	4.156	3.890	4.643	5.915
Total (FDI)	**13.563**	**13.337**	**19.274**	**13.950**	**11.546**	**13.163**

Source: CBT ***(incl. real estate purchased by non-residents)*

In 2018, **services sector** was the leading sector in the total FDI inflow ($3.625 million) with a share of 55.5%. Services sector was followed by **industry sector** with a share of 44% ($2.865 million).

When we look at the distribution of subsectors; **Manufacturing** is the **leading sector** with approximately $2 billion of FDI inflow, followed by **Wholesale and Retail Trade** and **Finance and Insurance.**

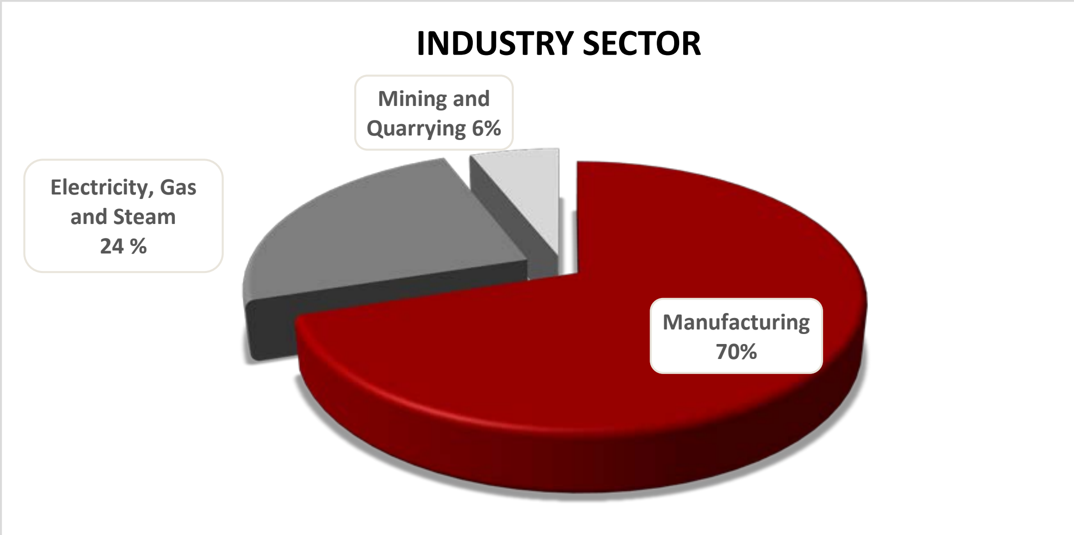
Sectoral Distribution of International Direct Investments

($ million)	2013	2014	2015	2016	2017	2018
Agriculture	**47**	**61**	**31**	**38**	**29**	**44**
Industry	**5.390**	**4.258**	**5.784**	**3.067**	**2.022**	**2.865**
Manufacturing	**2.843**	**2.742**	**4.237**	**2.240**	**1.202**	**1.999**
Food, Beverages, and Tobacco Products	475	451	983	706	198	504
Other non-Metallic Mineral Products Manufacturing	29	**158**	112	24	64	330
Chemicals and Chemical Products Manufacturing	272	491	340	288	142	321
Coke Coal and Refined Petroleum Products	236	101	1.809	0	0	164
Computer, Electronics and Optical Products Manufacturing	607	926	142	242	157	149
Electricity, Gas and Steam	**1.794**	**1.131**	**1.338**	**677**	**371**	**679**
Services	**5.086**	**4.313**	**6.278**	**4.420**	**5.350**	**3.625**
Wholesale and Retail Trade	**379**	**1.137**	**599**	**688**	**1.077**	**1.116**
Finance and Insurance	**3.415**	**1.470**	**3.516**	**1.766**	**1.464**	**1.041**
Banks	1.608	912	2.775	1.323	1.137	756
Activities of Holdings	229	226	438	272	288	167
Other Financial Activities	40	133	185	42	34	80
Insurance Activities	1.538	199	117	128	5	38
Transportation and Storage	**364**	**594**	**1.524**	**635**	**1.333**	**490**
Accommodation and Food and Beverages Activities	**59**	**24**	**11**	**250**	**82**	**238**
Real Estate Purchases by Non-Residents (Net)	**3.049**	**4.321**	**4.156**	**3.890**	**4.643**	**5.915**
TOTAL	**13.563**	**13.337**	**19.274**	**13.950**	**11.546**	**13.163**

