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How a company does business with a country that does not "exist": A case study of Genel Energy and Somaliland

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Abstract: The aim of this paper is to develop a better understanding of how the international non-recognition of a country impacts on its ability to attract foreign investment and on the investment decisions of potential investors. Through the use of the case study of Genel Energy in Somaliland this study comes to a number of conclusions: Firstly, determinants of foreign direct investment (FDI) in Sub Saharan Africa (SSA) as identified in existing literature such as political instability, infrastructure, human capital and insurance costs are similarly relevant in Somaliland. Secondly, this research identified three key elements of Somaliland's international non-recognition as having a negatively intensifying effect on the factors that determine the flows of FDI to SSA. These have been classified as inability to develop bilateral and multilateral relationships, lack of access to the international banking system and uncertainty (future status, sovereignty and borders).

Keywords: FDI, Non-Recognition, Somaliland, Political Instability.

Introduction

Reductions in barriers to international trade and investments, and technological advancements in transportation and telecommunications have led to a kind of "time and space compression" significantly reducing costs in international trade and ushering in an era of economic globalisation (Hill, 2009). The past three decades have seen a remarkable growth in both the number of transnational corporations (TNC) and the amount of FDI leading to the increased interdependence of traditionally distinct national economies. FDI is recognised as the primary mechanism of the interconnectedness of the global economy (Dicken, 2009). This perception seems to be consistent with the data: FDI today is worth US$1.4 trillion to the global economy and accounts for two-thirds of world trade and 69% of total foreign investment (World Bank, 2014; UNCTAD, 2013).

This is welcome news, especially for poor countries that do not have access to international capital markets (Asiedu, 2002). However, SSA, the poorest region, despite efforts to attract investment has not benefited from the FDI boom. The region's share of global FDI inflow, on an annual average basis, stood at 3.2% in the period 2000-2009; in comparison South Asia in the same period which received 19.2% of the global inflow of FDI (World Bank, 2009). When these countries were able to attract TNC's the common perception is that it was largely driven by abundant natural resources and market size (Morriset, 2001; Asiedu, 2006). For many observers the reluctance of TNC's to invest in SSA stems from factors that increase investor uncertainty such as political and macroeconomic instability, low growth, poor governance, weak infrastructure, hostile regulatory environments, and poorly managed investment promotion strategies (Dupasquier and Osakwe, 2005).

The self-declared Republic of Somaliland on the volatile horn of Africa shares with the region many of the obstacles to investment that impact on TNC investment decisions. However, in the case of Somaliland investor uncertainty is intensified by the country's non-recognition under international law. Somaliland's inability to enter into multilateral and bilateral trade agreements and exclusion from the international legal framework considerably raises the risks investors face and hence reduces the country's ability to attract FDI (Graham and Horne, 2013). Despite these considerable investment barriers Somaliland, over the last two years, has entered into several major agreements with a number of TNCs in extractive sectors, the biggest of which is Genel Energy PLC, an Anglo-Turkish petroleum company headed by ex-BP CEO Tony Hayward. These events raise a number of questions; firstly, how does the state's unrecognised status impact on the investment decision of the TNCs involved; and secondly, how does international non-recognition impact on the ability of the state to attract FDI. This work will attempt to answer these questions by studying the relationship between Somaliland and Genel Energy with the aim of shedding light on the particular barriers posed by the international non-recognition of Somaliland and how both entities deal with its impacts.

Literature review

On 26th June 1960, after 80 years of colonial rule, Somaliland gained independence from Britain and was immediately recognised by 34 United Nations members including the five permanent members of the Security Council (Drysdale, 2000). After only five days of independence Somaliland voluntarily united with Somalia which had gained her independence from Italy on the 1st of July 1960. Somaliland's haste to voluntarily relinquish its sovereignty and unite with Somalia was driven by strong Somali nationalism which had been festering in Somaliland and further intensified by Britain's decision to cede the Somali inhabited Ogaden region to Ethiopia (Nur, 2011). Somaliland's union with Somalia, as such, was intended to pave the way for the unification of all Somali territories under a single flag. This initial fervour soon gave way to despair for Somalilanders as their hopes for a viable state with equal distribution of power and wealth were dashed (SCPD, 1999).

The modern day Republic of Somaliland unilaterally declared independence from Somalia in 1991, after an extended civil war that led to the disposition of the oppressive Siyad Barre regime (Walls and Kibble, 2010). Twenty-three years on Somaliland remains internationally unrecognised despite four peaceful transfers of power, free and fair elections for the head of state, the lower house of parliament and local councils (Hoyle, 2000). Many observers agree that the overwhelming desire of Somalilanders to avoid a return to conflict and their aspiration to win international recognition has enabled much of the process of democratisation and associated peace and stability in the country (Kaplan, 2008; Eubank, 2012).

Somaliland's primary foreign policy strategy is to seek international recognition as a sovereign state. Its partners both on the continent and further afield, although happy to encourage stability, have continually stressed their concerns of the impact formal recognition might have on the wider Somalia predicament and the possible spill over of border related conflicts to other African states (Chatham House, 2011). These concerns are a perfect example of the hostility of the international system to non-state territorial units such as Somaliland. This hostility is most directly manifested, in Somaliland's case, in the norm of states refusing to recognise a secessionist entity without the recognition of the home state regardless of how dysfunctional or failed the home state may be(Graham and Horne, 2013).

