

SOMALIA

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SOMALIA

- The base of the economy is narrow because the majority of the population is nomadic and highly dependent on livestock and livestock exports for livelihoods.
- A lack of internal revenue and weak public financial management are serious constraints on the national budget, leaving the country almost totally dependent on foreign assistance.
- The AU Mission in Somalia and the Somali National Army have lately recovered many areas from Al-Shabaab control, and capacity development is ongoing but insecurity in most parts of the country, weak institutional capacity, and political instability remain the main obstacles to reconstruction and development.

Overview

The socio-economic indicators of Somalia remain very low. Somalia continues to be highly dependent on livestock production and exports with most exports going to Saudi Arabia. This reflects the country's narrow economic base and consequent high vulnerability to external shocks. Somalia's narrow economic base remains a binding constraint on the federal government's capacity to generate sufficient revenues to support reconstruction and development in an unstable macroeconomic environment.

A new income tax law has been prepared and submitted to parliament for approval. The new income tax legislation is part of a broader Revenue Mobilization Strategy aimed at increasing fiscal sustainability by raising adequate resources for financing fiscal recurrent expenditures. The strategy will initially focus on in-land revenue with new or restored taxes and increasing citizen awareness, accountability and legitimacy through improved tax administration. Security concerns and political instability still have a significant impact on economic development and the provision of social services.

The country has its third Prime Minister in two years. On the security front, government security forces and a strengthened AU Mission in Somalia (AMISOM) have registered significant progress. Donor co-ordination remains a significant challenge in Somalia due to the government's weak institutional capacity, the diverse roles of various regional entities (Federal Government, Puntland and Somaliland) in managing aid, and the challenging security environment, which has forced donors to mainly operate from the Kenyan capital, Nairobi. In order to manage donor aid, the main active donors in Somalia have been co-ordinating their work programmes under the *Somalia Development Partners Forum (DPF)*, whose membership includes the UN agencies, the Multilateral development banks (MDBs), about thirty Bilateral African and non-African representatives, and the NGO Consortium. The African Development Bank is playing a lead role in supporting the international reengagement of Somalia, particularly in the Arrears Clearance/Debt Relief process with the World Bank and IMF. The Bank will also continue its lead role in the areas of public financial management, notably through its representation and involvement in the *Financial Governance Committee (FGC)* established in 2014 and comprising government and donor representatives to deliberate on contracts, concession and recovery of national assets overseas.

Recent developments and prospects

According to the Somali Compact Progress Report of 2014, the socio-economic indicators of Somalia remain very low. Only one in three Somalis have access to safe water; one in ten children die before their first birthday; and one in 18 women die during childbirth. An estimated



1.1 million displaced people, living in camps with limited access to basic sanitation services, are at high risk of contracting infectious diseases.

Somalia continues to be highly dependent on livestock production and exports (most exports going to Saudi Arabia). This reflects the country's narrow economic base and consequent high vulnerability to external shocks. The narrow economic base and the unstable macroeconomic environment make it difficult to generate sufficient government revenues to support reconstruction and development. Remittances, estimated at USD 1.3 billion per annum, and foreign aid are supporting living standards and reconstruction. There have been significant efforts to bolster the private sector, promote inclusive engagement of the people in productive activities, including the diaspora, and generate employment especially for youth. Diversification of agricultural, livestock and fisheries production continues. For example, 60 000 farming households have been supported through voucher-based distribution of agricultural inputs and training. Linkages between producers and business have been developed leading to higher incomes and strengthening food security. To increase the incomes of pastoralists, community-based animal health workers have been trained and national livestock vaccination and treatment campaigns have been carried out. Fishermen received fishing gear and training as well as solar powered refrigerators. However, the provision of equitable opportunities for women is crucial in all sectors of the economy.

