



## Expansion of Multinational Corporations in de-facto States: The Case of Turkish Republic of Northern Cyprus

*Uluslararası Şirketlerin Tanınmayan Ülkelerde Yayılması: Kuzey Kıbrıs Türk Cumhuriyeti Örneği*

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### ABSTRACT

This article studies the dynamics of the existence and expansion of Multinational Corporations (MNCs) in the North Cyprus (Turkish Republic of Northern Cyprus, or the TRNC) within the context of embargoes and non-recognition in the international area. Therefore, we try to offer a better understanding on what mechanisms the MNCs use to expand their operations all over the world against extraordinary political situations. In this regard, the main research questions of this study are: ‘What are the dynamics of the existence and expansion of MNCs in the TRNC as an unrecognized state?’ and ‘How, and by using which tools and mechanisms do the MNCs exist, evolve, operate, and expand their capital in the TRNC market?’ Therefore, the mechanisms, tools, and processes used by the MNCs in their operating processes within the TRNC, and the dynamics and the forces behind investing in the TRNC despite the risks of illegality were investigated by conducting a field study. The field study was conducted through semi-structured in-depth interviews with nine participants who represented thirteen establishments of thirteen different MNCs operating in the TRNC. The findings of this research show that the MNCs use extraordinary tools and mechanisms in order to expand and legalize their investments in the TRNC.

### ÖZ

Bu makalede uluslararası şirketlerin (UŞ) Kuzey Kıbrıs Türk Cumhuriyeti’ndeki (KKTC) varlıkları ve genişlemeleri, ambargolar ve tanınmamışlık bağlamında araştırılmıştır. Bu yolla, uluslararası şirketlerin faaliyet alanlarını dünya çapındaki olağan dışı politik durumlar karşısında kullandıkları genişleme mekanizmalarının daha iyi anlaşılması sağlanacaktır. Bu bağlamda, çalışmamızın temel araştırma soruları şu şekildedir: “Tanınmayan bir devlet olan KKTC’de uluslararası şirketlerin var olmasının ve yayılmasının dinamikleri nelerdir?” ve “uluslararası şirketler KKTC pazarında var olma, gelişme, faaliyet gösterme ve sermayelerini genişletme süreçlerini ne şekilde, hangi araçlar ve mekanizmaları kullanarak yürütmektedirler?”. Buna istinaden, uluslararası şirketlerin KKTC’de faaliyet gösterdikleri süre içerisinde kullandıkları yöntemler, araçlar ve işlettikleri süreçlere ek olarak “yasa dışılık” riskine rağmen KKTC’de yatırım yapmalarının arkasındaki dinamikler ve itici güçler bir saha çalışması yürütülerek incelenmiştir. Bu saha çalışması, on üç farklı uluslararası şirketin KKTC’de faaliyet gösteren on üç kuruluşunun temsilcileri olan dokuz adet katılımcıdan oluşan örneklem ile gerçekleştirilen yarı yapılandırılmış derinlemesine mülakatların ışığında yürütülmüştür. Bu çalışmanın neticesinde elde edilen bulgular uluslararası şirketlerin KKTC’deki yatırımlarını alışılmadık araç ve yöntemler kullanarak genişlettikleri ve bu yolla yasal bir zemine oturttukları gözler önüne serilmektedir.

### 1. Introduction

The Turkish Republic of Northern Cyprus (TRNC) is a tiny de-facto state which is located in one-third of the Cyprus island in Eastern Mediterranean. Since the Turkish military intervention and the subsequent war in the island in 1974,

the island stands as partitioned into two (Turkish in the north versus Greek in the south). The northern part of the island, controlled by the Turkish Cypriots, is not recognized by any country in the world, except Turkey. In addition to

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△ Yazarlar bu çalışmanın tüm süreçlerinin araştırma ve yayın etiğine uygun olduğunu, etik kurallara ve bilimsel atf gösterme ilkelerine uyduğunu beyan etmiştir. Aksi bir durumda Akdeniz İİBF Dergisi sorumlu değildir.

this, there are economic embargoes<sup>1</sup> imposed on the TRNC. Therefore, naturally the international business activities in the TRNC have been quite limited.

Nevertheless, according to the U.S. Department of State data (2015 & 2019) there is an increase in the investments of the foreign companies and offshore companies in the TRNC market. There were 340 foreign companies and 333 offshore companies operating in the TRNC by June 2015 excluding the companies that are based in Turkey (U.S. Department of State, 2015). The number of these companies in the TRNC market has increased to 418 foreign companies and 456 offshore companies by July 2019, (U.S. Department of State, 2019). Therefore, the increase in four years consists of 78 foreign companies and 123 offshore companies, which are in total 201 companies, that are related with the international capital, invested in the TRNC market and started to operate here in the last four years. These foreign companies are the Multinational Corporations (MNCs) that operate in the TRNC market. On the other hand, the aforementioned offshore companies are the domestic companies of the TRNC that operate their businesses with the MNCs in the TRNC market. Moreover, these MNCs are the companies that are based in states that do not recognize the TRNC. Thus, it is possible to say that, since legally there is no state as 'the TRNC' from the perspective of these states, then the 'legality' of the investments of these companies in the TRNC is also in question.

In this regard, this article is an attempt to study the dynamics of the existence and expansion of MNC activities in the TRNC, an unrecognized de-facto state. Following this topic, research questions of this study are as follows:

- What are the dynamics of the existence and expansion of international businesses in the forms of MNCs in the TRNC?
- How, and by using which tools and mechanisms do the MNCs exist, evolve, operate, and expand in the TRNC market?
- How does the domestic market of the TRNC take shape with respect to the investments of the MNCs?

If one considers the MNCs as the representatives of international capital today, then one may argue that the existence and expansion of them in the TRNC would involve some extraordinary processes. The MNCs need to use extraordinary tools and mechanisms in order to legalize their investments in the TRNC. Moreover, in some cases, these companies even need to change the structures of their own investments in the TRNC in order to get around the obstacles on their expansion and operations and the difficulties that they face to this end, which were caused by the contexts of non-recognition of the TRNC and the embargoes imposed on the TRNC.

Therefore, the main objective of this study is to investigate and reveal both legal or extra-legal mechanisms and the tools that are used by the MNCs in order to operate and expand their businesses in the TRNC. This study is important in order to understand how the MNCs behave in order to legalize their investments in the quasi-legal states,

and how the businesses and their capital keep up with the extraordinary political situations such as non-recognition, and how they are getting around the juridical issues in the international arena related with the existence of their investments in the states that are considered as 'quasi-legal', such as the TRNC.

The existing literature does not present adequate information when it comes to how the MNCs exist and expand in de-facto states. Thus, this study will conduct a case study to concentrate on this issue in order to analyse the tools and mechanisms used by the MNCs in order to evolve, operate, and expand their businesses in the TRNC market. This case study is analysed by conducting a field study that consists of interviews that provide qualitative information about the issues related with the investments of the MNCs in the TRNC market.

The next part of the article is going to talk about the expansion methods, or foreign market entry modes of MNCs, and the reasons behind using different market entry modes for expansion. Then, the internal and political and economic structures of the TRNC will be presented in order to highlight its characteristics as a market for MNCs. The following section will present the research method and the analysis of the field study. Finally, some conclusions on the findings and analyses of the study are going to be made.

## **2. Business Expansion Methods and Their Viability in the TRNC Market**

In this section, we will first talk about the MNCs' methods for expansion into foreign markets. Then, we will explain the specific conditions of the TRNC market by emphasizing its dubious legality in terms of its relations with the MNCs.

### **2.1 Expansion Strategies and Foreign Market Entry Modes of MNCs**

According to Ghauri and Cateora (2010) the driving force of the MNCs to expand towards the international markets is the growth of these firms. However, they assert that the reasons behind the expansion of the MNCs, towards a particular market, and which entry mode to be used in this process, consist of a combination of the company objectives and the market characteristics of the targeted economic territory. The classical model of MNC internationalization developed by Dunning (1993) includes four different categories of MNC motives. These categories are market seeking, resource seeking, efficiency seeking and strategic resource seeking motives. In a resource seeking FDI, firms try to enter into countries to get access to raw materials or other crucial inputs that can provide cost reduction and lower operation costs, like cheap labour. In market seeking FDI, firms look for a considerable market for its products/offers. In efficiency seeking FDI, firms want to enter countries/markets where they expect benefits by achieving efficiency. Often those benefits come from economies of scale and scope, but also risk diversification. In the strategic asset seeking FDI, the aim is to acquire a new technological base (Dunning 1993). Therefore, it is possible to say that the main objectives of the MNCs are different from each other because they are different in size,

<sup>1</sup> For an explanation for the reasons behind using the term 'embargo', please see '1.2. The Economic Indicators and Assessment on the TRNC Economy with Respect to MNCs'.

sector, competitiveness and purposes, thus their needs are differing from the each other, and these different objectives can be reached by expanding into different territories in different forms.

Hill & Hult (2018) argue that there are three main decisions to be made by the companies before choosing the market entry mode in order to expand towards a particular economic territory in the international market. These decisions are related with the questions of ‘... which foreign markets to enter, when to enter them, and on what scale’ (Hill & Hult, 2018, p. 358). The existing risky situations for the future of the investment that are planned to be made by the firms in a particular economic territory affect not only the likelihood of MNC investment, but also the scale and the shape of this investment.

Regarding the first question, which is the question of ‘Which foreign markets to enter?’, Hill & Hult (2018) argue that this question must be addressed by the investor through assessing the potential of its investment in this particular economic territory for its relative long-term growth and profit in contrast to its competitors in the sector. The investment decision is made based on an assessment of the size of the market, purchasing power of the consumers in that market and the economic growth potential (Wadhwa & Reddy 2011; Hill & Hult 2018).

When it comes to the second question, which is related with the timing of entry to the foreign market, it has been argued that if a company is the first foreign company to enter a particular economic territory in a particular sector, or a product group, this provides this company what is called as the ‘first-mover advantage’ (Ghauri & Cateora, 2010; Hill & Hult, 2018). Being the first mover of a particular sector, or a product, gives the investor company some advantages such as an ability to create a well-known brand before its competitors enter this particular market, or gaining more experience about the inner dynamics of this particular market before its competitors enter here, or a cost advantage depending on the ability of the first-mover company on cutting prices below the prices of the products of the later entrant within this particular market (Ghauri & Cateora, 2010, p.267; Hill & Hult, 2018, p. 360).

The third question before choosing the foreign market entry mode for the companies is related with the decision on the scale of the entry to be made in that particular market. Regarding this issue, Hill & Hult (2018) argue that both of the small-scale and the large-scale entries have their own advantages and disadvantages for the companies that are entering to a particular market. While small-scale entry reduces the risks of huge losses of capital in contrast to a large-scale entry, on the other hand large-scale entry increases the chance of capturing the first-mover advantage (Hill & Hult, 2018, pp. 362-363). Therefore, when entering a new market, the companies must achieve the balance between the small-scaled entry and the large-scaled entry in accordance with their objectives and the internal structures of that particular market.