Political non-recognition has had a huge negative impact on the country and its people both in terms of economic and social development. Somaliland's GDP for 2012 was estimated at US$1.4 billion. With GDP per capita estimated at $347 the fourth lowest in the world (World Bank, 2013). As a consequence of international non-recognition Somaliland has some of the lowest levels of investment in the world, ranked 180th in the world for gross fixed capital formation. Furthermore, Somaliland has very high levels of unemployment standing at 72% for males and 83% for females (World Bank, 2013). The government of Somaliland has set economic growth as its priority and as a result has undertaken deep economic reforms in order to make the country more attractive to foreign investors. Many observers, such as Dupont (2011), stress that foreign investment is vital to Somaliland's economic and, ultimately, political viability as an independent state.

Background: Genel Energy PLC

Genel Energy PLC is an Anglo-Turkish oil exploration and production company listed on the London stock exchange. The company started its operations in 2002 as one of the first companies to engage with the Kurdish region of Iraq after the Iraq war (Genelenergy.com, 2014). Since 2002 the company has extended its operations across Africa through the acquisitions of material positions in Somaliland, Morocco and Ivory Coast. Genel Energy is an interesting case to study for this paper as it is by far the biggest foreign TNC currently active in Somaliland. Genel Energy is currently in the exploration phase of its operation in Somaliland with drilling expected to begin later this year (Genelenergy.com)

Theoretical Background

Despite the existence of numerous states around the world suffering from various degrees of international non-recognition and the rapidly increasing economic globalisation of the world driven by FDI, the dearth of research on the impact of international non-recognition on investment decisions of TNCs, and the unique challenges that these countries and foreign investors face as result of non-recognition, is rather surprising. Accordingly the literature studied for this review pulls together research from related fields such as the legal personality of states, FDI, TNC market entry strategies, political risk and work in the field of TNC nation-state relationships.

Unrecognised State in the literature

There are a number of de-facto states around the world; however, Somaliland is unique as the only completely unrecognised entity in the world today. The Royal Institute of International Affairs (Chatham House, 2011), suggests that there is, in fact, a hierarchy of international status. Recognised states are the pinnacle and enjoy uncontested recognition of their status as legal entities. They are followed by partially-recognised states that are recognised by one or more states but do not have access to international bodies as a result of contested legality or independence. Northern Cyprus and Abkhazia are good examples. Somaliland falls in to the final category as an unrecognised entity that might have the objective characteristics of a state but is unable to actualise this statehood (Chatham House, 2011). Scott Pegg's (1998) study, which assesses how international society and international law deal with unrecognised states and the impact these states have on those bodies, describes an unrecognised entity as a "de-facto" state. Defining a de-facto state:

> "As a secessionist entity that receives popular support and has achieved sufficient capacity to provide governmental services to a given population in a defined territorial area, over which it maintains effective

> control for an extended period of time without the recognition of de jure sovereign state".

Accordingly from hence forth in this paper unrecognised states will be referred to as de-facto states. Gerhard Erasmus (1988) and Robert Jackson (1987) discuss the legal personality of a state in international law and the criteria a geographical entity must meet to be recognised as a state. The authors also emphasise the hostility of the international legal system to fully functioning and stable de-facto states while providing full support for what Jackson (1987) refers to as 'quasi-states'; which are internationally recognised states that possess the same rights and privileges as any other state yet manifestly lack the rudimentary capabilities of a state (Pegg, 1998). Accordingly if these terms are applied to the Horn of Africa today then Somaliland would be the quintessential "de-facto" state while Somalia is a perfect fit for the definition of a "quasi-state".

Implications non-recognition for state and TNC

In terms of economics and trade the majority of literature on de-facto states seems mostly concerned with the economic implications of non-recognition for the state. For example, Milhalkanian (2004) and later Caspersen (2012: 40-45) argue that most de-facto states are low income countries and the cost of non-recognition increases over time as their economies decay (Graham and Horne, 2012). The meagre resources of de-facto states are generally reserved for security and the lack of access to foreign aid, particularly in budgetary assistance, leads to a lack of public investment in infrastructure and education (Collier and Hoeffler 2005). The lack of investment in infrastructure and human capital critically reduces the de-facto state's ability to compete with recognised nation-states for the private investment of TNCs (Dicken, 2011). Somaliland's budget of $210 million in 2013 is just about enough to run basic government services thus leading to the unavoidable neglect of key economic infrastructure such as roads, utilities and port facilities required for conducive business environments (Dahir, 2012; Somaliland.gov). In the case of Somaliland, its ability to compete to enhance its international trading position to capture a larger share of the gains of trade are further limited by a lack of access to the international banking system and insurance companies that insure foreign investment projects against political risk and guarantee property rights (Dolzler and Schreuer, 2008). Furthermore, Somaliland's exclusion from the international legal framework as a de-facto state raises an interesting question as to the jurisdiction of contracts agreed with TNCs, such as Genel Energy, and associated dispute resolution mechanisms (Maniruzzaman, 2005).

