

The Role of Diaspora-Led Foreign Direct Investment in Revitalizing Somalia's Private Sector: Opportunities and Challenges

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Publication Date: 2025/11/27

Abstract: Diaspora-led foreign direct investment (FDI) is a key driver of the private sector's resurgence in Somalia in the aftermath of a prolonged conflict marked by weak state structures and minimal state capacity. This study provides an overview of the size, sectoral orientation, and developmental implications of diaspora-led FDI in Somalia based on extensive qualitative documentation of academic research, institutional and policy documents, and primary survey data. Our review indicates that diaspora capital facilitates entrepreneurship, technology transfer, and employment generation in Somalia, albeit within a highly uncertain regulatory framework, limited physical infrastructure, and insufficient access to formal financial markets. The study concludes by providing concrete recommendations for policymakers to create an effective and equitable business environment for diaspora investors.

Keywords: Somalia, Diaspora Investment, Foreign Direct Investment, Private Sector Development, Financial Inclusion, Post-Conflict Recovery, Institutional Reform.

How to Cite: Dr. Amina Omar Mohamud (2025) The Role of Diaspora-Led Foreign Direct Investment in Revitalizing Somalia's Private Sector: Opportunities and Challenges. *International Journal of Innovative Science and Research Technology*, 10(11), 1540-1543. <https://doi.org/10.38124/ijisrt/25nov1116>

I. INTRODUCTION

Since 1991, Somalia's economy has faced chronic instability, as well as severe state collapse and widespread insecurity (Clingendael Institute, 2023). These conditions have led to significant disruption to formal public institutions and the erosion of the economy's ability to deliver basic services, such as infrastructure and regulation, thus compelling the private sector, primarily backed or run by diaspora investors, to serve as the main engine for economic revitalization (Meester et al., 2019; World Bank, 2025).

The Somali diaspora, estimated at more than two million worldwide, is also playing a critical role in supporting their home country's recovery through humanitarian assistance and economic investment (Hammond et al., 2011). Furthermore, annual remittances to Somalia are valued at between \$1.5 billion to \$2.0 billion, and represent one of the country's largest inflows of external funds; a substantial proportion of these remittances are invested directly in entrepreneurial activities as opposed to being simply consumed (Mohanty et al., 2024).

Differentiating themselves from traditional foreign investors, Somali diaspora investors exhibit a unique combination of risk-taking behavior, deep rooted kinship networks that facilitate trust, a dual motivation of profit-making and patriotism, and adaptability when navigating informality (Pangea Trust, 2022; Ibrahim & Dahie, 2016).

Notwithstanding the importance of diaspora-led investment for Somalia's economic development, the scale and effectiveness of diaspora-led investment is heavily contingent upon Somalia's restrictive regulatory environment, lack of infrastructure, and the degree to which financial markets can accommodate non-traditional investors (IFC, 2024; State Department, 2025).

Given Somalia's aspirations for sustainable development, developing a business environment that leverages diaspora investment is a key strategic imperative for policymakers and international stakeholders (UNCTAD, 2019).

II. LITERATURE REVIEW

➤ *Remittances and Investment: Scope and Impact*

While remittances have been shown to be important for household welfare, health, and education in low-income countries, they have very little direct multipliers effect on growth except where converted into entrepreneurial capital (Majid et al., 2017; World Bank, 2025).

By contrast, diaspora-led FDI invests in start-ups and expanding businesses, contributes to the development of value chains and promotes economic diversification in sectors that are less likely to be pursued by mainstream investors due to perceptions of risk (EU Global Diaspora Facility, 2024; Benson, 2016).

Research has demonstrated that many Somali diasporans accept lower or less certain returns – referred to as a "patriotic discount" – in order to pursue their long-term goals of social and economic transformation (Hassan & Warsame, 2024; Hammond et al., 2011).

➤ *Sectoral Foci and Private Sector Transformation*

The majority of diaspora-led FDI in Somalia is directed towards telecommunications, financial services, real estate, logistics, trade and increasingly agriculture and construction (Clingendael Institute, 2023; SONNA, 2025; State Department, 2024).

Telecommunications exemplify the role of diaspora FDI in creating new opportunities: for instance, companies such as Hormuud Telecom, which are funded almost exclusively by diaspora investors, have pioneered mobile payment and digital connectivity technologies that are driving further entrepreneurship (Mohamed & Doğan, 2024).

Additionally, diaspora capital has driven rapid urbanization and investments in physical infrastructure in Mogadishu and other urban centres, with positive indirect impacts on employment and professional skill development (Murshed, 2022).

➤ *Constraints and Structural Challenges*

Literature reviews have identified Somalia's fragmented and unclear investment law, lack of established mechanisms for resolving disputes, property right issues and lack of a single set of commercial institutions as serious barriers to the scale-up and formalization of diaspora-led FDI (IFC, 2024; Clingendael Institute, 2023).

Additionally, Somalia's lack of reliable and accessible physical infrastructure (electricity, transportation, internet etc.) outside of major urban centers constrains the geographical reach of diaspora FDI (Shuraako, 2020; Somali Community Link, 2023).

Informal clan-based investment agreements, which may allow for efficient transactional arrangements in fragile

environments, also tend to exacerbate inequality and social fragmentation, particularly in terms of marginalized communities and rural populations (Diaspora Centre, 2022; Barua & Naym, 2017).

➤ *Comparative Insights and Global Perspectives*

Comparative analyses have highlighted that the reliance on diaspora FDI for post-conflict recovery in Somalia mirrors other fragile states, however, Somali diaspora investors are uniquely positioned within informal networks (Asongu & Odhiambo, 2020; Murshed, 2022).