Finally, when the decisions have been made on where, when, and in what scale the foreign market entry will take its place, it is time for the MNCs, to choose which foreign market entry mode is to be used in order to expand in the market of a particular economic territory. We present and

examine five different kinds of foreign market entry modes within this study: exporting, licensing, franchising, joint ventures, and the wholly owned subsidiaries.

Exporting is the most common foreign market entry mode that is used by the manufacturing firms (Cullen & Parboteeah, 2010; Hollensen, 2007). ‘Exporting presents a low level of commitment and as the required resource commitments are minimal, the risk of bearing a potential loss is minimal as well’, because exporting does not involve FDI (Katsioloudes & Hadjidakis, 2007, p. 261). A distributorship agreement between the exporting company and the importing company may lessen the disadvantages in some circumstances. Since the distributors are considered as the ‘exclusive representatives’ of the exporting companies in a particular territory (Hollensen, 2007), this article is going to be concerned with the ‘distributors’ of the MNCs in the TRNC market while analysing ‘exporting’ as a foreign market entry mode.

Licensing is established through a licensing agreement between two companies, which are the ‘licensee’ and the ‘licensor’ (Cullen & Parboteeah, 2010, p. 249). ‘Through licensing, a firm (licensor) grants a foreign entity (licensee) some type of intangible rights, which could be the rights to a process, a patent, a program, a trademark, a copyright, or expertise. In essence, the licensee is buying the assets of another firm in the form of know-how or R&D (Ajami et al., 2006, p.25). An advantage of licencing as a foreign market entry mode is that the commitment of the licensee to the licensor is being assured by the ‘licensing agreement’. Moreover, Hill & Hult (2018) assert that ‘a primary advantage of licensing is that the firm does not have to bear the development costs and risks associated with opening a foreign market’ (p. 366) as the licensee bears most of the capital that is necessary for the overseas operation.

Franchising is one of the most well-known foreign market entry modes. It is a special kind of licensing in which the franchiser sells intangible property (normally a trademark) to the franchisee and also the franchisee agrees to follow strict rules on how it does business. Like licensing, the franchiser typically receives a royalty payment from the franchisee. It is more common in the service sector (Hill & Hult, 2018). In the franchising businesses, the franchisee is not only benefiting from the perceived value of the brand of franchisor, but also being assisted by the franchisor in order to increase the efficiency of their investments. On the other hand, franchising also provides the franchisor some advantages as well, such as ‘rapid entry and expansion in the foreign market without any major risk assumption or capital investment requirements.’ (Katsioloudes & Hadjidakis, 2007, p. 250). Instead, the ‘risks’ and ‘cost of capital’ of establishing a franchising business is expected to be covered by the franchisee. ‘Master franchising’, a special type of franchising, ‘is based on granting the foreign franchisee exclusive territorial right to a particular region or country. The master franchisee in the foreign country then assumes the role of franchisor’ (Katsioloudes & Hadjidakis, 2007, p. 250).

Another form of foreign market entry is ‘joint-ventures’, which involves establishing a company that is jointly owned by two or more independent companies (Hill & Hult 2018). Therefore, MNCs can expand in a foreign market by

establishing a joint venture with a local company in this particular territory.

'Wholly owned subsidiary' is another foreign market entry mode in which the foreign firm, or the MNC owns the whole stocks of the established company located in a particular territory (Ajami et al., 2006). In order to own a wholly owned subsidiary in the market of a particular economic territory, an MNC can set up an investment from scratch (greenfield investment), or it can acquire another local company that is already established in this market.

## 2.2 The Economic Indicators and Assessment on the TRNC Economy with Respect to MNCs

As it has been presented in the previous section, the economic indicators and the economic structures are important in order to identify the underlying reasons behind the MNC expansion in different economic territories. Therefore, in order to have a better understanding on how MNCs exist and expand in the TRNC, some economic indicators and structures of the TRNC market will be presented.

To begin with, Cyprus is the third largest island in the Mediterranean Sea, and the largest island in the Eastern Mediterranean Sea, and it is located in the midst of the continents of Asia, Africa, and Europe. Thus, it is possible to say that, since it is located where trade routes intersect, the TRNC is situated in a geographically valuable place for the international trade (Leigh & Vukovic, 2011, p.59). However, there is not significant number of people in the TRNC. The total population of the TRNC was 335,455 in 2016 and 93,292 of this population were consisting of students who were studying in the TRNC universities. The total working age population of the TRNC in 2018 was 132,818. The unemployment rate was approximately 5.5% (T.C. Lefkoşa Büyükelçiliği, 2018). Since the MNCs of manufacturing industry need huge masses of population as labour, not only the unemployed population of the TRNC, but also the total population of the TRNC is not sufficient to provide labour force for the 'efficiency seeking' manufacturing industry of the MNCs.

Moreover, when it comes to the GDP per capita of the TRNC, it was \$14,942 by the end of 2018 (T.C. Lefkoşa Büyükelçiliği, 2018).<sup>2</sup> In addition to this, the average minimum monthly wage in the TRNC was \$600 in 2018 (U.S. Department of State, 2018). Thus, it could be argued that, since the industrial manufacturing processes of international capital necessitates lower wages within the invested economic territories, the TRNC is not offering a good profit opportunity for the manufacturing MNCs due to its relatively high minimum-wage.

Another problem related to the TRNC market is related its political situation. TRNC is considered a 'de-facto state'. A de-facto state is an internationally unrecognized state, i.e. a state that is denied external sovereignty. As stated by Caspersen (2012), de-facto states also meet the following conditions: they have de facto control of their territory,

which is actually claimed by another state ('parent state'); they seek to build state institutions and demonstrate their own legitimacy; and they have declared or shown aspiration for independence.

The problem with de-facto states is that, compared to legally recognized states, they have harder time in their economic relations with other states and foreign companies. Recognition allows states to get into international agreements and contracts and any other recognized international legal frameworks, which makes it easier to acquire foreign investment (Buzard et al., 2017). De-facto states suffer from what Pegg (1998, p. 43) has called, 'the economic cost of non-recognition', because foreign firms are distrustful when it comes to investing in a de-facto state as legal contracts might not be internationally binding there. Investors may also be afraid of offending the parent state, for fear of being banned from having economic relations with its typically larger market. Unrecognized status also increases cost of living in de-facto states as local companies cannot import goods directly and international investors would also be discouraged by the lack of international insurance and other forms of protection for investments (Caspersen, 2012). Exports from de-facto states are similarly limited, as they usually face restrictive measures in international markets. Further problems are created by the transportation complications, because direct travel may not be possible from and to de-facto states. As a result, de-facto states are known to receive little FDI (Hoch and Rudincová, 2015). All these create dependency of de-facto states on their 'patron states', i.e. the states that recognize and support them.

In 1983, nine years after the partition of the island, the Turkish Cypriots declared their self-determination and established the TRNC. However, Turkey is the only state that officially recognized the TRNC. As a reaction, the UN started an embargo on the TRNC by declaring the 'UN Security Council Resolution 541' which states that the declaration of the TRNC was incompatible with the 1960 Treaty about the establishment of Republic of Cyprus, as well as the 1960 Treaty of Guarantee. Thus, the attempt to create TRNC was declared invalid. As a consequence, the TRNC is an unrecognized state in the world<sup>3</sup>. Furthermore, while there are political and economic embargoes imposed on the TRNC by the states and international organizations such as the EU which do not recognize it since 1983, the Republic of Cyprus (RoC) in the South is a member state of the EU and it pursues its existence as a recognized state in the international area.

Moreover, there are also some economic embargoes that originated and depended on the political non-recognition of the TRNC. These economic embargoes not only cause an isolation of the TRNC from the international markets, but also undermine the industrial development of the TRNC (Kanol & Köprülü, 2017). The international institutions like Universal Postal Union, the International Civil Aviation Organization and the International Air Transport

<sup>2</sup> The average GDP per capita of East Asia and Pacific Countries was \$10,367, Latin America and Caribbean Countries was \$9,271, and Middle East and North Africa Countries was \$7,373 in 2017. The GDP per capita in some countries, where huge industrial manufacturing plants of MNCs prevail are \$8,827 in China, \$3,864 in Indonesia, \$6,595 in Thailand in 2017 (The World Bank, 2019).

<sup>3</sup> Although the 'UN Security Council Resolution 541' declaration does not mean to an embargo on the TRNC as *de jure*, this study refers this situation as 'embargo', depending on the difficulties that the TRNC society is having as outcomes of this declaration as *de facto*. These difficulties were provided in '1.2. The Economic Indicators and Assessment on the TRNC Economy with Respect to MNCs' section.

Association refuse to deal with the TRNC. (Pegg, 1998, p. 4). Therefore, some processes and activities related with international trade, such as transportation and communication are getting harder to be accomplished. For example, if one attempts to send or ship anything (i.e. a good, a payment, a document, or a letter) from the TRNC to any state that does not officially recognize the TRNC, he/she must identify his/her address as 'Mersin10/Turkey', which is a kind of masked address for the TRNC which makes it look like an address in Mersin, a city of Turkey. In this process, the item to be shipped from/to the TRNC to anywhere in the world must firstly arrive to Turkey, then depart from Turkey in order to reach the recipient address.

Due to its non-recognition, there are no direct flights or navigation routes from any other state to the TRNC, except Turkey. This significantly increases both the costs and the inconvenience of traveling to Northern Cyprus (Pegg, 1998). While this situation directly undermines the tourism sector in the TRNC, the less the number of tourists visiting the TRNC means less buoyant of commerce within this economic territory, thus the whole economic activity gets undermined.

The economic embargo was greatly exacerbated with the ruling of the European Court of Justice (ECJ) in 1994, which deemed the food certificates issued by Northern Cyprus as unacceptable for the EU<sup>4</sup>. As a result, many production industries of the TRNC have been undermined. Just three years after this ECJ ruling, a domestic company of the TRNC, named 'Sanayi Holding', went bankrupt, closed down its 57 manufacturing plants and laid off hundreds of workers (Gürsel, 2019, June 11). Therefore, it is possible to say that not only the agricultural industry, but also the production industries of the TRNC were banned from the international markets due to embargoes.

Due to all these above mentioned problems caused by its de-facto status, the TRNC economy has remained quite weak. TRNC remains completely dependent on its patron state, Turkey, for its economic survival. Turkey provides substantial amount of financial aid every year to the TRNC to compensate for its economic disadvantages (Caspersen, 2012; Bozkurt, 2014; Bryant and Hatay, 2015). Therefore, the TRNC is a typical de-facto state in economic sense, and thus, naturally it is not a favourite destination for FDI.

With the efforts of the seventh UN Secretary-General of the UN Kofi Annan, in order to solve the Cyprus Conflict by a reunification of the island under a federal state solution, known as the 'Annan Plan', was offered to the TRNC and the RoC by the United Nations. Thus, the Annan Plan was voted through two separate and simultaneous referenda at both of these states on the 24th of April 2004 (Sözen & Özersay, 2007). However, the Annan Plan could not be implemented, as the Plan was rejected by the Greek Cypriots with 76% of the votes although it was approved by the 65% of the Turkish Cypriots.