***Research Aims,* Objective and Research Question**

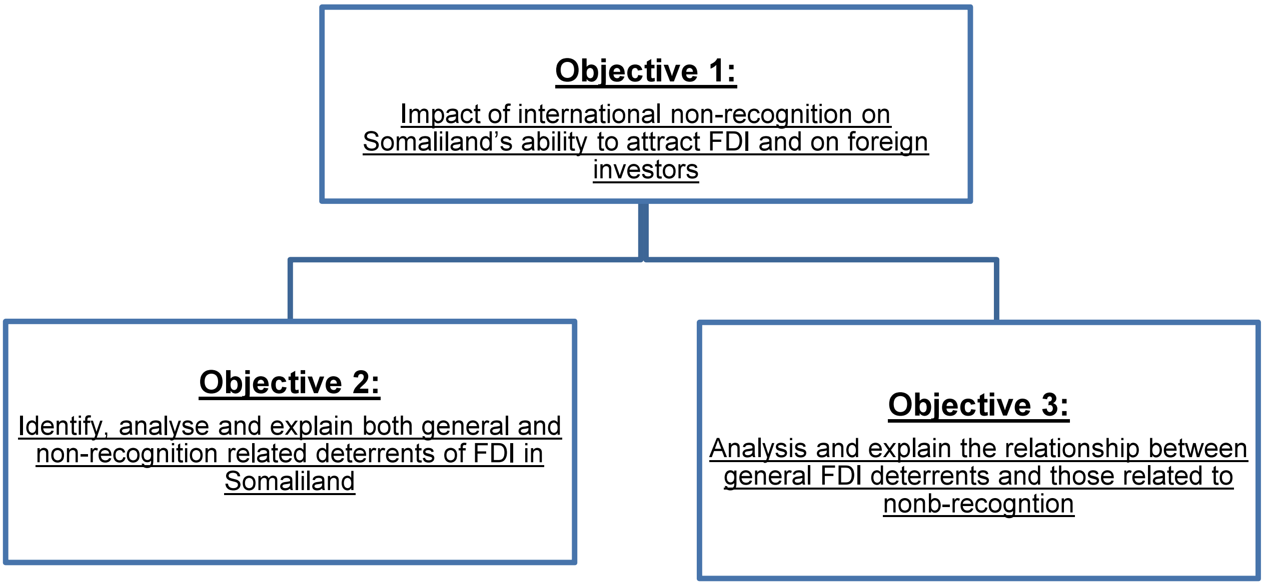
The aim of this study is to fill a gap in the existing literature that concerns countries that are not internationally recognised. Research in this field has tended to avoid discussing the implications of non-recognition for the attraction of foreign investment. Furthermore, existing literature in the field of FDI determinants have also not considered how such determinants might be affected by the international non-recognition of a state. Accordingly, the objectives of this study are as follows:

The overall objective of this research is to identify and examine the particular legal, political, economic and social barriers to foreign investment posed by a state's non-recognition under international law. The broad nature of the overall objectives leads to the development of a number of minor objectives which this research hopes to achieve. The first of these minor objectives, as is illustrated by figure 1, is to identify, analyse and explain the key deterrents of FDI in Somaliland both general and non-recognition related. Secondly; to identify, analyse and explain the relationship between the general deterrents of FDI and factors that are non-recognition related.

Accordingly the research question for this paper will be:

How does international non-recognition of a state impact on the inflow of FDI?

Fig. 1: Research objectives



Research Methodology

In order to understand the particular barriers of non-recognition and associated strategies TNC's and de-facto states employ to overcome such barriers, it is necessary to gain insight into the relationship between a de-facto state and a TNC. Accordingly to understand the detailed intricacies of this relationship requires the research to be analytical in nature. In order to avoid the risk of following a rigid methodology that does not permit alternative explanations of the reality of the issue and to better understand the nature of the problem, the research will follow an inductive logic in which theories are outcomes of the research (Saunders et al., 2007; Bryman and Bell, 2011). The author takes an Interpretivist epistemological position for this study due that the fact that the focus of the research is to analytically identify the strategies adopted by Genel Energy and Somaliland in the environment of non-recognition of the state and how this impacts on each entity and their consequent relationship. Also, constructivism (Saunders et al., 2007) in which social phenomena are continually developed by social actors, will be employed for this research because the strategy formulations of both entities are based on, and influenced by, the interactions between the entities and host country's business environment.

Because of the epistemological position of the author, research logic and ontological position, a qualitative research strategy will be employed for this study. Generally, qualitative research is concerned with attempting to make sense of, or interpret, phenomena in terms of the meaning people bring to them (Denzin & Lincoln 2011, p. 3). Such a viewpoint underpins this research since it is an attempt to understand how each entity interprets the issue of non-recognition and their subsequent actions.

Data Collection Methods

In order to gain the required level of understanding to sufficiently answer the questions raised, the case study design allows for the in-depth exploration of the issue within its context. The use of case study design will allow for the research to "produce rich holistic, and particularised explanations that are located in situational context through the using of multiple methods of data collection to uncover conflicting meanings and interpretations" (Bryman and Bell, 2011, p.114). In line with this principle, the case study of Genel Energy will be studied in the context of its operations in Somaliland. To gain a clearer understanding of the issues under investigation, semi-structured interviews with officials from Genel Energy and Somaliland government will be used in conjunction with the analysis of company and country specific documents.

Sampling
The researcher used a purposive sampling approach for this research, the aim of which is to sample participants in a strategic way, to ensure that participants who form the sample are relevant to the problem being investigated (Bryman and Bell, 2011). In line with expert sampling, the author interviewed participants who have first-hand experience or are currently experiencing the phenomenon being investigated. Accordingly, the participants selected for this study were high ranking officials from both Genel Energy and the Somaliland government who were directly involved in the negotiations between the two parties and as such are considered experts in the phenomenon under investigation.