Source: CBT

The inflows to **Industry Sector increased** by around **30%** compared to 2017 and reached $2.865 million by the year-end. Regarding the changes in the sub-sectors; **Manufacturing significantly increased by 40% ($1.999 million)** and took the lion share from Finance and Insurance sub sector in 2018, whilst it is the leading sub sector under Industry sector with a share of 70%. It was followed by **Electricity, Gas and Steam** sub sector with a share of **24%** which doubled its intake in 2018 and reached **$679 million**. Despite the peak in last year, **Mining and Quarrying sub sector** radically decreased and constituted $183 million with a share of **6%**.

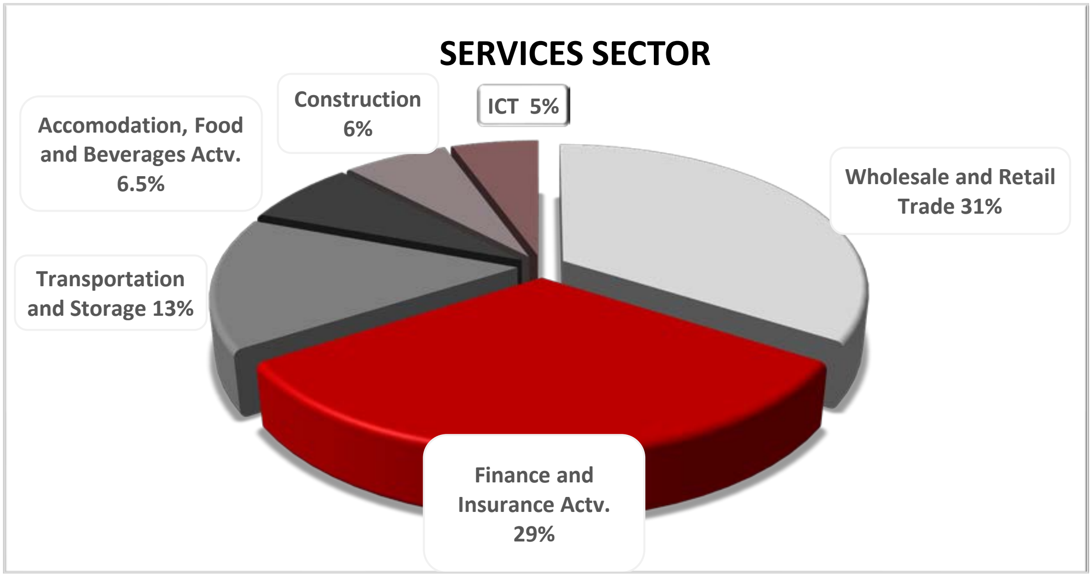
Distribution of FDI Inflows to Industry Sectors in 2018



Source: CBT

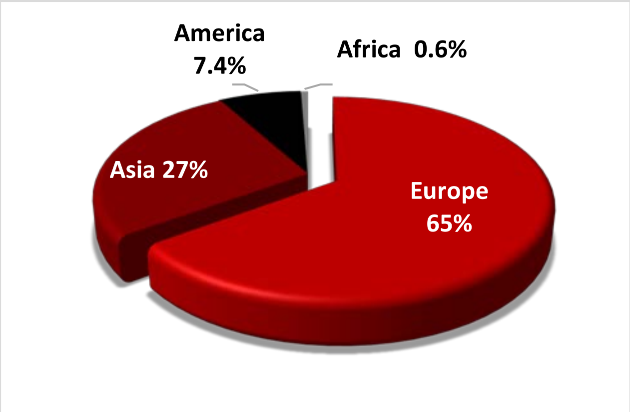
The inflows to **Services Sector significantly decreased** by **32%** compared to 2017. This year **Wholesale and Retail sub sector** became **the leading sub sector** under Services Sector with a share of **31%** and reached **$1.116 million.** It was followed by **Finance and Insurance sub sector which** decreased by 29% compared to last year and recorded as $1.041 million. **Transportation and Storage** sub sector radically decreased to $490 million, with a share of 13%, and ranked **third**. These sub sectors were followed by; **Accommodation, Food and Beverages Activities, Construction,** and **ICT** with 6.5%, 6% and 5% shares, respectively.