With the rejection of the Annan Plan, the TRNC could not succeed to end its economic and political isolation. On the other hand, the RoC became a full member of the EU in 2004 and began to reap its benefits (Gökçekuş, 2009).

However, after the Annan Plan referenda, the TRNC started to develop more direct relationships with international bodies and institutions and also experienced increasing penetration of international capital (Bryant 2015). Also, the 2004 Green Line Regulation allowed some limited trade (mostly fresh produce and raw materials) between the two sides of Cyprus. Yet when considered together with the obstacles placed against the industrial development of the TRNC, such as non-recognition, this penetration of the international capital meant that 'Turkish Cypriots have been incorporated into the global economy as consumers rather than producers' (Bryant, 2015, para. 10). Therefore, one may argue that, while the non-recognition of the TRNC undermines the economic development of the TRNC, it does not completely prevent the MNCs pursue their expansion and profit-making in the territories of the TRNC.

However, another important issue about the internal political and economic structures of the TRNC is related with the private property ownership. According to a report of the US Department of State, 'Investors are advised to consider the risks associated with investing in immovable property [in the TRNC]' (US Department of State, 2015, p. 15). The underlying reason behind this situation is that the ownership of private property in the TRNC, especially the lands that were owned by the Greek Cypriots before the partition of the island, are still a matter of conflict today. Although the Immovable Property Commission (IPC) is established in 2005 to handle the disputes on private property ownership in the territories of the TRNC, according to the IPC (Immovable Property Commission, 2020), there are hundreds of applications made by the Greek Cypriots and not all of the applications are concluded with a final solution. Thus, it is possible to say that the security of the property ownership in the TRNC is carrying some particular risks depending on the European Court of Human Rights (the ECHR) ruling about the property disputes at the TRNC. The risks on the property ownership decrease the attractiveness of the TRNC in terms of FDI.

On the other hand, there are some governmental incentives (e.g., the tax allowances, investment allowances, and some exemptions from the Value Added Tax) that are given by the TRNC state regardless of whether an investor is local or foreign (TRNC State Planning Organization, 2018). Therefore, it is possible to say that the de-facto TRNC state is aiming to encourage both the domestic and international capital to invest in the territories of the TRNC. However, although the state authorities of the TRNC are endeavouring to increase the export-oriented manufacturing investments in the TRNC, exports to countries other than Turkey is highly problematic due to international embargoes. Therefore, the export-oriented investments and production get undermined in the TRNC.

Based on the information given above, it is hard to claim that the TRNC is an attractive location for international capital. However, we still see increasing MNC activity in the TRNC. Why? First of all, as mentioned before, every company has different objectives, needs, and strategies. Therefore, it can be argued that, for the ones that are in search of a territory to establish a production facility, the

<sup>4</sup> Although the ECJ ruling in 1994 does not refer an 'embargo' as *de jure*, it could be argued that the consequences of the ECJ ruling mean an 'embargo' on the TRNC goods as *de facto*.

TRNC cannot offer good opportunities, because: (1) the wages are relatively high in the TRNC, (2) the total population and working population in the TRNC are not creating huge masses of labour power that is necessary for the giant production processes of the international capital (3) the phenomenon of non-recognition is aggravating the transportation and communication issues between the TRNC and the world market (excluding Turkey), (4) the economic sanctions imposed on the TRNC by the EU undermine the competitiveness of the businesses that operate in the TRNC depending on their inability to sell their products to the EU markets, (5) the property ownership issues in the TRNC and the ECHR rulings on this issue increase the risks related to the ownership of property in the TRNC for the businesses.

However, it can be argued that, for some MNCs which are in the consumption sector that produce fast moving consumer goods, the TRNC market may be feasible in the long-run to a certain extent as long as their products get consumed domestically, and as long as it is cheaper establishing a small-scale production unit than exporting their goods to the TRNC. This kind of establishments could be practically succeeded by the MNC through specific foreign market entry modes such as joint ventures and wholly owned subsidiaries.

When it comes to the resource-seeking MNCs that operate in the production industry which are seeking to get access to the raw materials, it is possible to say that, regardless of whether the TRNC has a resource-rich geography or not, depending on the problems that are arising from the issues of non-recognition of the TRNC and the economic embargoes imposed on the TRNC, the extraction processes of the raw materials with the production process of the MNCs will be undermined, in the senses of lack of communication and high costs of transportation. Therefore, it is possible to claim that the TRNC market is not a feasible location for this kind of investments of the MNCs, as long as they have some other objectives such as, for example using their investments in the TRNC market as a reserve to be used actively in the future. However, in order to do this, the property ownership of the MNCs in the TRNC must be guaranteed in some certain way and by some certain authorities.

However, it could be argued that since the GDP per capita, the minimum wages, and therefore the purchasing power are high enough in the TRNC to be used as a market by the MNCs, the TRNC can be a feasible location for the 'market-seeking' investments of the MNCs. Although the communication and transportation processes between the TRNC and the rest of the world are difficult to achieve, these difficulties could be overcome in such circumstances depending on the following reasons; (1) the process of shipping goods from a certain country to the TRNC is easier than shipping goods from the TRNC to that country, and (2) since the purchasing power is high, the costs of transportation could be reduced relatively by increasing the prices of the goods in the TRNC market. In addition to the latter reason, it must be noted that depending on the non-recognition and the economic embargoes, the domestic market of the TRNC is already unable to reach these goods in relatively low costs, neither by producing these goods, nor by importing them from somewhere else. Therefore, it

is possible to say that, despite the difficulties in the communication and transportation processes, the TRNC market is still feasible for such investments of the MNCs. When it comes to the choice of the foreign market entry modes for this kind of investment, it could be argued that exporting, licencing, and to some extent joint ventures in the form of licencing, could be practical for the MNCs in order to expand in the TRNC market. However, it is quite an important issue here that the inner structures, mechanisms, and the dynamics of these kinds of foreign market entry modes in the TRNC are going to be different from what they actually are in the territories that do not have such political and economic conditions like non-recognition and economic embargoes.

Finally, when it comes to the MNCs that operate in the service sector, it is possible to say that most of these MNCs can also be considered as market-seeking companies and depending on the internal economic indicators in the TRNC, such as the high purchasing power, the TRNC market is feasible for the investments of these companies as much as the other market-seeking companies from different sectors. However, depending on the structural differences of the companies in the service sector compared to the ones in the production industries, these companies need to invest in the TRNC market through different foreign market entry modes such as franchising, but establishing joint ventures can also be practical for them in some circumstances. Yet, in addition to these, if an MNC decides to establish a joint venture in the TRNC market, then this company must take into consideration the continuing property ownership disputes in the TRNC and the possible risks that will result from these disputes. As a result, the inner structures, mechanisms, processes, and the dynamics of the foreign market entry modes, which are used by the MNCs in order to invest in the TRNC market, will also be different from the ones that do not have issues such as non-recognition and economic embargoes. In this sense, these inner structures, mechanisms, processes and the dynamics which are being used by the MNCs in order to pursue their expansion in TRNC are worth further investigation.

### **3. An Analysis of the MNC Activities in the TRNC Market**

As mentioned, there has been an increase in the investments of the MNCs in the TRNC market. Due to the non-recognition of the TRNC in international relations and the political-economic embargoes imposed, it has been argued that the tools and mechanisms that are used by MNCs and the dynamics of the foreign investments in the TRNC are expected to be different from what they actually are in the territories that do not have those conditions. Therefore, in this section, our goal is to investigate and analyse these different structures, tools, mechanisms and the inner dynamics of the investments of the MNCs in the TRNC market.

#### **3.1. Research Method**

Primarily, the research was conducted through semi-structured in-depth interviews with representatives of thirteen MNC establishments in the TRNC. Depending on their knowledge and responsibilities about the companies' historical backgrounds, operations and organic structures, these representatives are purposively selected out of either

the executive managers of these establishments in the TRNC such as wholly owned subsidiaries, or owners or executive managers of the domestic companies that are operating businesses of these MNCs in the TRNC through bounding themselves to these MNCs by specific written and official agreements such as distributorship agreements, franchising agreements, licensing agreements, or joint venture agreements. However, there are some domestic groups of companies in the TRNC that do these kinds of businesses with multiple MNCs. Therefore, we have

interviewed four executive managers and one owner in four domestic groups of companies that do mutual businesses with nine MNCs, one owner and two executive managers of domestic companies that do business with three MNCs, and one executive manager of a wholly owned subsidiary of an MNC. In brief, we had nine interviewees in total who belong to eight companies that could be considered associated with thirteen MNCs.<sup>5</sup> The Table-1 presents the sample of the semi-structured in-depth interviews:

**Table 1.** List of the interviewees

MNC Code	Market Entry Mode	The Local Company Code	Interviewee Name/Position
MNC 1	Exporting /Distributorship	Company A	Haydar / Executive Manager
MNC 2	Exporting /Distributorship	Company B	Haşmet / Executive Manager
MNC 3	Exporting /Distributorship	Company B	Haşmet / Executive Manager
MNC 4	Exporting /Distributorship	Company C	Mithat / Owner, Shareholder
MNC 5	Exporting /Distributorship	Company C	Mithat / Owner, Shareholder
MNC 6	Franchising	Company A	Kenan / Executive Manager
MNC 7	Franchising	Company D	Yüksel / Owner, Shareholder
MNC 8	Franchising	Company E	Tamer / Executive Manager
MNC 9	Franchising	Company E	Tamer / Executive Manager
MNC 10	Franchising	Company E	Tamer / Executive Manager
MNC 11	Licensing	Company F	Haluk / Executive Manager
MNC 12	Licensing & Joint Venture	Company G	Biröl / Executive Manager
MNC 13	Wholly Owned Subsidiary	No Local Company (Named as Company H)	Faik / Executive Manager

*Note.* In order to ensure confidentiality, the names of all of the MNCs have been hidden and given a 'code number' with the term 'MNC'. The same technique has been applied on the existent investments in the TRNC, for the same reason, their codes represented as numeric codes with the term 'Company'. The interviewees' names are also changed in order to ensure confidentiality. Also, for protecting their identities, genders of all of the interviewees have been represented as 'male' regardless of their gender.

As it can be seen in Table-1, each of the interviews represents a different MNC. The number of the interviews in respect to the market entry modes follows as; five exporting/distributorship, five franchising, one licensing, one joint venture with a licensing, and one wholly owned subsidiary. The reason why we have more cases of certain entry modes with respect to other modes is related to the availability of these specific kinds of market entry modes in the TRNC market; thus, they are represented proportionally in this study. However, the limitation on the multiplicity of the companies in the sample set is due to the unwillingness of some companies to participate in this study.