Data Analysis
The most common forms of qualitative data analysis involve the use of thematic analysis. This is a set of analysis techniques that are used to search for themes within the data that refer to the topic and can be used to draw findings or conclusions (Bryman and Bell, 2011). Such thematic analysis techniques include the use of a content analysis approach which the author has selected for this research in order to analyse the data gathered. As Gao (1989) suggests, content analysis is best suited to the study of recorded data that can be easily repeated in order to continuously perform reliability checks. This tyupe of analysis is suited to this research as the interviews will be recorded and stored allowing for the replaying of interview recordings to aid in re-analysis and search for new themes. To ensure the reliability and validity of the findings, this paper will follow the systematic procedure of content analysis. Starting with the preparation of the data and determination of material to be included, selection units of analysis, developing coding categories, coding the material, analysing and interpreting results and drawing conclusions from the data.

Findings

All interviews were recorded using an electronic device; the interview data consisting of all three scripts was then converted into mp4 format in order to achieve compatibility with NVIVO software. The files containing the data were then imported into NVIVO before creating a project ready for coding. Before coding could begin, nodes were created. The coding procedure consisted of identifying relevant themes that are important to understanding the phenomenon under investigation. This process resulted in the construction of six nodes: drivers and opportunities, challenges and limitations, impact of non-recognition on Somaliland's ability to attract FDI, factors promoting FDI to Somaliland, strategies and objectives, long term future and stability. These nodes represent the themes that have been generated from the data. These themes have been categorised into the following three general categories for the purpose of analysis and discussion: motives for investment, impact of Somaliland's business environment, and sustainable strategy.

Firstly, in discussing the company's market entry strategy in Somaliland Participant 1 explains that Genel Energy made its entry into Somaliland in August 2012 with the award of an exploration licence for onshore blocks SL-10-B and SL-13. Genel's presence was further extended in November 2012 with the acquisition of a 50% in a further three blocks (SL-6, SL-7 and SL-10a). According to Participant 1 the market entry strategy employed by Genel Energy was a form of acquisition which gave the company a 75% stake in a production sharing agreement that had been signed with the government (Participant 1, 2014). Production sharing agreements are the most common form of contractual agreements for oil exploration and development companies, particularly in SSA where such arrangements are considered "standard practice" (Participant 1). Therefore, in terms of market entry for Genel it was necessary to accept the structures of the industry and adopt appropriate strategic choices to comply with those structures (De Wit and Meyer, 2010)

According to Dickens (2010) TNCs internationalise for one of two reasons: market orientation or asset orientation. According to Participant 1 Genel's key motive for investing in Somaliland was the potential to find oil, thus suggesting that Genel's investment decisions in Somaliland are driven by asset orientation reasons. Participant 1 in further supporting this reason suggests that "the potential to find oil is the key driver. The geology of Somaliland is analogous to that in Yemen, which is a prolific oil province, and the petroleum system has been proven through numerous oil seeps. There are potentially billion barrel prospects." Considering that Genel Energy is an oil exploration and development company it was expected that the main driver of investment would be "natural resources", however, another important driver of investment for Genel in Somaliland was the country's openness to trade (Participant 1,). Somaliland's tax regime is very investor friendly particularly for foreign investors who can benefit from a three year "tax holiday" with a further 50% reduction on any profits reinvested in to the enterprise after the tax holiday expires. According to Participant 1 this openness, and the oil discovery potential along with a production sharing agreement with the government which ensures that all capital invested by the company for exploration, production and facilities is recouped from the sale of the oil produced, made Somaliland an attractive investment opportunity.

Participant 2, on the other hand, while confirming Participant 1's suggestion of the potential for oil discovery being the main motive behind Genel's decision to invest in Somaliland, does not make any mention of trade openness as being a driver of investment. Data from Participant 2 does however bring to light two further motives for investing in Somaliland; geographical location and unexplored nature. Participant 2, in discussing the advantageous geographical location of Somaliland, describes the country as "being strategically placed on the world's busiest shipping lane (Red Sea) with Ethiopia another geologically interesting and landlocked nation sharing a long border to the west". Somaliland's access to the Red Sea shipping lanes and the existence of a deep water port in Berbera is vital to firms driven by supply-orientated variables such as natural resources (Dunning, 1990). The other investment motive emphasised by Participant 2 is the geologically under-explored nature of Somaliland which is surprising for country "that potentially has prospects for billions of barrels" (Participant 2). Participant 2 suggests that the lack of attention from oil exploration and production firms as well as other natural resource orientated firms is due to a number of factors. Firstly, general and warranted security concerns associated with a region that contains countries such as Somalia and Eritrea affected by conflict, terrorism and piracy has led to a reluctance of firms to commit to unproven resources. Secondly, Somaliland's unrecognised status for the past 23 years has kept it under the radar of potential investors. Participants 2's assertion that the geologically under explored nature of Somaliland was considered an advantage in the investment decision is interesting as it implies that aspects of Somaliland's status as an internationally unrecognised entity can be advantageous to resource orientated firms.