Somalia has a long history of receiving aid from non-traditional donors such as China, the Arab League and Turkey. The role of Turkey, which has significantly increased aid to Somalia since 2011, is particularly notable. Total official Turkish aid to Somalia in 2011 was USD 93 million, making Somalia the highest recipient of Turkish aid in sub-Saharan Africa (OECD Stat, 2012). This aid was initially targeted at addressing the humanitarian crisis but, since 2012, its sector focus and modalities of choice have evolved, providing both project aid and programme aid such as budget support, rehabilitating infrastructure and improving service delivery. Total planned Turkish aid for 2014 was USD 128 million, making Turkey the single biggest bilateral donor for Somalia. Turkish aid is having a visible and lasting effect on the Somalia aid landscape (FGS donor mapping, 2014)

Macroeconomic policy

Fiscal policy

A new Income Tax Law has been prepared and submitted by the Federal Government of Somalia (FGS) to the parliament for approval. The new income tax legislation is part of a broader Revenue Mobilization Strategy aimed at increasing fiscal sustainability by raising adequate resources for financing fiscal recurrent expenditures. The strategy will initially focus on in-land revenue with new or restored taxes and increasing citizen awareness, accountability and legitimacy through improved tax administration.

The *Somali New Deal Compact*, endorsed in Brussels in September 2013 by the Federal Government of Somalia (FGS) and international partners, adopted a new architecture for intermediating economic reconstruction and development financial assistance for the country. The new financial architecture entails establishing a *Somali Development and Reconstruction Facility* (SDRF), which will house separate multi-partner trust funds: the AFS (the proposed AfDB multi-partner trust fund for Somalia), the Special Financing Facility (SFF), the World Bank Group, United Nations (UN) and multi-partner trust funds. The new financing architecture is intended to improve the transparency, effectiveness and efficiency of development assistance by (among other actions): i) creating a common governance and management co-ordination structure for the separately managed funds; ii) eliminating the fragmentation of development assistance and improving co-ordination and thereby ensuring better reconstruction and development results; and iii) ensuring that the provision of development assistance complies with the New Deal principles in fragile states (i.e. the use of country systems with the client government leading the process).



Monetary policy

High public expenditures and low revenues have contributed to persistent fiscal deficits, which have largely been financed by printing money. This has resulted in high money supply growth and contributed to inflationary pressures. The Central Bank of Somalia, with assistance from the AfDB, World Bank and IMF, is in the process of improving its capacity to conduct monetary policy and regulate the financial sector.

Economic co-operation, regional integration and trade

Somali diaspora remittances have been and continue to be an important source of foreign exchange and livelihood for the majority of Somalis. These inflows assist households in combating poverty and financing their enterprises. International concerns about the use of remittances to finance terrorism and the consequent planned withdrawal of international banking services by global banks like Barclays Bank in the UK and other banks in the US have either closed, or are threatening to close, the bank accounts operated by Somali Money Transfer Operators (MTOs), a vital channel for Somali remittances. Consequently, it is generally agreed that there are no credible quick solutions to the foregoing remittances threat. Development partners (including World Bank, DFID and IMF) are, nonetheless, currently collaborating with the FGS to come up with a workable solution to Somalia's remittances problem, including the provision of targeted support. The FGS is drafting Anti Money Laundering/Combating Financing of Terrorism (AML/CFT) legislation and aiming to ratify related UN conventions for adoption by mid-2015. The World Bank Group, in partnership with FGS, is developing an initial Action Plan to build AML systems and capacity for better financial/remittance supervision. The Central Bank of Somalia (CBS) has recently extended provisional licenses to MTOs, which will be renewed under more stringent rules from January 2015. DFID is, in collaboration with the Financial Sector Deepening Trust (FSDT) for Africa, assessing how to reduce and manage risk in the 'last mile' of the UK-Somali remittance corridor. The AfDB might complement IMF and WB support to CBS, by providing capacity-building technical assistance in bank regulation and supervision, internal financial controls, and the establishment and implementation of AML/CFT regulations.