The interview questions consist of seventeen core questions and twenty sub-questions that are related with the core questions. In other words, they are focused on finding out how the related investments were established under the quasi-legal conditions of the TRNC, the specific obstacles faced not only in the establishment but also in the growth and operational phases of these firms, and also the other possible problems or opportunities faced by these firms. The goal was to discover what different processes that the foreign firms and their local collaborators had to go through while making and managing FDI in the TRNC, as an unrecognized de-facto state, compared to ordinary legally recognized states. The interview questions can be categorized under the following topics: the story of the establishment phase of the MNC or the domestic companies that represent the MNCs in the TRNC market and the investment processes of the MNCs; the decision-making

process of the market entry and the reasons behind investing in the TRNC market; the governmental policies of the TRNC state on foreign investments, and the effectiveness of the governmental incentives for foreign investments; how and in what ways the structures and operation processes of the investments of the MNCs have been changed in respect to the context of non-recognition of the TRNC and political and economic embargoes related with the TRNC; the kind of organic links that exist between the local companies in the TRNC that do businesses for the MNCs and the MNCs themselves, and the kind of legal/illegal agreements or partnerships involved in this way; which tools and mechanisms the establishments of the MNCs use to buy the goods abroad that are necessary for their businesses in the TRNC; the position of the establishments/investments of the MNCs in the TRNC market, and the market share of them in the TRNC; how they (either the domestic companies that do mutual businesses with the MNCs, or the international companies, which are the subsidiaries of the MNCs, themselves) see the sector that they are doing businesses in the TRNC market; and lastly (this is applicable only for the companies that have production facilities in the TRNC), whether they exploit the domestic natural resources of the TRNC. The interviews were done between the time period of 7th of May 2018 and 31th of December 2018.

At the end of this study, some general conclusions about the structures, processes, tools and mechanisms of these investments of MNCs within the TRNC market as a market

<sup>5</sup> The interviews in this study have been applied under the permission of the Middle East Technical University (Ankara) - Human Subjects Ethics Committee.



of an unrecognized state, will be presented. The variations of the results and findings, thus the conclusions, are limited to the information that were gathered from the participants of the field study.

### 3.2. Existence and Expansion of International Businesses in the TRNC Market

In this part, the structures and the dynamics of the existence and expansion of MNCs in the TRNC are analysed. The interviews conducted have provided us important information on the tools and mechanisms that are used by the MNCs in the TRNC market. We will interpret this information in the light of the information provided in the previous sections. However, before beginning the analysis, it must be noted that as TRNC is recognized by Turkey, so the MNCs that have Turkey as their home country were not included in this study. This study analyses only the MNCs that are based on the states that do not officially recognize the TRNC.

#### 3.2.1. Exporting

The most common way to accomplish exporting as a foreign market entry mode for the MNCs in the TRNC market is to set up a kind of a 'distributorship agreement' between the particular MNC and a local company of the TRNC. Three domestic companies that import goods from the five MNCs were selected out of the distributors of these MNCs. While 'MNC1' is an industrial production company that produces 'fast-moving consumer goods', the 'MNC2' and 'MNC3' are two different industrial production companies, with different brands, in the 'automotive sector', 'MNC4' is another industrial company that produces 'professional cleaning products' and 'MNC5' is an industrial production company which is producing 'commercial laundry equipment'. All of these MNCs are operating worldwide, and all of them are defining themselves as 'one of the leading companies' in their sectors and they are continuously expanding in different markets in the world.

When it comes to the local firms, it is possible to say that the establishment dates of some of the local firms can be traced back to the dates before the partition of the island in 1974. However, most of the firms that do distributorship for these MNCs in the TRNC market are established after 1983. All the three local companies (Company A', the 'Company B', and the 'Company C') are established by the domestic businessmen of the TRNC and none of them has any foreign shareholders. However, some of the distributorship agreements between these local companies and the MNCs can be traced back to the time period between 1974 and 1983, during the Turkish Federated State of Cyprus (*Kıbrıs Türk Federe Devleti-KTFD*) which was the state on Northern Cyprus declared temporarily in 1975 and existed until 1983.<sup>6</sup> It was not recognized by the international community either. Thus, the centre of Company A was existing in an unrecognized state when it signed a distributorship agreement with MNC1 and started its operations.

The interviewee Haydar said that their company, Company A, is written as the distributor company of MNC1 in the TRNC, and the TRNC is described as a state in the agreement. However, he didn't give any information about

how, or in what ways, this agreement is being legalized in the home country of the MNC. When we checked the internet site of MNC1, we could find Company A as a distributor of MNC1 in the TRNC. Haydar noted that Company A is doing its business operations with a full responsibility and liability as the only distributor of MNC1 in the TRNC. Hence, all of the standards such as working hours, trade routes within the TRNC, annual business plans, and education of workers are being planned and operated mutually by MNC1 and Company A.

The Company B had signed its distributorship agreements with MNC2 and MNC3 after the establishment of the TRNC. Haşmet, the interviewee in Company B, did not give any information about the decision-making process of Company B, or of MNC2 and MNC3 on investing in the TRNC. Both MNC2 and MNC3 had some other local companies of the TRNC as their distributors within the TRNC market before Company B established a distributorship agreement with them. Haşmet noted that Company B was doing businesses in other sectors as a representative of other MNCs in the form of distributorship before its agreements with MNC2 and MNC3. Haşmet did not give any information about how the distributorship agreements of Company B with MNC2 and MNC3 are legalized in the home countries of MNC2 and MNC3, but he stated that Company B, as a distributor of MNC2 and MNC3, is operating with a full responsibility and liability for their products. The Company B is providing all the after-sale services in the TRNC and all of the replacement parts for the automobiles that they sell in their services are original products of MNC2 and MNC3. When we checked the web site of MNC2 and MNC3, we could not find any information stating that Company B is the official distributor of MNC2 or MNC3. Therefore, one may argue that depending on these situations, the legality of each of the distributorship agreements between Company B and MNC2, as well as MNC3, are in question in the international area. On the other hand, Haşmet stated that Company B provides and guarantee services for the products that are bought from other foreign dealers of both MNC2 and MNC3 and MNC2 and MNC3 also provide and guarantee services in international area for the products bought from Company B as a distributor of these companies. Thus, in practice MNC2 and MNC3 are working their businesses with Company B as their official distributors for this particular territories, but their distributorship agreements Company B might have been established through a 'hidden distributorship' kind of an agreement.

The interviewees in Company A, Company B and Company C stated that they cannot write the TRNC as a 'state' in their contact addresses in their international contacts. Haydar stated that during the importation processes of the goods by Company A, they are not having any difficulties caused by their contact address because MNC1 has a production facility that provides goods to the region from Turkey. As, Turkey recognizes the TRNC, the inner working structures of the co-investment in the form of a distributorship agreement between MNC1 and Company A in the TRNC

<sup>6</sup> It was succeeded by the TRNC in 1983.



do not undergo a change by the context of non-recognition of the TRNC.

On the other hand, the Company B is importing all the products of MNC2 from a country that does not recognize the TRNC, since MNC2 does not own any production facility in Turkey. When it comes to MNC3, while Company B can import some of the replacement parts from Turkey, all the imported automobiles are produced in a country that does not recognize the TRNC. None of the products that are shipped by MNC2 or MNC3 can arrive the TRNC directly on a legal base. As the TRNC is unrecognized by this particular state, there is not any shipping way or a flight between that state and the TRNC. The involved companies are getting around this problem with a kind of a 'tunnelling method'. This method is also used by Company C with MNC4 and MNC5. In this method, the MNC ships its products first to Turkey, and when these goods arrive to the customs of Turkey, the 'so-called' international shipping of these goods seems like ended, but then, these goods are shipped from Turkey to the TRNC. This process is being accomplished by using a 'masked' address for the TRNC in the international area, which is 'Mersin10/Turkey'. However, this method for the importation increases the costs of shipping and causes a waste of time in the shipping processes for the local companies of the TRNC, as well as for the MNCs which operate in the TRNC.

In addition to this, there are some structural differences that exist in the businesses of Company C, as a distributor of MNC4 and MNC5, which are related with the context of non-recognition. It must be noted that the prevention of the productive industries in the TRNC through the embargoes and non-recognition is the biggest factor in the decision of Company C to establish distributorship agreements with MNC4 and MNC5. Mithat, who is one of the owners/shareholders of Company C, stated that the owners of Company C were the first party to call for a distributorship agreement with MNC4 and MNC5 due to the lack of production of these goods in the TRNC.

Another structural difference in the operations of Company C with MNC4 and MNC5 is related with the issues that involve the 'legality' of the distributorship agreements:

Mithat: They do not believe that our country is legal, on the governmental basis... According to their home states, we do not have such a state here. Oh, of course... yes, there is a country, but they cannot consider it as a legal state and make a legal agreement with us anyway. So they cannot submit this agreement to the governments of their home states to procure acceptance for its legality.

Interviewer: Then if we consider the issue from the perspective of law...

Mithat: It is made in 'gentlemen like'. ...They cannot report it to their home country as a 'responsibility'. If something bad happens, they cannot prove their home state that our company is a legal entity. This is a disadvantage for them, and we show understanding for this issue. Though, it is a disadvantage for us, too. We cannot move any issue on to 'any' international sort of arena. So there is a reverse situation regarding this,

actually. Our government recognizes an agreement made with them as 'legal', but theirs does not.

We are going to call that kind of a distributorship agreement as 'in-practice distributorship' which is not expected to be established in a state that does not have any issues like 'non-recognition'. According to the information Mithat provided about this kind of distributorships that his company (Company C) involves in with MNC4 and MNC5, the features of 'in-practice distributorship' are as the following:

- The domestic company, which is the distributor of the MNC, is operating its business through a full responsibility and liability for 'only' the products that this company sells in the particular territories that the domestic company is responsible for.
- Thus, even if the products sold by the domestic 'in-practice distributor', are guaranteed by this distributor within the territory, these products are not covered by the guarantee of the MNC at the after-sale services at the international level. In addition to this, the products of the MNC are sold anywhere in the world, including Turkey, are not covered by the guarantee of after-sale services of this particular brand of the MNC by the 'in-practice distributor' of this MNC.
- In this kind of a distributorship agreement, the alliance between parties is established through a tie that is based on a kind of 'gentlemen's agreement', or a bond of communion, rather than a legally bounded 'official' tie.
- The transportation processes of the goods are provided by the aforementioned 'tunnelling method'. This method increases the costs, but the companies are getting around this problem by increasing the prices of the products that are being sold by the 'in-practice distributors'. By this way, a customer is paying more money for a product of an MNC, but he/she is receiving lesser value for this product, than he/she receives from a product he/she bought from a 'legal' distributor due to the reason provided above. In the context of 'in-practice distributorship', the extra cost is paid by the customer, but a value that is normally included in the price of the goods, which is the after-sale services at international scale, is not received by the customer.
- By operating through an 'in-practice distributorship' of an MNC, the domestic company is taking advantage of the 'brand reputation' of the MNC within its market in order to gain a competitive advantage in sales. In addition, as a distributor, it is not a responsibility anymore for this company to provide after-sale services for the products of the MNC that were sold outside of its own domestic market. On the other hand, the MNC is also taking advantage of the 'in-practice distributorship' by getting rid of the duty of providing guarantees for the products sold by the in-practice distributors at the international scale. Thus, the MNC decreases some of the costs caused by the after-sale guarantees.