In summary, Genel's market entry strategy for Somaliland was not related to, or specially adapted for, the international political status of the country but was rather compliant with industry standards. Genel's motives for investing in Somaliland, in line with the general motives of resource-seeking firms (Dunning, 1990), is driven mainly by potential oil prospects in the country. It seems however from the data that Somaliland's openness to trade, geographical location and the under explored nature of its promising acreage were also significant in the firm's decision to invest in Somaliland.

As an unrecognised country located in the volatile Horn of Africa region, Somaliland poses a challenging array of political, economic, financial and operational risks to investors as is illustrated in figure 7. Participant 1, in defining the challenges that Genel faces in its operations in Somaliland, summarises these factors into the three following categories: security risks, political instability and infrastructure under development. In identifying security risks as the paramount threat to investment Participant 1 explains that "while security issues are of course an issue in many places around the world, is particularly acute in Somaliland." The security issue came to a head in September 2013 with Genel suspending operations due to issues relating to the "security of employees and subcontractors" (Participant 1). Participant 1, although not providing any particular details as to the specific security issues, hints at these security issues being related to "instability in the eastern regions of the country". Somaliland is bordered to the east by the semi-autonomous state of Puntland with which there has been a protracted border dispute stretching back to 1998 with sporadic episodes of violence (BBC, 2014). According to Participant 1, another key challenge for Genel's operations in Somaliland was the poor state of infrastructure in the country. Infrastructure of the host country is considered as one of the most important factors for resource seeking firms because good infrastructure enhances the productivity of investment (Wadhwa et al, 2011; Wheeler and Moody, 1992). Somaliland's infrastructure is extremely dilapidated with a shortage of paved roads to move heavy equipment from the port of Berbera to the extraction sites and the port itself suffering from years of neglect and under investment (Dahir, 2012). As Morisset (2000) and Wheeler and Moody (1992) both suggest for resource seeking firms, such as Genel, whose general goal is to export to markets outside of the host country the state of the host country's infrastructure, is of a major concern. Political instability is also identified by Participant 1 as being of long term concern for Genel. This political instability, however, is less to do with the internal political situation of Somaliland which is considered by Genel as being "relatively stable" (Participant 1) but rather the unresolved status of Somaliland's sovereignty.

Participant 2 while substantiating the factors of infrastructure, security concerns and political instability as posing significant operational risks to Genel in Somaliland also identifies a number of factors (some impacting directly on the operations of Genel and other more generic business environment related factors). Again, as with Participant 1, political instability as discussed in this interview is less concerned with the internal political situation of Somaliland than a concern "due to Somalia's claim of sovereignty over Somaliland" (Participant 2). Genel Energy, although recognising the existence of the risk that a future resolution to the status-quo could (however unlikely) result in a re-absorption of Somaliland in to Somalia, are very confident of the legality and longevity of their contracts with Somaliland (Participant 2). Along with the security and political instability related factors that impact on Genel's operations in Somaliland, Participant 2 also emphasises the high technical risk posed by the low quality and scarcity of human capital in Somaliland. Human capital is an important supply condition that is considered to be an important promoter of export and production-orientated FDI (Agiomirgianakis et al, 2003). Accordingly, the lack of highly technically skilled human capital in Somaliland requires Genel to bring in the required level of expertise from outside of the country thus increasing operational costs (Participant 2). Due to non-recognition, Somaliland is considered by the international community as a region in Somalia rather than a separate country in its own right. Consequently issues related to

Somalia but not present in Somaliland, such as piracy, conflict and terrorism significantly increase insurance costs (political risk, shipping, personnel etc) for firms wishing to invest in Somaliland such as Genel Energy.

In summary, the analysis of the interview data relating to the challenges and limitations faced by Genel Energy in its Somaliland operations has produced five factors that are considered risks to investment and, although not in this case, can act as deterrents to FDI. These factors are: security, political instability, infrastructure, human capital and insurance. Considering that the company under study operates in the oil exploration and production industry, these findings cannot be generalised across other industries. Interestingly out of the five factors only insurance and political instability are directly related to Somaliland's unrecognised status. However, it can be argued that issues related to infrastructure, security and human capital factors have been intensified by Somaliland's lack of international non-recognition.

In terms of minimising the impact of the risks associated with the business environment of Somaliland both participants from Genel Energy imply that maintaining a close working relationship with the Somaliland government is the main avenue to improving issues such as security and infrastructure. Participant 1, for example suggests that the importance of future oil revenues to the government and Somaliland in general ensures that the government has as much of a stake in the success of Genel's operation in Somaliland as Genel itself. One of the main areas of co-operation between the government and Genel Energy is security. Genel's suspension of operations in September 2013 resulted in a number of high level discussions between the Somaliland government and Genel Energy and although neither participant has clarified the details of these meetings they have however both suggested that the outcome was an agreement to resume operations in mid 2014. However, according to Participant 3 (high ranking government official) discussions resulted in an agreement to establish a specially trained unit of Somaliland police charged with the protection of Genel staff, subcontractors and facilities. Participant 2, also suggests that Genel Energy is committed to the social development of areas in which it operates with programs underway prior to the suspension of activities medical centres, water wells and, most importantly, key infrastructure such as roads.

Government Perspective

No single interview stands alone but "It has meaning to the researcher only in terms of other interviews and observations" (Whyte, 1953). Accordingly the interview conducted with Participant 3, who is a high ranking official in the Somaliland government, is expected to provide a deeper insight into the factors that both influence the investment decisions of potential investors and those factors that either deter investment or negatively impacts on the operations of such firms operating in Somaliland. The same NVIVO coding process was utilised for this interview with the themes identified in coding categorised into the following categories: impact of international non-recognition on Somaliland's business environment, and factors that promote FDI in Somaliland.