Distribution of FDI Inflows to Services Sector in 2018



Source: CBT

Distribution of FDI Inflows by Countries and Regions in 2018



Source: CBT

	Countries	FDI Inflow (million $)	Share (%)
1	Netherlands	833	13
2	Azerbaijan	516	7.9
3	Italy	509	7.8
4	Austria	465	7.1
5	USA	446	6.8
6	UK	409	6.2
7	Germany	349	5.3
8	Luxembourg	329	5
9	France	293	4.5
10	Taiwan	246	3.7
	Other	2.139	32.7
	Total (Capital Inflow)	6.534	100

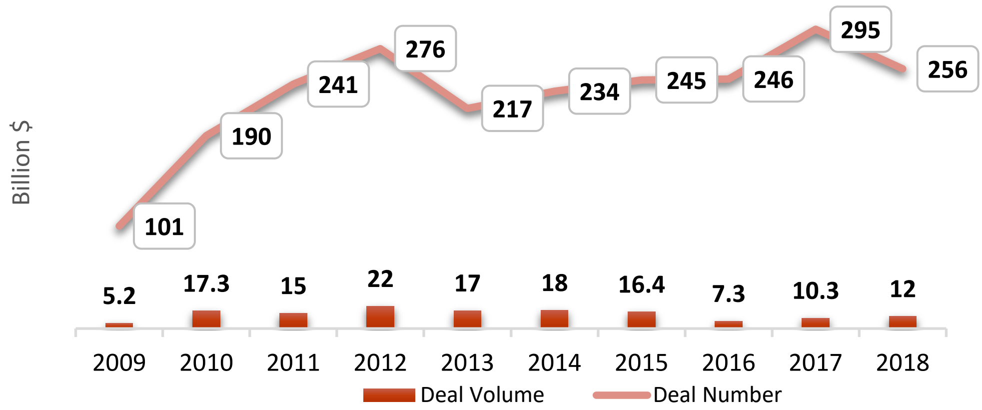
As of 2018 year-end, the main FDI sourcing countries to Turkey are **the Netherlands, Azerbaijan** and **Italy**. In regard to the distribution of FDI inflows at regional level; **European countries** are the main source of the FDI inflows with a share of **65%** followed by **Asian countries** with a share of **27%**, **America 7.4%** and **Africa 0.6%.**

MERGERS & ACQUISITIONS (M&A)

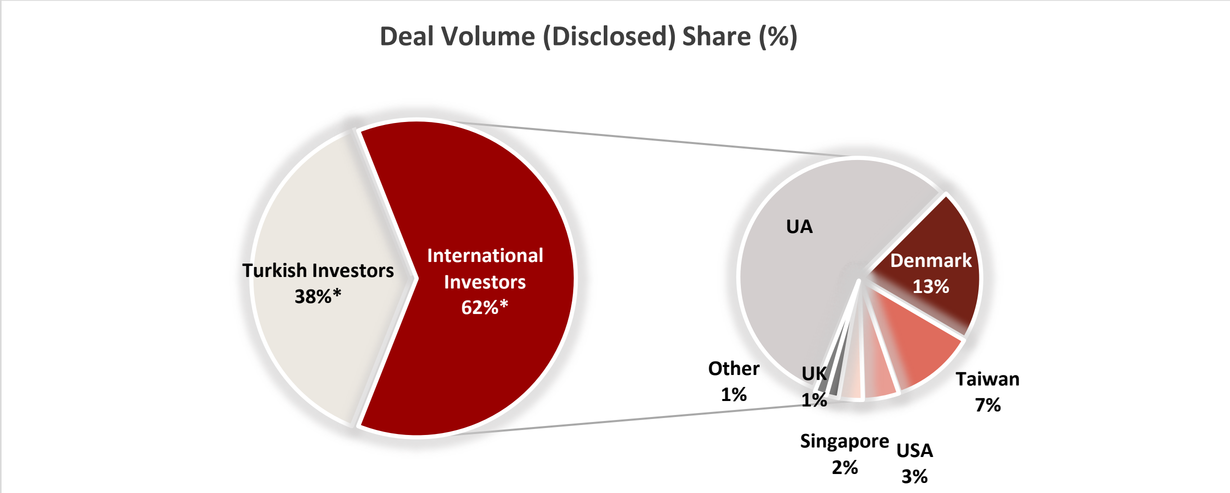
According to Deloitte's "*Annual Turkish M&A Review 2018 Report*" which provides an overview of the mergers and acquisitions in Turkey; the total of M&A deals was 256 with the estimated volume of $12 billion. This estimated volume corresponds to 17% increase comparing to 2017. The share of **international investors in the total deal volume** is 63**%,** highest share since 2015.