Companies A, B, and C all stated that operating a business with an MNC gives them a competitive advantage within the TRNC market due to the 'brand reputation' of the

MNCs. Haydar noted that there some are local brands in the TRNC operating in this sector, but MNC1 is the leading company with respect to the market shares. Thus, their market shares are sufficient for these co-investments in order to be profitable investments for the domestic companies and the MNCs. Moreover, Haşmet, from Company B noted that the market share of MNC2 in the TRNC, is the highest market share amongst all the markets that MNC2 has operations in the World. The Company B even has some awards given by MNC2 for its market share. Haşmet stated that their profitability ratio is also quite high. In this sense, it is possible to say that, even if the total population of the TRNC is small, in some sectors, such as the automotive sector, if the market share is high, then distributor relationships in this small-scaled economy may provide a profitable investment for the MNCs, as well as for their domestic associates.

Nevertheless, an important point to state here is that because of the embargoes, the production industries of the TRNC are excluded from the international markets. Thus, the people of the TRNC are indeed forced to be involved with the international markets as the consumers. Even if the TRNC is a non-recognized state, the MNCs are expanding their business there by exporting their products through domestic companies in the TRNC. They are establishing 'specific' kinds of distributorship agreements and continue to profit by using this small-scaled market of the unrecognized state, the TRNC. This situation is bringing some advantages to the domestic companies of the TRNC that work with the MNCs and their profitability increases more with respect to their competitors in the TRNC. As the domestic companies establish businesses with the MNCs and facilitate their penetration into the TRNC market, they are investing their accumulated capital in other sectors through other co-investments with other MNCs. By this way, there is increased concentration in the TRNC market. Few domestic businesses who work with the MNCs are becoming larger establishments named as 'group of companies'.

### 3.2.2. Franchising

First of all, it is possible to say that franchising, as a foreign market entry mode, is being used in the TRNC market by the MNCs that operate in the service sector, as well as by the commercial MNCs that have industrial production. While the former are using this market entry mode in order to establish their shops that sell services, the latter are also using this market entry mode in order to establish shops as a part of their chains of distribution that are selling their goods produced at their factories located in another country which provides cheaper costs of labour. The sample of this study for this specific kind of market entry mode includes two 'coffeehouse' companies, MNC6 and MNC10; a 'coffee and coffeehouse' company, MNC7; and two 'textile' companies that sell their goods, MNC8 and MNC9. Companies A, D, and E are the domestic companies of the TRNC. While Company A is the franchisee of MNC6, Company D is the franchisee of MNC7, and Company E is the franchisee of MNC8, MNC9, and MNC10 within the TRNC market. The establishment date of Company A dates back to the years before the partition of Cyprus; however, the franchising agreement between Company A and MNC6 was signed in the 2000s, after the Annan Plan. The

Company D was established in the same year with its franchising agreement with MNC7 in the 2010s. The Company E was established in the 2000s but signed all the three franchising agreements with MNC8, MNC9, and MNC10 in the 2010s.

The MNC6 has nine shops located at several cities of the TRNC; four of these shops are owned by Company A as a 'master franchisee', and five of these shops are owned by other domestic companies as the 'sub-franchisees' of Company A. On the other hand, MNC7, through Company D as its franchisee, has two shops and MNC8 has three shops. There are two shops of MNC9 and three shops of MNC10. However, according to the information gathered by the interviewees, the number of the shops of all the MNCs 6, 7, 8, 9, and 10 in the TRNC are increasing constantly. In addition to this, Company A, Company D, and Company E are constantly sparing a constant percentage of their revenues in order to expand their investments and/or in order to make new investments. Thus, it is possible to say that all of these MNCs are expanding within the TRNC market through their franchisees.

In all of the five different franchising agreements between the Companies A, D, E and the MNCs 6, 7, 8, 9, and 10, all of the interviewees stated that their companies were the first parties in order to get into contacts with the MNCs. Kenan from Company A stated that the reason behind this investment was the 'brand reputation' of MNC6. The reason of 'brand reputation' was also valid for Company D in deciding to establish a franchising investment with MNC7. The reason of 'brand reputation' was also valid for Company E in the decision-making process for establishing a franchising investment with MNC8. In other words, the domestic companies believe that due to brand reputation of the MNCs, doing franchising businesses with these companies gives them some competitive advantages within the TRNC market. This could be one of the most important reasons behind establishing franchising investments with the MNCs.

Kenan also stated that, before establishing a franchising agreement with MNC6, Company A was operating distributorships for some other MNCs. Thus, by establishing a franchising agreement and opening up these coffee shops, Company A has invested its accumulated capital gained from its other co-investments with other MNCs in a new profitable co-investment with another MNC. A similar situation to this has been found in the story of Company E. Before starting its businesses with the MNCs 8, 9, and 10, Company E had distributorship of an MNC based in Turkey and invested its accumulated capital from this distributorship on the franchising business with MNC8. The Company E signed the franchising agreements with MNC9 and MNC10 after the establishment of the franchising agreement with MNC8. Thus, Company E also became a 'group of companies'. Therefore, the claim related to concentration of capital in the TRNC through co-investments of the domestic companies and the MNCs and the 'groups of companies', is supported in franchising businesses, too.

Kenan states that when 'the brand reputation' comes together with the 'first mover advantage', it brings a big market share in that specific sector in the TRNC market:

In our sector... As I said, we can easily say that we are the market leader (in the TRNC). Well, it is because we are the first franchisee company (in the TRNC), and because MNC6 has an important place in the world markets, and also, we do the work right.

Each of the franchising case has some different features than the others. To begin with, the franchising between Company A and MNC6 is the most regular case as the franchising agreement between Company A and MNC6 is a legal franchising agreement both in the TRNC and in the home state of MNC6. The most important reason behind this, according to Kenan, is that the home country of MNC6 is not an EU member. Kenan expressed that although the domestic company of the RoC (the Greek side), which is the franchisee of MNC6 in the RoC, tried to undermine the establishment processes of the franchising businesses of the MNCs with the domestic companies of the TRNC through 'lobbying activities', Company A could succeed to establish a legal franchising agreement with MNC6, Kenan stated that:

Here (in the TRNC), you know, the embargos, etc... Since the TRNC is an unrecognized country, it is pretty difficult for MNCs to enter the market of the island (the TRNC). Also there's the Greek (RoC) lobby, etc... But the real reason is that it is (MNC6) a company based in the 'Country X'; because they are not a member of the EU, they stay away from those kinds of political issues... TRNC was eventually a new market and a new country for them (for MNC6). So we could establish the agreement.

Yüksel from Company D also mentioned the same problem:

Well, they (the MNC's RoC franchisees) say 'Cyprus is an EU territory, and that we are in the EU and it is actually the whole island (Cyprus)... There is a temporary 'status quo' situation. When this situation comes to an end, I will open one', and they can deceive the firm (the MNC) by this way. There is actually another country in itself, but... because it is unrecognized, they say 'it is an occupied territory'. You know all these things... but we cannot explain the world this situation because we do not have such a lobbying abroad...

The 'lobbying activities' of the domestic companies of the RoC are obviously creating some difficulties on these franchising agreements between the TRNC companies and MNCs. However, once MNCs realize that the TRNC has a separate market from the RoC, then they sign a franchising agreement with the domestic companies of the TRNC, regardless of whether this franchising agreement is going to be 'legal' or not in their home states. Tamer, from Company E, stated that before Company E contacted MNC8 for a franchising agreement, MNC8 was not aware that the TRNC has a separate market than the RoC. Therefore, Company E invited a manager from MNC8 to the TRNC in order to convince MNC8:

Foreign companies outside the island are now aware that the island has two separate 'markets' being North and the South. They (used to) know it either as a common market, or the reverse, a Greek (the RoC) market. Well, you know, humbly, there is a situation caused by the smear campaign orchestrated by the Greeks (the Greek

Cypriot companies). Of course, we are... a quite insistent company. So we sent a second mail to ...the development manager of the company (MNC8). And fortunately he took us seriously, and came to visit us. After he came, everything happened easily and quickly.

When it comes to the operational processes and the tools and mechanisms used by the franchisee companies in the TRNC and their franchisor MNCs, it is possible to say that all of the domestic franchisee companies of MNC6, MNC7, MNC8, MNC9, and MNC10 in the TRNC (Company A, Company D, and Company E) are operating with a full responsibility and liability to these MNCs. As it has been mentioned above, Company A is the 'master franchisee' of MNC6. There is no 'joint venture agreement' between these two companies, but MNC6 has given Company A the official right to establish 'sub-franchising agreements' with other companies in the TRNC. The reason behind why MNC6 did not establish a joint venture with Company A while signing a 'master franchisee' agreement could be caused by the issues on the property ownership in the TRNC which has been mentioned in the previous section. Thus, MNC6 avoided risking its capital and pursued its benefits through the royalty payments received from Company A and expanded its capital by getting a share from the royalty payments that Company A receives from its sub-franchisees as well. In addition to this, Kenan stated that the expansion of capital through the number of the stores in the TRNC market is an obligation for Company A due to their franchising agreement with MNC6:

In the contract which we signed... it was written that in the first decade we had an obligation to open at least seven stores, and we met this condition.

Moreover, there are some other responsibilities of Company A against MNC6 as a franchisee: they are being audited by MNC6 in a regular base every year, all the operations are being realized under the rules that MNC6 determines, and they cannot sell any product in these coffee shops without the approval of MNC6. Moreover, Kenan stated that this is an important rule for all of the franchising agreements, but there are some domestic companies in the TRNC that use the brand names of the MNCs but do not seem to be like a 'real' franchisee:

Before we put up for sale any product in our stores, we have to receive approval from the corporate office of MNC6... Though... in 'X Province' a firm, an X Company which claims that it is an MNC's franchisee, can actually hire a pita maker and sell pitas inside of its coffee shop. Well, then you understand that it is not a real franchisee, it is just... the name of the brand which was just somehow given to the shop.

After our interview, we checked that MNC's internet site in order to investigate that issue and, in line with the statement of Kenan, we also could not find any information regarding a franchisee of this particular MNC in not only in the TRNC but also in the whole Cyprus. Thus, it is possible to say that this particular establishment that Kenan was talking about is not a real franchisee of that particular MNC; it is indeed a 'counterfeit franchisee'. This kind of an establishment could be peculiar to the TRNC market thanks to the non-recognition status of the TRNC. In addition to this, even if all the interviewees from Company A, Company D, and

Company E claimed that these companies are real franchisees of MNC6, MNC7, MNC8, MNC9, and MNC10, after our interviews ended, we checked the internet sites of all of these MNCs. According to their internet sites; MNC6, MNC7, and MNC9 do have franchisees in the TRNC, so it is possible to say that the franchising agreement between these MNCs and Companies A, D, and E are legalized in the home countries of these MNCs. The internet site of MNC10, there is no information about any of its franchisees located anywhere in the world, so the result is limited to the claims of the interviewee from Company E. It is possible to say that the franchising agreement between Company E and MNC8 has been legalized by using a kind of a 'tunnelling method' by showing Company E as a domestic company based in the RoC; in this sense Company E could also be called as a 'tunnelled franchisee' of MNC8.