The interview with Participant 3 corroborates business environment related factors identified by the Genel Energy interviewees (Participant 1 and Participant 2) as having a negative impact on investor operations such as infrastructure, security and insurance. However, data from the interview with Participant 3 introduces a number of other factors that were not considered a hindrance for Genel Energy but are likely to have an impact on the government's ability to improve the attractiveness of the business environment and/or the investment decisions of potential investors; these include access to international banking, misinformation, lack of foreign assistance, travel restrictions and perceived uncertainty over contract legalities. Participant 3 suggests that, although all of these factors pose significant barriers to foreign investment, the lack of foreign assistance that comes with being an unrecognised state has the biggest impact on the investment environment of the country. "Somaliland is a poor country, due to the meagre financial resources at its disposal the government is unable, without foreign assistance in the form of aid or loans, to invest in the physical infrastructure of the country such as roads and ports or in the schooling, training and development of its human capital" (Participant 3). This situation is further exacerbated by the lack of access to the international banking system which ensures that the government has no access to credit. This lack of access to international banks, according to Participant 3, also severely inhibits the growth opportunities of local firms who do not have access to the vital functions provided by international banks to facilitate international trade such as discounting or letters of credit (LOC). As no country in the world recognises Somaliland as a sovereign country, its passports are not accepted anywhere in the world apart from severely restricted access to South Sudan, Ethiopia, South Africa and Kenya, thus imposing travel restrictions on local businesses and trade. According to Participant 3 another major deterrent of FDI is the lumping together of Somaliland and Somalia which leads to the misinformed assumptions that Somaliland suffers from risk issues associated with Somalia. This situation is made worse by misinformation provided by officials from Somalia to potential investors in Somaliland to deter such investment. Surprisingly, although both Genel Energy interviewees (Participant 1 and Participant 2) suggested that the company did not have any concerns regarding the legality of its contracts with Somaliland, Participant 3 implies that for many firms who want to invest in Somaliland a key concern for them is the jurisdiction of contracts and its dispute resolution mechanisms.

From the interview with Participant 3 a number of factors were identified that both impact on the operations of firms operating in Somaliland and which can act as deterrents for potential investors. These factors fall into two categories first of which is common FDI deterrents such as poor infrastructure, perceived instability, insurance, and security. The second such category can be defined as factors related to Somaliland's international non-recognition that intensify the effect of common FDI deterrents; these include lack of foreign assistance, lack of access to the international banking system, travel restrictions and concerns over contractual agreements.

In terms of the factors that attract foreign investment to Somaliland Participant 3, as is illustrated in figure 10, agrees with the interviewees from Genel Energy on the importance of the role of natural resources, geographical location and trade openness as a motive to invest in Somaliland. According to Participant 3 the most important attribute of Somaliland for foreign investors is its endowment in natural resources which not only includes highly sought after hydrocarbons but also a wealth of metals such as copper and iron ore as well as wide variation of gemstones and minerals. As is the case with Participant 2, Participant 3 also discusses the importance of the geographical location of Somaliland particularly for production and export-orientated investment in saying, "Somaliland's geographical location is also very strategic and acts a gateway for landlocked countries in Africa that have either large markets or are oil producing such as Ethiopia and South Sudan while acting as bridge between Africa and Asia." In agreeing with Participant 2, in regards to the role of trade openness in attracting FDI to Somaliland, Participant 3, suggests that the primary goal of the Somaliland government is to gain international recognition and they believe that attracting foreign investment which facilitates integration into the global economy is a key strategy to achieving this goal. Attracting foreign investment would also boost productivity in the local economy as a result of the positive spill-overs of FDI. Accordingly the Somaliland government has implemented a very investor friendly tax regime to encourage and increase inflows of FDI. Participant 3 also discusses the importance of the newly implemented Somaliland Development Corporation (SDC) which is a UK registered company designed to empower economic investment in Somaliland. As Participant 3 explains "with the support of the UK government we have set up the Somaliland Development Corporation (SDC) which circumvents the problem of non-recognition by providing a transparent and enforceable means by which investors can invest in Somaliland". SDC is expected to act as an investment corporation that facilitates international investment in Somaliland, in other words, it acts as a conduit for international private investment and partners based in Somaliland with UK legal protection.

In summary, Participant 3 agrees with the participants from Genel Energy in that the most important driver of investment in Somaliland is its endowment in natural resources. The findings from Participant 3's interview also support Participant 2's assertions that the geographical location and trade openness of Somaliland plays an important role in attracting foreign investment to Somaliland. However, unlike the participants from Genel Energy, Participant 3 sees the development of the SDC as being an important promoter of FDI in that it provides added reassurance for potential investors as to the enforceability of contracts agreed through this vehicle