Donor co-ordination remains a significant challenge in Somalia due to the government's weak institutional capacity, the diverse roles of various regional entities (Federal Government, Puntland and Somaliland) in managing aid, and the challenging security environment, which has forced donors to mainly operate from the Kenyan capital, Nairobi. In order to manage donor aid, the main active donors in Somalia have been co-ordinating their work programs under the *Somalia Development Partners Forum* (DPF), whose membership includes the UN agencies, the MDBs, Bilateral African and non-African representatives, and the NGO Consortium. The DPF is playing a lead role in supporting the international reengagement of Somalia, with the AfDB supporting the Arrears Clearance/Debt Relief process with the World Bank and IMF. The international financial institutions (IFIs) will also continue to play a lead role in the areas of public financial management, notably through representation and involvement in the *Financial Governance Committee* (FGC). The FGC is spearheading the *Financial Governance Programme*. It has generated several important results including the review of key concession contracts, and it is planning support to the Central Bank. Debt/HIPC experts funded by the AfDB are working on the reconciliation of the country's external debt figures, formulation of a Debt Management and HIPC strategy, and training of debt management staff. Furthermore, the Somalia Donors Group (SDG) is an active group and its meetings discuss such issues as: follow-up action on the Copenhagen Meeting (priorities, New Deal structure, next steps); Multi-Partner Trust Funds; status of the country systems; and partnership principles baseline assessment. The meetings also discuss revenue sharing through fiscal federalism.

A high-level Partnership Forum (HLPF) was held in Copenhagen, 19-20 November 2014. The overall goal was to maintain the constructive momentum towards a secure, stable and



developed Somalia. The meeting reviewed the progress in the five Peace and State Building Goals since the signing of the Somali Compact in September 2013. This included taking stock of achievements, identifying challenges, and jointly agreeing on how to address them. The participants also discussed the way forward and the key milestones in the year ahead. The main takeaways included: the need to focus on implementing the Somali Government's Vision 2016; highlighting progress and challenges in the democratic formation of federal states; holding a referendum on the constitution and new elections; a joint AMISOM and Somali army offensive to liberate and stabilise more areas under Al-Shabaab control; improving financial accountability and partnerships; re-engaging with international financial institutions; and increasing the effort to reverse the fast deteriorating humanitarian situation. The need to build resilience and find longer-term solutions was also discussed, including the implementation of the Bank's sub-regional Drought Resilience and Sustainable livelihoods Programme.

In order to move forward, an information note has been prepared for the AfDB Board of Directors' consideration. The note has three main purposes, namely, to: i) assess the implementation progress and relevance of the initial (2013-15) Country Brief priorities; ii) outline the main challenges that have hindered the smooth implementation of the Bank's proposed interventions in Somalia; and iii) provide a more realistic and strategic results framework, given the actual resources available for the Bank's engagement in Somalia for the remainder of this Country Brief (i.e. up to end 2015). In addition, the establishment of the proposed AfDB multi-partner trust fund for Somalia (AFS) has gathered pace. It will be one of the multiple funds under Somalia's new development financial architecture.

Political and security developments

Security concerns and political instability still have a significant impact on economic development and the provision of social services. The country has its third Prime Minister in two years following a standoff between the President and two successive Prime Ministers. On the security front, government security forces and a strengthened AU Mission in Somalia (AMISOM) have registered significant progress. The first phase of an offensive against Al-Shabaab has seen significant gains in terms of newly recovered territory. However, Al-Shabaab continues to engage in spontaneous attacks including attacks on key government installations and public offices. Some MPs and senior government officials have been assassinated. However, in June 2014, the UN Security Council extended the AMISOM mission in Somalia for one additional year and also partially lifted the arms embargo on the country for the same period to enable the Federal Government of Somalia to strengthen its security forces. In this regard, the FGS continues its effort to build a federal government system. The Interim Juba Administration based in Kismayo has been established; the New Southwest state based in Baidoa has been recognised by the FGS and the UN; and dialogue with Somaliland and relations with Puntland are improving.



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