There is another method that must be noted here. In some cases, the franchisee in the TRNC is being forced to use a kind of 'masked brand' for its original franchising business. We tried to include a fast-food company of this kind into our sample, but the managers of this company refused to participate in the research. Therefore, in order to get some information, we visited a store of this company in the TRNC, on the 9th of August 2018, and had a talk with the store manager. He confirmed that they are a franchisee of a well-known MNC and added that all the products they sell are imported from that MNC and all the business processes in these stores are being operated under the rules and regulations of that MNC.<sup>7</sup> While there is no deeper information about that kind of a franchising agreement, we will claim that this kind of a franchising is another specific kind of franchising which is peculiar to the quasi-legal states, such as the TRNC. We will call this kind of a franchising as 'masked franchising', as they use a brand name different from the real franchisor MNCs'.

When it comes to the operational processes that the franchisees located in the TRNC, it looks like the context of non-recognition plays a great role in these processes also. Yüksel, from Company D, is aware that the lack of after-sale services of the equipment that they use in their stores is a problem caused by the status of non-recognition of the TRNC:

Our biggest troubles are these actually; here (in TRNC), there is not a technical service for the equipment related to the job (coffee machines, etc...) which came from the franchisor (MNC7). We use the equipment, but here (in TRNC) there is not a technical service although you can find these services in the RoC and in Turkey, so we cannot have them serviced whenever we need to.

Lastly, since MNC8 and MNC9 are textile companies, all of the products sold in the stores of their franchisee, Company E, are being imported from these MNCs to the TRNC. On the other hand, MNC6 and MNC10 are 'coffeehouse companies' and MNC7 is both a 'coffee' and a 'coffeehouse' company. All of these three MNCs have their own coffee beans. Therefore, all the franchisees of these companies in the TRNC (Companies A, D, and E) are

importing their franchisors' coffees. All the three participants stated that they use, what we call, the 'tunnelling method' in order to get around the problems related to the transportation of goods to the TRNC and this situation increases the costs of transportation. Yet this problem is being overcome by increasing the prices of the products and services in the franchising businesses.

To conclude, in this foreign market entry mode as well, the MNCs find a way to get around of the issues related with dubious legality of their investments and expand through the domestic companies in the TRNC. They use different tools and mechanisms such as establishing a 'tunnelled franchising' or a 'masked franchising' with the domestic companies in order to pursue their business goals. However, there are some real franchising businesses in the TRNC market that are considered as 'legal establishments' in the home countries of some MNCs, such as the franchising business of MNC6. They all have to use the 'tunnelling method' for their international transportation processes. This situation increases the costs, but as it was mentioned above, this problem is solved by the companies by increasing prices of their products. As a result, although the products or services that the MNCs sell are standardized products all over the world, the people of the TRNC are being forced to pay more than the people who live in internationally recognized countries. In addition to this, since the franchisees are paying royalty fees to their franchisors, one may argue that these franchisees could be considered as the consumers of their franchisors to a certain extent. However, once a domestic company becomes a 'master franchisee' of an MNC, this 'domestic' company is also becoming a part of the international business by selling an MNC's 'franchising business' in the domestic market. By this way, the domestic companies pursue not only the profitmaking processes of the MNCs, but also their own expansion.

### 3.2.3. Licensing

MNC11 is an industrial production company that produces 'fast-moving consumer goods' and Company F is a company that produces 'fast-moving consumer goods that are licensed' by MNC11. However, in addition to the production of the 'licensed products', Company F is producing also its own brands' products in the TRNC. The Company F has a large production facility located in Famagusta, a large distribution plant and its centre in Nicosia. There are more than 2500 sales points in every cities of the TRNC, which is expected to increase in the following years.

Company F was established as a joint venture between a domestic company of Turkey (we will call that company as the 'Company F1'), which was a licensee of MNC11, and a few local businesspeople during the time period of 1974 and 1983. The Company F1 owns more than 80% of the shares of Company F, so the domestic shareholders have less than 20% of the shares of Company F. The Company F was established first as the distributor of MNC11 in the TRNC. Haluk from the Company F stated that Company F had been distributing the products that were produced under the

<sup>7</sup> By the end of 2019, this MNC decided to use its original brand name for its stores located in the TRNC. Thenceforward, these stores are using their original brand names in the TRNC market.

license of MNC11 at the production facilities of Company F1 in Turkey, as well as the products that were produced by Company F1. However, after the declaration of the TRNC, Company F established a production facility in the TRNC and started to produce the products of MNC11 at this plant.

When it comes to the question of how the license agreement between Company F and MNC11 has been legalized, Haluk explains as:

Because MNC11 was running a business with Company F1 in Turkey, and Company F1 established Company F here in 1981, and because Company F1 (as a licensee of MNC11 in Turkey) established a factory through Company F here (in the TRNC) in 1983; the products which were produced here (MNC11 branded products) were upheld as if they were made in Turkey. However, because (thereafter) Company F1 was completely acquired by MNC11, the operation here (Company F) directly proceeds via MNC11.

Thus, it could be argued that the rights for the usage of 'MNC11 licence' of Company F have been provided by a kind of a 'tunnelled licensing agreement' between Company F1, and MNC11. However, about ten years after the establishment of Company F, MNC11 bought Company F1. After that, Company F started to work as a 'licensee' of MNC11. However, Haluk stated that the tunnelling method is still used by Company F and MNC11 in order to legalize the usage of the 'licensing rights' of MNC11 for the products produced by Company F:

Interviewer: Does the legal link between Company F1 and MNC11 look as if it is established via Turkey?

Haluk: It looks like that... but in reality, it is not via Turkey. Well, we neither have a direct contact with Turkey, nor running our business under 'MNC11 Turkey'. We purchase the concentrates (a kind of an input which is necessary to produce the 'licensed' products of MNC11) directly from the (headquarter of) MNC11.'

Moreover, the link between Company F and MNC11 was provided by also through a 'masking method' that shows Company F as a 'distributor' of MNC11, not a 'licensee' of MNC11 on official base.

Interviewer: You openly use the brand name of MNC11 in the TRNC. Is it because your license agreement was made via Turkey? Because... As you know, there are some companies here that cannot use their own names.

Haluk: Currently... I won't say 'We can't use'. Because we have the right of production and filling (packaging the beverages), the central firm (MNC11) lets us use the name... but, as I said, because we can't get involved in marketing procedures or other things like the auditing processes here... and because MNC11 does not own another brand under the name of itself to compete with in the TRNC market... This place looks as if it's a distributorship although we are not distributors... and we have to keep on producing.

Moreover, Haluk stated that due to the articles of the 'licensing agreement' between Company F and MNC11, Company F does not have permission to export the 'licensed

products of MNC11' that Company F produces, so it sells them all domestically. This constraint imposed by MNC11 is because of the non-recognition of the TRNC. Another important issue is that Company F is not audited by MNC11 directly. The Company F has its own auditing operations for the products that are produced under the license of MNC11, but the reports of these auditing processes are reported to MNC11.

Similar with the other companies presented, Company F and MNC11 are also using the 'tunnelling method' for the transportation processes which shows the TRNC as a province of Turkey. The same problems, like the increase in the costs and loss of time, are also valid for this case. In addition to this, Haluk stated that Company F is importing all the inputs from a facility of MNC11 which is located in an EU country. Therefore, because of these problems in the transportation processes, Haluk states that Company F has to stockpile a particular amount of the products while waiting for the shipments of inputs and this creates inventory costs for them. However, just like the other companies, Company F is also getting around of this problem by raising the prices of its products in the TRNC market.

We will refer to the 'licensing agreement' between Company F and the MNC11 as a 'tunnelled-masked licensing' agreement. The basic features of the 'tunnelled-masked licensing', as another kind of a foreign market entry mode peculiar to the states that have conditions like non-recognition and embargoes, are:

- The licensing agreement is being legalized in the home country of the MNC by using a 'tunnelling method' that shows the licensee company as a company based in a recognized state by the home country of the licensor MNC.
- In order to restrict its licensee to import the 'licensed' products of the licensor to other markets, the licensing agreement is 'masked' by showing that agreement like as if it is a kind of a distributorship agreement. Thus, the licensee is prevented from importing these products to other markets.
- Because the licensee seems like a kind of a distributor of its licensor (the MNC), the licensee company is not being included in the auditing processes of the licensor. Instead, the licensee is auditing its production process by itself and reporting the results to its licensor. Therefore, the licensee is still operating with a responsibility and liability against its licensor MNC.

The last thing to be mentioned related with Company F and MNC11 is that these companies are benefiting from the governmental incentives promised by the TRNC during the importation processes of the inputs. These are some kinds of tax allowances like 'exemption from customs duties' that were promised by the TRNC state. In addition to this, the land where the centre of Company F is located was provided by the TRNC state as an incentive to this investment. Thus, contrary to the import-based sectors, the TRNC state is providing some incentives to the production companies in order to promote the industrial development. However, since the production industries of the TRNC are undermined due to the non-recognition and embargoes, one

can argue that these incentives are not going to be very beneficial for the domestic production. Due to the embargoes, the producers in the TRNC are going to be unable to export their products to the international markets. Therefore, the governmental incentives that are provided by the TRNC state are, indeed, beneficial for the representatives of the international capital and their interests rather than the industrial development of the TRNC.

### 3.2.4. Joint Ventures

Company G is a joint venture production company which operates in the 'construction sector'. It was established by MNC12, which a company from EU, and another MNC based in Turkey, which we will call 'Company G1'. The Company G was established in 1983, after the establishment of the TRNC, by Company G1 as a foreign direct investment in the TRNC. Due to the fact that the TRNC is a recognized state by Turkey, this investment was a legal investment both in the TRNC and Turkey. However, MNC12 bought more than 75% of the stocks of Company G, so the joint venture was established in 1994. Thus, Company G is a joint venture company of MNC12 and Company G1 today. Company G does not have any subsidiaries in the TRNC. Its only facility has 33 workers in total. However, it has more than 30 dealers in the TRNC market and the number of these dealers is increasing day by day. Also, Company G is a licensee of MNC12.

At the beginning of the interview, Birol, the interviewee from Company G, avoided giving some of the information about the establishment processes of the joint venture. However, he stated that:

In the past years, Company G was bought on the assumption that a possible solution agreement (on the Cyprus dispute) 'will be made' in Cyprus. This company was bought with a belief that this place would be a modern country; a country which would be reconstituted, where two societies work together; where marinas, highways and airports were designed together as if there is a 'united' Cyprus...

Thus, if the Cyprus dispute can be resolved in a peaceful manner in the future, then the value of this particular investment of MNC12 in the TRNC would increase. However, this is a risk that MNC12 took in the face of issues like the property ownership disputes, thus the possibility of losing capital; and it is 'not yet known' if the Cyprus dispute will be resolved or not in the near future. Therefore, one may argue that this investment (Company G) currently is kind of a 'reserve capital' for MNC12.