Discussion

In terms of the investment motives of companies investing in Somaliland such as Genel Energy, the findings suggest that the most important variable is the resource endowment of the host country. Considering that the company under study for this paper operates in the oil exploration and production industry it was expected that their main motive for investing in Somaliland would be for resource-seeking reasons, however, interview data from the government perspective also confirms that Somaliland's most attractive attribute is its endowment in natural resources. Accordingly, these findings support the conclusions reached by Asiedu (2006) and Morisset (2001) who both found natural resources to be the key driver of FDI in SSA. The findings also suggest that trade openness plays a key role in attracting FDI inflows to Somaliland. As Charkrabarti (2001) discusses a country's openness to trade is generally measured by the ratio of exports plus imports to GDP, however, these can also be seen by the policies adopted by governments such as tariffs and quotas on international trade and entry barriers of international firms (Dmirhan and Masca, 2008). Again, these findings agree with those of Asiedu (2006) and Morisset (2001) as well as host of other literature that suggests trade liberalisation has a positive impact on a country's investment environment such works include: Gastanaga et al (1998), Blancheton and Opara-Opinba (2010) and Onyeiwa and Shrestha (2004). In regards to trade openness, this study found that Genel as a resource seeking firm found the openness of trade in Somaliland, particularly investor friendly tax holidays and profit repatriation rights, as a motive to invest. These findings support Jordaan's (2004) assertion that resource-seeking TNCs favour investing in more open economies as imperfections that come with trade protection lead to higher transaction costs. According to Dunning (2000) locational attractions of alternative countries is determined by the immobile, natural or created endowments that firms can use jointly with their own competitive advantage. Accordingly, in support of this view the findings suggest that Genel's decision to invest in Somaliland was driven by natural resources endowments, an attractive trade policy and the strategic geographical location of Somaliland.

While the findings of this study agree with existing literature on the importance of natural resources and trade openness to attracting FDI the study also identified a new theme not discussed in the previous literature as being a motive for foreign investors in Somaliland. Both Genel Energy senior management and the Somaliland government felt that the under-explored nature of the county's oil and gas deposits was a key attraction for Genel. This is an interesting theme as it suggests that Somaliland's exclusion from the international investment framework, and thus limited interaction with large oil TNCs, has led to a limited exploration of very promising geology "which is analogous to that of Yemen, which is a prolific province, and with proven petroleum system by numerous oils seeps" (Particpant 1).

Impact of Non-recognition on FDI Inflows to Somaliland?

This study identified political instability, poor infrastructure, limited stock of human capital and insurance costs to be the key factors that negatively impact on the operations of investing firms in Somaliland and Somaliland's ability to attract FDI. These findings are consistent with the existing literature on the determinants of FDI to SSA, particularly works reviewed in this study such as Aseidu (2002), Aseidu (2006), Morisset (2001), Loree and Guisinger (1995), Bezuidenhout et al (2014), Naudé and Krugell (2003) and Noorbakhsh et al. (2001).

Table.2: Theoretical framework of the impact of non-recognition on the determinants of FDI

Common Deterrents of FDI to Somaliland and SSA	**Non-recognition related factors that impact on FDI inflows**		
	Uncertainty (*borders, contractual agreements, future status*)	**Inability to develop bilateral and multilateral relationships or receive foreign assistance.**	**Lack of access to international banks**
Political Instability	*Uncertainty over the future status of Somaliland exposes firms to risks that arise from changes in policy or policy makers, contract repudiation and changes in law.*	*Non-recognition means that Somaliland is not able to establish bilateral and multilateral relationships. Accordingly, firms cannot benefit from international trade agreements. The country also doesn't benefit from foreign assistance particularly in budget support.*	*Access to international credit facilities provides a facility for governments to borrow in order to bridge gaps in their budgets and provide basic services to population. These are not available to Somaliland*
Physical Infrastructure		*loans and grants from foreign and international organisations are not available for the development of infrastructure*	*Lack of credit facilities ensures government is unable to borrow in order to develop infrastructure*
Human Capital		*Foreign assistance to maintain schools and university not available*	*Lack of credit ensures government is unable to borrow to develop education and training sectors*
Insurance	*Non-recognition and uncertainty over sovereignty in Somaliland's case result in higher insurance costs as it is considered part of a failed state*	*Non-participation in international investment protection bodies severely limits Somaliland's ability to attract FDI*	*Many international banks provide products to insure against political risk. Due to non-recognition these facilities are not available to Somaliland*

The stated aim of this study was twofold: firstly, to understand how international non-recognition impacts on the ability of an unrecognised state to attract foreign investment, and secondly, how the international non-recognition of state impacts on potential investors. Accordingly, the findings of this study differ from the existing literature in that it identifies the existence of variables related to international non-recognition of a host country that intensifies the impact of the identified determinants of FDI on both the ability of the de facto state to increase FDI inflows and the operations of existing and potential investors (see figure 10). As figure 10 illustrates the three aspects of international non-recognition identified in this study as intensifying variables of common FDI determinants are: uncertainty (future status, contractual agreements and borders), inability to develop bilateral and multilateral relationships, and the lack of access to international banking system. The following section explains the relationship between these factors and general deterrents of FDI identified in this study.