Thus, Somalia requires specific innovations in investment laws and diaspora engagement platforms, designed to meet diaspora expectations and socio-political realities (Willemsen et al., 2019).

III. METHODOLOGY

Qualitative document analysis (QDA) was used to analyze comprehensive academic research, grey literature, institutional and policy reports and primary survey data (Walter, 2025). The QDA employed a thematic methodology to identify common themes across the analyzed materials (Walter, 2025). Over 50 primary and secondary sources were analyzed, including:

- Peer-reviewed journals (e.g. World Development, African Finance Journal, Development Studies)
- Reports from Clingendael Institute, IFC, World Bank, EU Global Diaspora Facility
- Surveys of diaspora investment (Shuraako, 2020; Pangea Trust, 2022)
- Case studies of successful diaspora-owned MSMEs and large firms.

➤ *The Inclusion Criteria Focused on:*

Recent coverage (post-2015) of empirical and theoretical work related to diaspora investment, private sector development and institutional reform in Somalia and similar fragile contexts (Mohanty et al., 2024).

Thematic coding enabled the identification of repeated patterns, challenges, policy recommendations and gaps in evidence (Walter, 2025).

IV. RESEARCH FINDINGS

➤ *Sectoral Patterns and Economic Impact*

Our primary data indicate that diaspora investors fund all types of MSMEs with average initial investments ranging from US\$5,000 to US\$100,000 and in many cases are undertaken in collaboration with family members or community cooperatives (Benson, 2016; Shuraako, 2020).

Telecom, real estate and logistics have attracted the greatest amounts of diaspora FDI and have contributed to a large increase in employment and the professionalization of

management, as well as the increased use of digital tools (Clingendael Institute, 2023; SONNA, 2025).

Spillover benefits from diaspora FDI include the transfer of technology from abroad, as well as the introduction of international business models -- specifically in digital finance, mobile money, and entrepreneurial training (EU Global Diaspora Facility, 2024; Naughton et al., 2021).

➤ *Social and Institutional Dynamics*

Most diaspora investors rely on kinship and clan-based networks to facilitate transactions in environments without formal regulations; however, this model can strengthen segmentation and exclusion, particularly in periphery regions (Diaspora Centre, 2022).

Many diaspora investors combine profit seeking and a commitment to national development; moreover, many diaspora investors seek to generate benefits for their community, create jobs, and/or to enable future return migration (Pangea Trust, 2022; Somali Community Link, 2023).

➤ *Barriers and Risk Factors*

Uncertainty surrounding the regulatory framework in Somalia, a fragmented investment law and ambiguous property rights reduce incentives for large-scale and institutionalized investment (IFC, 2024; State Department, 2025).

High levels of insecurity and politically-induced violence have resulted in a high level of concentration of capital in safer urban areas, reducing the possibility of rural diversification (Clingendael Institute, 2023).

Exclusion from financial markets is exacerbated by the lack of domestic banks; in fact, over 90% of adults in Somalia are outside of the formal financial system and most transactions occur informally (World Bank, 2025).

V. DISCUSSION

The diaspora-led FDI bridge the “missing middle” in finance and fill the gap left by the state, IFIs, and risk-averse multinational investors (Mohanty et al., 2024; Asongu & Odhiambo, 2020).

The informal but resilient trust networks supporting diaspora FDI are adaptable in fragile settings, but may solidify clan-based silos and limit the development of the business ecosystem across the nation (Murshed, 2022).

Comparative analysis indicates that while diaspora engagement is crucial, Somalia’s context necessitates the implementation of strategic investment law reform, financial innovation (diaspora bonds and digital platforms), and government-led but inclusive diaspora engagement strategies (IFC, 2024; Willemsen et al., 2019).

Through inclusive policies and partnerships between donors and the private sector, it is possible to expand access to infrastructure, credit, and skills and thereby mitigate market segmentation and foster entrepreneurship in rural areas (Wardheer News, 2024; Somali Community Link, 2023).

VI. POLICY RECOMMENDATIONS

- **Legal and Regulatory Framework:** Develop a unified national investment law with strong property rights, contract enforcement, and investor protection to attract both diaspora and local entrepreneurs (IFC, 2024; State Department, 2025).
- **Financial Innovation:** Design and promote diaspora bonds, loan guarantees, and regulated digital lending to formalize diaspora financing and expand financial inclusion (World Bank, 2025; EU Global Diaspora Facility, 2024).
- **Institutionalized Engagement:** Develop recurring diaspora investment forums, mentorship programs and knowledge-sharing platforms to promote a transparent and supportive business environment (Clingendael Institute, 2023; Naughton et al., 2021).
- **Infrastructure Development:** Collaborate with donors, IFIs, and the domestic private sector to develop physical infrastructure — transport, energy, and digital access — particularly in underserved rural areas (SONNA, 2025).
- **Social Inclusion and Cohesion:** Support co-investment models, and target marginalized communities and women to mitigate against the risks of exclusion and regional disparities (Diaspora Centre, 2022; Somali Community Link, 2023).

VII. CONCLUSION

Diaspora-led FDI is a vital component for reviving Somalia’s private sector and ensuring economic sustainability, not just as a source of funding, but as a means of introducing transnational expertise and adaptive business models (Clingendael Institute, 2023; World Bank, 2025).

Closing the remaining gaps in legal frameworks, infrastructure, and financial services will be required to transform diaspora goodwill into sustainable and inclusive development.

With coordinated reforms and effective engagement, Somalia can realize the full potential of its global diaspora as both an investor and a partner in transformative growth (Walter, 2025).

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