When it comes to the organic links that exist between Company G and MNC12, Birol states that Company G is not only a joint venture, but also a licensee of MNC12. However, he added that, although Company G is a licensee and operates in accordance with all the standards, rules and regulations designated by MNC12 and produces original 'licensed' product of MNC12, Company G is neither allowed to put the original 'licensed' brand name of MNC12 on the packages of these products, nor it is allowed to use this brand name anywhere in any market. Birol admitted that this situation is a result of the non-recognition of the TRNC, and it undermines the ability of Company G to export its products to any foreign market. When Birol

was asked whether his company faced any difficulties or sanctions, he answered as:

Well, we did not encounter any sanctions but... We could not use our world-wide reputed name (MNC12) as the name of company and as the brand of our products. We experienced a difficulty like that. Apart from this, we are limited in exportation; we cannot export. One of the results of being unrecognized is that... we can almost never export.

It is possible to say that this kind of a 'licensing and joint venture' investment is a phenomenon which is peculiar to the establishments that exist in states with issues like non-recognition and embargoes. We will call these kinds of investments as 'custodian joint venture'. In this kind of an investment, it is possible to say that there are two different market entry modes used by the MNC, which are the 'joint venture' and 'licensing'. However, the 'license' of the products produced in this joint venture establishment is hidden by using a different brand name for these products and for the joint venture than the original name of this MNC.

When it comes to the issue of competition in the TRNC, Birol stated that there are four competitors of Company G in the TRNC market, but Company G is the only company in this sector that has a production facility in the TRNC. He also added that the shares of these four companies and Company G in the market are almost equal. The Company G is gathering nearly 50% of its inputs by exploiting the natural resources of the TRNC.

### 3.2.5. Wholly Owned Subsidiaries

Before beginning, it must be noted that, establishing a wholly owned subsidiary in a particular market is a costlier method than the other foreign market entry modes, and riskier due to the issues related with the property ownership in the TRNC. Consequently, this kind of foreign market entry mode is not preferred as much as the other market entry modes by the MNCs in the TRNC market. The MNC13 seems to be like one of the rare MNCs that took these risks, but the story of this MNC in the TRNC is quite unique.

First of all, MNC13 is a company operating in the 'Information Technology and Telecommunication' sector. However, Company H was first established in 1995 in the TRNC as a wholly owned subsidiary of another MNC which was based in Turkey (Company H1). However, following the acquisition of Company H1 by MNC13, Company H1 became a wholly owned subsidiary of MNC13 in 2006. All of the stocks of Company H are owned by MNC13 today. There are 22 sub-offices and more than 1000 sales points of Company H located in every city of the TRNC, and these numbers are increasing day by day. In addition to this, the expansion process of Company H is backed by the headquarter of MNC13.

In order to legalize its links with Company H, MNC13 uses a kind of a 'tunnelling method' as well. The reason behind this situation is that the home country of MNC13, which is an EU member, does not recognize the TRNC, so MNC13 needs to legalize its subsidiary in the TRNC according to the laws of its home country. This tunnelling method is created by showing this subsidiary in the TRNC (Company

H) as a part of the wholly owned subsidiary of MNC13 in Turkey (Company H1). However, this situation brings some differences on the operational processes of Company H. Faik, our interviewee from Company H, told us that:

All our liabilities are directly linked to Turkey (Company H1). We are integrated to the group (MNC13) via Turkey... Well, there is a pre-assessment before Turkey's assessment in the processes. We report it (any process of Company H) to Turkey (Company H1), and Turkey reports it to the group. Well, global operation is... actually 'financial responsibility', apart from that... our 'systematic connections' are established in some other different ways... as it should be, it is just like how it works in different groups (MNCs). We get in touch with the group at the same time as well.

We will call this kind of an investment model as 'wholly owned tunnelled-subsubsidiary'. The 'wholly owned tunnelled-subsubsidiary' operates with a full responsibility and liability against the owner company (the MNC), but the operational processes of the 'wholly owned tunnelled-subsubsidiary' are being audited by another wholly owned subsidiary of the owner company (the MNC). It can be argued that this kind of a foreign market entry mode is peculiar to the investments located in states that have issues like non-recognition, like the TRNC.

### 3.3. Summary of the Findings

**Table 2.** A summary of the findings on the structures of the businesses of global capital in the TRNC

FOREIGN MARKET ENTRY MODES	FINDINGS
<b>Exporting</b>	<ol style="list-style-type: none"> <li>1. Distributorship agreements are commonly used by the MNCs/TNCs.</li> <li>2. Although ordinary distributorship agreements are existent, some different kinds of (extraordinary) distributorship agreements are also being made in some cases. Such as:               <ol style="list-style-type: none"> <li>a) Hidden Distributorship</li> <li>b) In-Practice Distributorship</li> </ol> </li> <li>3. No governmental incentive (from the TRNC state) has been used by the MNCs/TNCs or the domestic companies.</li> </ol>
<b>Franchising</b>	<ol style="list-style-type: none"> <li>1. Although ordinary franchising agreements exist, some different kinds of (extraordinary) franchising agreements are also made in some cases. Such as:               <ol style="list-style-type: none"> <li>a) Tunnelled Franchising</li> <li>b) Masked Franchising</li> </ol> </li> <li>2. No governmental incentive (from the TRNC state) has been used by the MNCs/TNCs or the domestic companies.</li> </ol>
<b>Licensing</b>	<ol style="list-style-type: none"> <li>1. Some companies use the 'tunnelling' method and 'masking' method together in order to legalize the licensing agreement in the international area; the 'Tunnelled-Masked Licensing'. Some structural differences exist due to the usage of these methods, such as:               <ol style="list-style-type: none"> <li>a) The licensor prohibits the licensee to export the 'licensed' goods that produced in this factory of the licensee.</li> <li>b) The licensee is not subjected to the auditing processes of the licensor; the licensee audits itself and reports the results to the licensor.</li> <li>c) The licensee experiences successive periods of capital expansion and capital downsizing due to the prohibition of exporting.</li> </ol> </li> <li>2. The TRNC state provides governmental incentives to these kinds of businesses.</li> </ol>
<b>Joint Ventures</b>	<ol style="list-style-type: none"> <li>1. The joint ventures allow benefiting from the 'imperialist dispossession' of the TRNC. In other words, the idea of 'accumulation by dispossession' exists in the minds of the global capitalists.</li> <li>2. There is no relevant information about the usage of governmental incentives provided by the TRNC state.</li> <li>3. The MNCs may establish a kind of 'masked' licensing agreement through establishing a 'Custodian Joint Venture' business.</li> <li>4. The MNCs may exploit the natural resources of the TRNC.</li> </ol>

In summary, it is possible to say that, while pursuing their expansion processes in the TRNC market, except the structural differences that could be handled within operational processes inside the MNCs, such as using tunnelling methods, the MNCs are not experiencing much difficulties related with the non-recognition of the TRNC. Quite the contrary, some of them are in fact enjoying the governmental incentives provided by the TRNC state, such as the tax allowances and the land grants, and they are pursuing their expansion through their investments in the forms of different foreign market entry modes, such as 'exporting', 'franchising', 'licensing', 'joint ventures', and 'wholly owned subsidiaries'. On the other hand, in some of these market entry modes, such as 'exporting', 'franchising', and 'licensing', the MNCs pursue their interests by expanding their businesses without risking their capital by getting associated with the domestic companies, or without spending money on these investments. The MNCs either sell their products, or sell the usage rights of their brand names to these domestic companies of the TRNC. However, in order to legalize their businesses which are located in the TRNC, MNCs use some different methods such as 'tunnelling', 'masking' or a kind of 'hiding' mechanisms for their own operations in the TRNC. (Please see Table-2 below for details.)



**Wholly Owned Subsidiaries**

1. The MNCs may use a kind of 'tunnelling method' in order to legalize their wholly owned subsidiary (in the TRNC) at the international area: 'Wholly Owned Tunnelled-Subsidiary'.
2. The TRNC state provides governmental incentives to these kinds of businesses.

In order to expand in the TRNC market, most of the MNCs are using exporting (through distributorships), franchising, and licensing as foreign market entry modes. Since the TRNC is a small-scale economy, the reasons behind preferring these market entry modes could be due to the market size of the TRNC. However, another important reason behind choosing these market entry modes more commonly could be caused by the disputes on the property ownership in the TRNC. Thus, by using their distributors, franchisees, and the licensees, the MNCs are eliminating the risk of losing their properties located in the TRNC; avoiding the capital costs of establishing their investments in the TRNC; pursuing 'the sale' of their products in this particular market; and getting extra payments, such as a percentage of the profits, and the royalty fees, from these domestic companies. Therefore, the domestic companies of the TRNC, which have business agreements with the MNCs, are bearing the capital costs of these investments and the legal risks on their own. Therefore, in any case the MNCs have found ways to avoid the costs and risks born by investing in the TRNC, or at least have found ways to transfer them over their local partners.

Another important finding of this study is that MNCs with productive investments in the TRNC market are either getting governmental incentives from the TRNC state for the capital costs, such as land appropriation, or they are exploiting the natural resources of the TRNC for their inputs. Thus, it is possible to say that, the MNCs are either eliminating the risks related with the disputes on the property ownership in the TRNC through eliminating the capital costs of 'land' by using the governmental incentives, or they are taking these risks in return for exploiting the natural resources of the TRNC. Moreover, regardless of whether it is an investment in a production industry or not, the wholly owned subsidiaries of the MNCs are also benefiting from the governmental incentives provided by the TRNC, such as tax allowances.

#### 4. Conclusion

In this study, it has been attempted to analyse the dynamics of the existence and expansion of international businesses in a de-facto state. It is possible to say that, no matter for what reason (market-seeking, efficiency-seeking, or resource-seeking) and in what form (industry or service sector), the primary objective of those firms is to gain profit by selling their goods or services. We argue that, in order to expand and continue to accumulate capital, MNCs would even expand to markets which have problems related to legality and recognition, like the TRNC. Thus, being an unrecognized de-facto state is not an impediment to the expansion of international business into these territories.

One finding of this study is that, under normal conditions, due to its small market and relatively high labour cost, TRNC is not a very attractive site for MNC investments.

Something else which further decreases the attractiveness of TRNC for the MNCs is that it is internationally unrecognized, so the legality of its existence and of its economic relations are in question. Moreover, there are international embargoes imposed on the TRNC which highly restrict its international economic activities, especially when it comes to exportation and transportation. Therefore, as a typical de-facto state, the TRNC has a weak economy which is dependent on Turkey and it has not been attracting much FDI. Despite these problems, there are increasing MNC activities in the TRNC markets, and that is the puzzle that this study has been trying to explain.