Political instability

As is discussed by Lucas (1993), Azzimont and Sarte (2007), Asiedu (2006) and numerous other existing studies, because of risks associated with political instability, capital is unlikely to flow from developed economies to developing countries. To minimise such risks TNCs prefer to invest in locations that expose investments to less risk as a result of higher levels of political stability. As discussed by Asiedu (2006) one of the key deterrents of FDI to SSA is the high levels of political instability that most countries in the region suffer from. In Somaliland's case uncertainty over the unresolved nature of its sovereignty and the potential for change to the status quo raises the risk of sudden change of policy makers and/or otherwise favourable economic policies. There is also the potential for political change to lead to repudiation of contracts previously agreed thus increasing the risks of expropriation. Inability to develop bilateral and multilateral relationships also increases political risk in Somaliland for a number of reasons. Firstly, as Dicken (2011) says "TNCs look to their home-country government to provide it with diplomatic protection in hostile foreign environments". Participant 3 (government official) in our interview confirms that the presence of the TNCs home-government in some form is considered as a form of reassurance for foreign firms investing in the country, however "Somaliland does not have any official foreign embassies in its capital, for that reason many firms feel they don't have adequate protection from their government" (Participant 3). Secondly, many of the countries in SSA receive foreign assistance particularly in the form of budgetary assistance (World Bank, 2014); however, Somaliland as an unrecognised country does not benefit from such support. This leads to Somaliland struggling to provide basic services for its citizens and as Blanko and Grier (2009) argue poor social conditions often lead to dissatisfaction which can ultimately contribute to political instability and violence, increasing political risk for foreign TNCs operating in such a country.

Infrastructure

Mengistu (2009) suggests that the lack of adequate infrastructure has played major role in SSAs poor FDI performance over the years. He suggests that foreign investors are naturally cautious about investing where basic infrastructural requirements such as roads, ports, railways, telecommunication systems and basic utilities are inadequate. Somaliland's exclusion from the "states only club" means that it does not have access to foreign assistance either through bilateral or multilateral aid (provided by international bodies such as the United Nations, World Bank or the African Development Bank) that could be used to developed the country's dilapidated infrastructure. Furthermore, non-recognition and the consequent exclusion from the international banking system means Somaliland is unable to get credit facilities and loans for the improvement of its roads, airports, seaports and telecommunications infrastructure.

Human Capital

Works by Naudé and Krugell (2003) and Noorbakhsh et al. (2001) identified human capital measured in terms of literacy levels and secondary school enrolment plays a key role in FDI attraction in SSA. This study, although supporting these findings in terms of the impact of human capital on FDI inflows, finds that for de facto states like Somaliland issues related to lack of quality human capital stock is intensified by non-recognition. According to the World Bank (2014) "school enrolment is much lower in Somaliland than in all countries in the region". The government's meagre budget of $218 million for 2014/2015 (Somalilandgov.com) was its highest ever, highlighting the government's limitations in investing in the development of the country's human capital. International non-recognition, as is the case of physical infrastructure, means that Somaliland is not able to receive foreign assistance or borrow to invest in developing its human capital.

Insurance costs

As Gordan (2008) argues the public and private institutions that provide insurances to protect against shipping and political risk influence the flows of FDI to developing countries. In other words, countries in SSA who pose higher risks of political risks to investment will face higher insurance premiums which act as a deterrent of FDI inflows. Somaliland’s case is exacerbated by its non-recognition for a number of reasons. Firstly, the international community still sees Somaliland as part of Somalia instead of an independent sovereign state, ensuring that all of the risk issues endemic in Somalia such as piracy, terrorism and conflict are considered present also in Somaliland. Secondly, although Somaliland is a functional, stable and democratic country, it is seen by insurance institutions as being a region of a failed state. Even more importantly Somaliland’s non-participation in international investment programs such as the World Bank’s MIGA both further raises the cost of insurance and lack of cover for foreign investors.

Limitations and Areas of Further Research

In this research, the author faced a number of difficulties and problems. The first such difficulty was a mixture of time limitation and the very small number of international firms operating in Somaliland, as a result of these factors this study only investigated one company trading in Somaliland. This is a problem as this company only operates in the oil exploration and production industry, accordingly it is difficult to generalise the findings across all industries.

Secondly, because of the ongoing negotiations between Somaliland and Genel Energy some of the interviewees were reluctant to answer certain questions due to the sensitivity of their positions. Such questions regarded the level of cooperation between the entities on security. There were also difficulties in gaining answers as to the agreements between Genel and Somaliland on production sharing and the share of profits each can expect. This would have been interesting as it would have shed light on non-recognition impacts on Somaliland’s bargaining position in negotiations with Genel.

Finally, as this study is the first of its kind, there are many ways in which this research can be taken further. As discussed above a wider study involving a number of distinct industries in Somaliland or other countries with varying degrees of non-recognition can be conducted to test the findings of this study or develop it further. Also, this study can be further extended by testing how the factors identified in this study such as in-access to international banking systems or insurances costs impact on the FDI inflows to countries that are internationally recognised but suffer from such issues.

Practical recommendations:

Somaliland‘s non-recognition is a major hindrance to its ability to attract FDI. When the theories of globalisation and international economic integrations are considered it becomes apparent that FDI is the driving force behind the increased integration of nations. This situation highlights Somaliland’s difficult position: it needs FDI to increase integration in to the global economy and thus speed up the process of international recognition. However, without international recognition its ability to attract FDI is severely limited. The willingness, however, of resource-seeking TNCs such as Genel Energy to invest in Somaliland despite these limitations shows that some firms consider potential returns in Somaliland to outweigh the risks. The findings of this study confirm that, along with its abundant natural resources, Somaliland’s trade policies and advantageous geographical location are considered attractive attributes by resource-seeking TNCs. Accordingly; Somaliland should market these attributes to potential investors in order to increase its FDI inflows and consequent integration into the global economy thus making international recognition more likely.

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