Regarding the number of deals realized by International Investors, number was similar to last year, recorded as 74 transactions. Excluding the privatizations where Turkish investors were more active, the deal volume of international investors increased by 38% compared to 2017 and reached $7.6 billion in 2018 by doubling the level of 2016.

Deal Volume and Deal Number in 2018



Source: Deloitte Annual Turkish M&A Review Report 2018



Source: Deloitte Annual Turkish M&A Review Report 2018
*(*including non-disclosed deals- Turkish Investors 37%, International Investors 63%)*

In 2018, the number of deals executed by the EU and North American investors increased by 12% compared to 2017, the investors from Asia Pacific and Gulf regions had again limited involvement in deal activity.

Regarding the deal number; the number of deals executed by the European investors once again sealed the highest number of international investors' deal activity in 2018 with a share of 49% and recorded as 36 deals. However, the total volume of European investors has slumped comparing to 2017 and constituted 29% of the total deal volume. In contrast to the decrease in the volume of deals originated from the European region, the investors from UAE, Denmark and Taiwan contributed to the deal volume of international investors to a great extent with big ticket transactions.

In 2018, it was observed that the investors from USA continued their interest in the Turkish market despite to the volatile relations with 15 deals. Additionally, investors from Germany, Italy and the UK yet again were active investors.

Top 5 Disclosed M&A in 2018

Target	Sector	Acquirer	Country	Stake	Deal Volume (Million $)
**Denizbank ** **	Financial Services	Emirates NBD Bank	UAE	100%	3.191
U.N. Ro-Ro	Transportation	DFDS	Denmark	99%	1.172
Trendyol	Internet & Mobile Services	Alibaba	China	n/a	728
Oyak Cement	Manufacturing	Taiwan Cement Corp	Taiwan	40%	640
Gram Games	Internet & Mobile Services	Zynga, Inc.	USA	100%	250

Similar to the previous year, technology, internet and mobile services yet again were the leading sectors in terms of the deal number in 2018. These sectors constituted 38% of the total deal number. This year, financial services sector represented 27% of the total deal volume and became the leading sector. In 2018, logistics and transportation sector ranked second with 10% share of the total deal volume, followed by media with a share of 8%. Although technology, internet and mobile services were the leaders in terms of the number of deals, they were thus behind the financial services and logistics sectors regarding deal volume due to the small sized deals.