The hypothesis of this study was that, due to the issues related with international laws and regulations, investing in an unrecognized state may create different mechanisms and dimensions than investing in the territories of other states that do not have such conditions. In this sense, a field study of MNC activities in the TRNC was conducted through semi-structured interviews with the representatives of local companies which have ties to MNCs in order to reveal and examine these differences, the inner dynamics of the investments of the MNCs in the TRNC market, the tools and mechanisms used by them within their investments and operational processes in the TRNC and the effects of these investments on the domestic market of the TRNC. The data and analysis of the field study were provided in the previous section.<sup>8</sup>

First of all, this study showed that, although the TRNC is an unrecognized state with a small-scale economy, the MNCs have been expanding in the TRNC market. Though quite limited, the MNC activities have always been somehow present in the TRNC, but they definitely increased in the post Annan Plan period. This may be because the TRNC's interactions with the international institutions increased after the Annan Plan referenda and this gave more confidence to foreign investors. At the same time, probably this increase in MNC activities is also due to rising expectations for the future reunification of the island or another peaceful solution for the 'Cyprus Dispute'. The opening of border crossings between the TRNC and the RoC in Cyprus in 2003 and the 2004 Green Line Regulation which allowed some limited trade between the two sides can be other factors that boosted MNC investments in the TRNC. In fact, we can consider the Annan Plan as an important turning point for MNC activities in the TRNC.

Due to the context of non-recognition of the TRNC, even if there exists a de-facto state named the TRNC in these particular territories, the businesses of the MNCs in that particular state could be considered as 'quasi-legal' in the international area. Although the home countries of these MNCs do not recognize the TRNC, some of these states are already considering the TRNC operations of the MNCs as 'legal'. When it comes to the other states that do not consider these investments as 'legal', it is possible to say

<sup>4</sup> The analyses and findings of the interviews were confirmed by an expert who double-checked the transcripts of the interviews for objectivity.

that the MNCs are achieving to legalize their investments located in the TRNC before the laws of their home states as well as the international laws by using extraordinary methods, tools, and mechanisms, such as use of 'tunnelling method' for the appearance and determination of the location information of these investments. However, after the opening up of the border gates between the TRNC and the RoC and the Annan Plan, the MNCs started to use some addresses that seemed as if they were based in the RoC for their tunnelling methods.

MNCs use some other methods for their investments in the TRNC market; they establish different kinds of businesses with different working structures that can be considered as 'extraordinary' with respect to their investments in the territories that do not have the same political status with the TRNC. Some of these establishments can be exemplified as the 'hidden distributorships', 'in-practice distributorships', 'masked franchising', or the 'custodian joint ventures'. In fact, the MNCs tend to use any opportunity and alternative to overcome the obstacles on their expansion processes.

Another finding of this study is that, MNCs generally choose less risky market entry modes in the TRNC. Since the TRNC market poses a lot of risks such as embargoes, non-recognition, and property issues, MNCs are generally convinced by the TRNC companies to come and invest in the TRNC. In doing so, they mostly choose methods like licensing and franchising where the risk falls more on the local companies rather than the MNCs. This is a very important finding, because it shows that although de-facto states may look like risky locations for FDI, MNCs can still find ways to minimize their risks. In fact, neither the de-facto state nor its local companies have much bargaining power with the MNCs under the 'quasi-legal' conditions of the de-facto state.

Another finding which is again related to the specific conditions of the TRNC, especially to the small size of the market and high income level, is that the productive efficiency-seeking investments do not come to the TRNC. Therefore, most of the MNC activities in the TRNC are in services and commercial sectors and are created by distributorship, licensing and franchising agreements. In that sense, the TRNC is getting linked to the international capital, though not as a producer but as a consumer society. The TRNC can export almost nothing to the states other than Turkey, but it continuously imports products from countries that do not recognize the TRNC through the MNCs. Hence, the TRNC is continually running large trade deficits (Theophanous et al. 2008). Thus, also in terms of trade, MNCs are the main winners in their relationship with the de-facto state, the TRNC.

There is another important issue related with the findings of this study. Some domestic companies establish businesses linked with the MNCs due to the fact that the 'brand reputations' of the MNCs provide them a competitive advantage over their rivals within the TRNC market. Therefore, by eliminating their rivals in the TRNC market, they are able to dominate the market and make high profits. However, they invest their accumulated capital in some other mutual businesses with other MNCs either in the same or in different sectors. By this way, these domestic companies grow and become 'groups of companies' and the capital in the TRNC is getting concentrated and centralized

in the hands few business groups. Therefore, MNC investments in the TRNC are not only beneficial for the MNCs but also the domestic companies who do businesses with them. Considering the limitations of the TRNC market, the growth of these domestic business groups and their domination may have serious adverse effects in terms of monopolizing or at least decreasing the competition in the TRNC market. Therefore, how beneficial these investments are for the TRNC economy and the society in general is an important question to be discussed, but it exceeds the limits of this study.

Though limited, the findings of this study are important for two reasons. Firstly, this study adds on the literature by providing a better understanding on the different structures, tools and mechanisms that are used by the MNCs, particularly in the context of quasi-legal states. By this way, this study shows the capability of international capital to overcome juridical issues and political limitations in time and space. Secondly, this study not only shows the capability of international capital to overcome these limitations for its expansion processes, but also explains 'how' and 'in what ways' MNCs expand towards these territories. Thus, by pointing out the adaptability and persistence of MNCs in even challenging foreign markets, our study contributes to the 'international business' literature. The scholars who are interested in the implications of our study with respect to organization-environment relations can further analyse the MNCs activities in different kinds of legal or quasi-legal conditions. Besides international business literature, this study also contributes to the 'de-facto states' literature, especially in terms of their economic conditions and international economic relations, and to our knowledge, it is the first extensive study of the TRNC case regarding MNC activities. Therefore, since this study deals with the economic outcomes of an international political condition, such as "non-recognition" of a particular state, this study also aims to contribute the International Political Economy literature by providing a better understanding on the inner-dynamics and reflections of processes related with such outcomes. It must be noted that the findings of this study are limited to the case of the TRNC. Therefore, in order to have a better vision on these issues, further investigations could be made by choosing different cases of de-facto states that have similar political conditions with the TRNC. So far, de-facto states literature is dominantly focused on their political issues. There is very little discussed in terms of their economies, especially with reference to FDI. Therefore, this study has the potential to be a pioneer study for investigation of MNC activities in de-facto states.

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## Appendix: The Interview Questions

### Şirketinizin KKTC'ye girişi hikayesinden biraz bahsedebilir misiniz?

- Yabancı ortaklarınız (veya anlaşmalı olduğunuz yabancı şirket/şirketler) ile ilk siz mi iletişime geçtiniz yoksa onlar mı size ulaştı?
- Neden böyle bir ortaklık (veya anlaşma) istediniz/istediler? Karar sürecinizi (veya karşı tarafın ilk tepkilerini) bize anlatabilir misiniz?
- Bu sektörde daha önce yabancı ortaklarınız (veya anlaşmanız) olmadan KKTC'de herhangi bir iş yapmış mıydınız?
- Neden yatırım yapmak için KKTC'yi seçtiğinizi/seçtiklerinizi bize biraz anlatabilir misiniz?
- KKTC'ye yatırım yaparken herhangi bir teşvikten faydalandınız mı?
  - Evet ise kimden/nereden ne gibi bir teşvik/teşvikler aldınız?
- Gerek yatırımınızı yaparken, gerek ise işleyiş süreciniz içerisinde olsun, KKTC'nin siyasi olarak Türkiye haricinde başka bir ülke tarafından tanınmamasından ve KKTC'ye karşı uygulanan ambargolardan dolayı çeşitli siyasi veya ekonomik zorluklarla veya yaptırımlarla karşılaştınız mı?
  - Evet ise ne gibi zorluklarla veya yaptırımlarla karşılaştınız?

### Şirketiniz ile anlaşmalı/ortağı olduğu şirket arasında ne tip bir bağ (ortaklık/anlaşma) var? Bu anlaşma(lar) ne tip bir resmiyete dayanıyor?

- Şirketinizin anlaşmalı/ortağı olduğu şirkete karşı belli sorumlulukları var mı?
- Şirketiniz anlaşmalı/ortağı olduğu şirket tarafından herhangi bir denetlemeye yahut uyulması gereken standartlara tabi mi?
- Şirketiniz anlaşmalı/ortağı olduğu şirkete herhangi bir ödeme (franchising bedeli v.b.) yapmakta mı?
- Şirketiniz anlaşmalı/ortağı olduğu şirketten hammadde, ara madde yahut mal alımı yapmakta mı?
  - Evet ise;
    - Şirketiniz bu alımın ne kadarını, ne şekilde, nereden yapmakta?
    - Şirketiniz bu alımlar hususunda herhangi bir kotaya tabi mi?
    - Şirketiniz bu alımları yaparken KKTC'ye yönelik uygulanmakta olan ambargolardan ve KKTC'nin siyasi olarak (Türkiye hariç) tanınmayan bir devlet olmasından ötürü belli zorluklarla karşılaşılıyor mu?
  - Evet ise ne gibi zorluklar ile karşılaşılıyor?
  - Hayır ise;
    - Şirketiniz üretiminin tamamını KKTC'de mi gerçekleştiriyor?
  - Evet ise, üretim şirketinizin anlaşmalı/ortağı olduğu şirketin ülkesinde gerçekleştirilmek yerine neden KKTC'de gerçekleştiriliyor?
  - Hayır ise, üretimin tamamı neden şirketinizde gerçekleştirilmiyor?
  - Bu durumun üzerinde KKTC'ye yönelik uygulanmakta olan ambargoların ve KKTC'nin siyasi olarak (Türkiye hariç) tanınmayan bir devlet olmasının ne derecede etkisi var?
- Genel olarak şirketinizin KKTC'deki yerel piyasada durumu nasıl bize biraz bahsedebilir misiniz?
- Şirketinizin KKTC'de faaliyet gösterdiği alanlarda rakipleri var mı?

- Evet ise;
- Şirketinizin KKTC'de faaliyet gösterdiği sektör(ler) içerisindeki payı, (varsa) rakip firmalara kıyasla, ne kadardır?
- Şirketinizin aynı sektörde olan KKTC yerel firmaları ile rekabeti son yıllarda nasıl seyretmekte?
- Hayır ise;
- Şirketinizin KKTC'de faaliyet göstermekte olan yerel firmalar ile ortak çalışmaları var mı?
- Şirketinizin KKTC'de açılışından bu yana kârlılık oranı nasıl?
- Şirketiniz elde etmiş olduğu kârdan büyüme veya yeniden yatırım için pay ayırmakta mı?
- Evet ise;
- Şirketiniz KKTC'de büyüme veya yeniden yatırıma ne kadar pay ayırmakta?
- Sizce KKTC'de büyümeyi veya yeniden yatırım yapmayı etkileyen faktörler nelerdir?
- Hayır ise;
- Şirketinizin yakın gelecekte KKTC'de büyüme veya yeniden yatırıma pay ayırması söz konusu mu?
- Sizce KKTC'de büyümeyi veya yeniden yatırım yapmayı etkileyen faktörler nelerdir?
- Şirketinizin sektörü son yıllarda KKTC'de nasıl bir değişim göstermekte?
- Şirketinizin ürün pazarında son yıllarda nasıl bir değişim oldu?
- Şirketiniz KKTC'nin yerel kaynaklarından faydalanıyor mu?
- Evet ise, şirketiniz KKTC'nin hangi yerel kaynaklarını ne kadar kullanmakta?