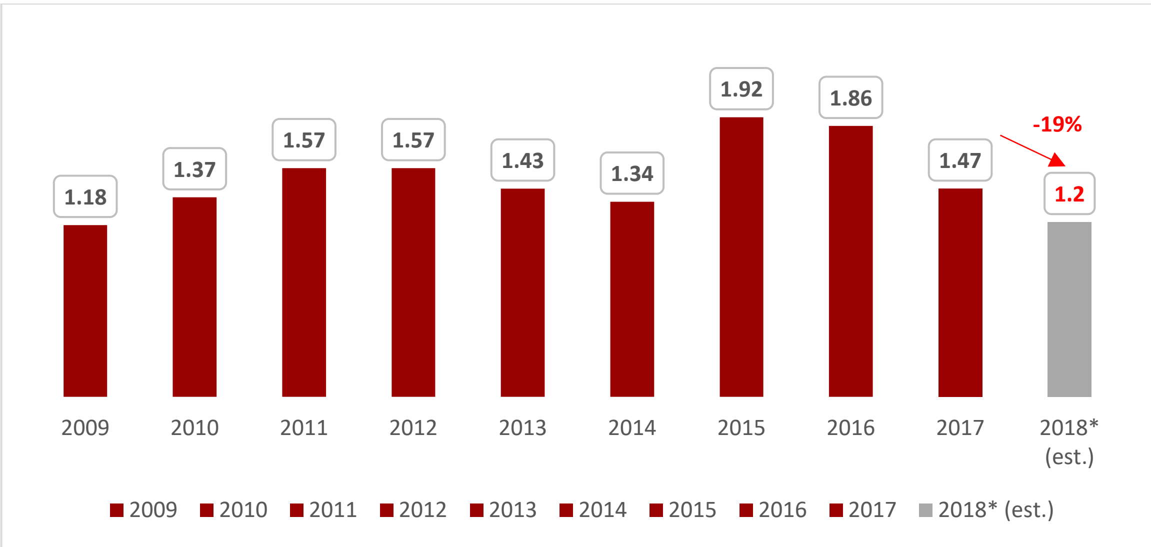
According to Deloitte's report; rising expectations for a global economic slowdown in addition to continued macroeconomic challenges in the domestic market raise concerns about investor appetite for M&A in 2019; however it was emphasized that investors with a strategic and long-term view are expected to continue to invest on selected opportunities in the Turkish market.

According to EY's 'Mergers and Acquisitions 2018 Report'; it is expected that small and medium sized deals will lead the transactions pipeline and many awaiting big size deals will be realized in 2019. Energy sector which was one of the target sectors with active transactions is expected to be in the focus of the investors due to the private sector deals and the privatizations. The appetite of the investors for food and beverages and the manufacturing sectors with value added production will be at the forefront of M&As in 2019.

GLOBAL TRENDS and TURKEY'S RANKINGS

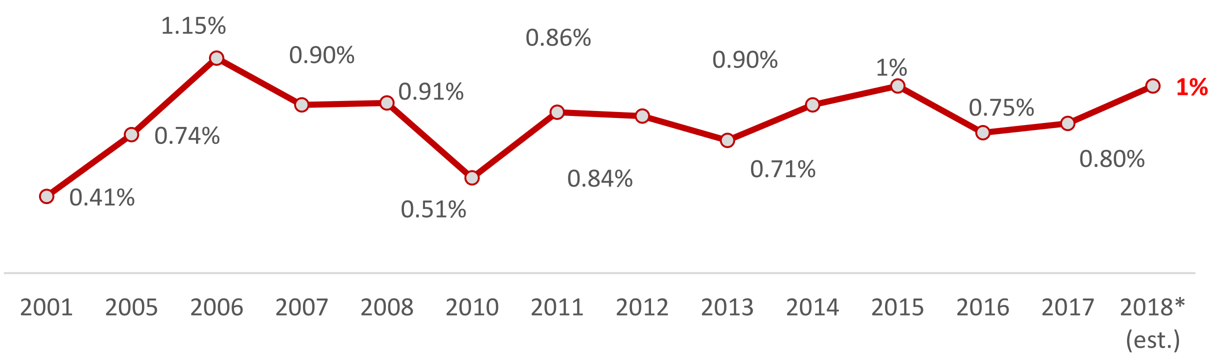
In regard to the preliminary findings of the World Investment Report (WIR) 2019 which is annually published by United Nations Conference on Trade and Development (UNCTAD); it was estimated that global FDI inflow will be decreased by around 19% and will be recorded as $1.2 billion by the end of 2018. The **decline** was concentrated in **developed countries** where FDI inflows fell by 40% to an estimated $451 billion, mainly due to large repatriations of accumulated foreign earnings by United States SMEs, following tax reforms.

Global International Direct Investments



(Trillion $) *Source: UNCTAD WIR 2019 Preliminary Findings*

Turkey's Share in the Global FDI (%)



Source: UNCTAD WIR 2019 Preliminary Findings

This decline in the **developed economies** caused an unprecedented 73% decline inflows to Europe, reaching only $100 billion (net of large negative flows in some countries) – a value last seen in the 1990s. A decrease was also reported in the United States (-18%) to $226 billion.

In contrast, FDI to **developing economies** remained resilient, with an increase of 3% to $694 billion. The share of developing economies in global FDI reached 58%. Half of the top 10 host economies are developing economies. Among developing regions, flows increased by 5% in developing Asia and 6% in Africa (although growth there was concentrated in very few countries) but declined in Latin America and the Caribbean (-4%). East and South-East Asia was **the largest host region**, accounting **for one-third of global FDI in 2018** and **almost all of the growth in FDI** to developing economies. FDI to the **transition economies** declined by 8% to $44 billion.

In 2018, IMF has lowered its predictions both for Turkey's and the global economies growth in its World Economic Outlook Report 2018. IMF has lowered its global economies growth predictions from 3.9% to 3.7% due to increasing risks. For Turkey's growth, the prediction was revised from 4.2% to 3.5% in 2018. Regarding the consumer price index of Turkey to reach 15% by the end of 2018, 16.7% by the end of 2019. Unemployment rate was predicted 11% by the end of 2018 and 12.3% by the end of 2019. Finally, the Report precited the GDP ratio of current account deficit to GDP to reach 5.7% by the end of 2018 but decline to 1.4% by the end of 2019.

According to the World Economic Forum's Global Competitiveness Report 2018; Turkey has declined by 3 points among the competitor countries compared to 2017 and reached 61st place in 2018. With the "Global Competitiveness Index 4.0" which was added to the Report, a new competitiveness field has been created for global rankings. The **"Country for Business 2018"** index published within the Report shows **Turkey ranked as the 56th country**. When we look at the competitor countries in the region, Bulgaria is ranked 46, the Czech Republic 28, Hungary 42, Poland 34 and Romania 43, it can be stated that Turkey holds a good place in the ranking.

Ranking	Economy	Score
Hungary	48	64.3
Mauritus	49	63.7
Bahrain	50	63.6
Bulgaria	51	63.6
Romania	52	63.5
Uruguay	53	62.7
India	58	62.0
Kazakhstan	59	61.8
Colombia	60	61.6
Turkey	61	61.6

Source: WEF 2018 Global Competitiveness Report Ranking

Despite the lowered predictions of some indexes, Turkey's ranking on the **Doing Business 2019,** was increased by **17 points**, reaching **43rd place in the rankings** compared to last year's ranking of 60. It has been reported that Turkey is within the 10 countries that has shown the most notable improvement since the first launch of the Doing Business Report.

Turkey has shown the most progress in: Ease of Doing Business, Construction Permits, Getting Credit, Paying Taxes, International Trade, Enforcing Contracts, Registering Property and Starting and Closing Businesses. If we look at the countries in the region; Bulgaria has declined by 9 points to 59th place, the Czech Republic declined by 5 points to 30th place, Hungary declined by 5 points to 53rd place and Romania declined by 25 points to 52nd place. Only Turkey and Poland, located in the Eastern European region increased by 12 points reaching 33rd place in the ranking.

According to the OECD 2018 Economic Outlook Report; OECD has increased Turkey's expected 2018 inflation and growth rate. Turkey's **predicted growth rate for 2018 increased from 3.2% to 3.3%. Turkey's predicted inflation rate for 2018** significantly **increased from 12.0% to 16.8%** (year-end inflation rate: 21.28% TurkStat)

The **3.7% growth rate for 2018 for the world economy has remained the same** but the **predicted growth rate for 2019 has declined by 0.2 points to 3.5%.** The main factors behind this decline are: the slowdown of global trade and investments due to the reciprocal customs tariffs, the capital outflows of developing markets and the devaluation of currencies.

TURKEY'S RANK IN INTERNATIONAL INDEXES

INDEX	TURKEY'S RANK									CHANGE
	2010	2011	2012	2013	2014	2015	2016	2017	2018	
World Bank Ease of Doing Business Index	60	68	72	69	51	63	69	60	43	↑
UNCTAD World Investment Report FDI Inflow Ranking	29	26	24	22	22	20	24	26	-	-
WEF Global Competitiveness Index	61	59	43	44	45	51	55	53	61	↓
IMD Global Competitiveness Index	48	39	38	37	40	40	38	47	46	↑
Transparency International Corruption Perceptions Index	61	54	53	64	53	66	75	81	78	↑

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  - World Economic Forum – www.weforum.org
  - Institute for Management Development – www.imd.ch
  - Transparency International - https://www.transparency.org