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February 7, 2020

Statement by the Staff Representative on Somalia
Executive Board Meeting
February 12, 2020

This statement provides an update on recent developments in Somalia, including the outcome of the mission for the second review of Somalia's Staff-Monitored Program and request for a new financing arrangement. The staff report for the second review and request for a new arrangement will be discussed with the Executive Board at the HIPC Decision Point.

RECENT DEVELOPMENTS AND PERFORMANCE UNDER SMP IV

1. **Macroeconomic conditions are stable.** Given the mitigating effects of the humanitarian response, real growth in 2019 is expected at 2.9 percent, despite Spring drought conditions and higher-than-normal rainfall in Autumn. However, these conditions have led to a slight deterioration of the current account deficit, with food imports increasing and agricultural exports declining. Inflation in Mogadishu for 2019 came in lower than projected at 3.1 percent, as increased food production in the latter part of the year, together with a reduction in food transportation costs as security conditions improved, reduced food prices. Looking ahead, staff project a slight recovery in growth in 2020 to 3.2 percent, in part reflecting stronger harvests.

2. **Fiscal conditions continue to strengthen**. Data for 2019 show a continued strong fiscal performance, with cumulative domestic revenue for the FGS reaching US$229.7 million (relative to the indicative target of US$196.3 million), a 25 percent increase over 2018. This reflected both an increase in tax revenues (of US$15.9 million or 11 percent), and a sharper increase in non-tax revenues (US$30.4 million or 68 percent), mostly due to the commencement of payments by International Air Transport Association of over-flight fees. Expenditures came in below projections (US$325 million relative to US$340.5 million), resulting in an estimated fiscal surplus for 2019 of US$13.3 million.

3. **Quarterly reporting of fiscal outcomes across the FMS has begun and been sustained.** While further work is needed to improve the quality, these preliminary figures suggest that domestic revenues for the FGS and FMS together could represent about 6 percent of GDP in 2019, relative to a projected 4 percent for the FGS alone.

4. **The broader momentum on fiscal federalism is being maintained.** Finance Ministers of the Federal Government (FGS) and Federal Member States (FMS) have met on two further occasions since September, while technical cooperation on customs modernization and public financing management has also strengthened. This has helped build consensus on some key

fiscal issues, including principles governing inter-governmental transfers, the need for a common customs tariff, and the need to harmonize fiscal processes to enhance the quality of fiscal reporting. The fiscal federalism chapter of the Constitutional Review has also been discussed.

5. **The mission reached a staff-level agreement on the completion of the 2nd review of the current Staff-Monitored Program (SMP)**. All structural benchmarks and ITs for September and October were met. In addition to the commencement of regular quarterly reporting of fiscal operations across FGS and FMS, the *Revenue Act* was enacted, and Finance Ministers of the FGS and FMS agreed some preliminary expenditure assignment guidelines on the allocation of "shared revenue". These initial guidelines are primarily focused on the sharing of budget support grants—which comprise the largest portion of the current base of "shared revenues". The guidelines are expected to evolve as the FGS begins to implement the *Revenue Act* and the base of "shared revenues" expands; they will hold until the formal model of fiscal federalism is confirmed in the updated Constitution.

6. **All December 2019 ITs have been met and the outlook for the SBs is positive; February 2020 SBs are on track.** Staff can confirm that the December SB on including goods inspection in the automated customs' processes has been met. The review on the use of commitment controls, is ongoing preliminary analysis suggests the SB will have been met or almost met, subject to final clarifications from the authorities. With respect to February 2020 SBs, amendments to the *Procurement* and *Statistics Acts* have been passed by the Senate and are now awaiting Presidential signature, and draft implementing regulations on procurement are ready to be issued. Progress on issuing licenses to mobile money operators is also well advanced.

7. **Other critical reforms are progressing.**

a. Legislation. In addition to the *Revenue Law*, the *Public Financial Management Law*, *Companies Law* (on corporate registration and governance) and *Anti-Corruption Law* were enacted.

b. Central Bank of Somalia (CBS). The CBS continues to make progress on its modernization agenda. The new organizational structure was approved by the CBS Board and work to recruit key staff (human resources manager, change management adviser, legal adviser) is progressing well. In addition, plans to recruit new executive directors to support the new functional organization are advancing. To support the implementation of the mobile money licensing and regulation regime, the CBS has strengthened its supervisory capacity. An IMF safeguards assessment was undertaken in the last week of January.

c. AML-CFT. AML-CFT regulations have been issued that cover all financial institutions and their incorporation into the annual re-licensing processes will support improved compliance. Although capacity remains low, the Financial Reporting Center's

technical and phyiscal infrastructure is building,and interagency cooperation is deepening through the operation of the National Anti-Money Laundering Committee (NAMLC).

d. Governance and anti-corruption. The *Audit Bill* has passed the House of the People and is now in the Senate. The process for selecting the nine Commissioners for the Anti-corruption Commission is underway. In parallel, and the authorities are well advanced in developing a National Anti-Corruption Strategy and a program has been agreed with the UNDP to help operationalize it. Outreach is underway to raise public awareness on the importance of fighting and reporting corruption.

NEW 3-YEAR EXTENDED CREDIT (ECF) AND EXTENDED FUND FACILITY (EFF)

8. **A staff-level agreement on a new financing arrangement has been reached.** Just prior to the HIPC Decision Point, the authorities will request Board approval of a new three-year SDR 291 million (178 percent of quota) blended ECF/EFF Fund arrangement.[1] Access under the new arrangement will be heavily front-loaded, given the large up-front balance of payments needs. Staff understands that the authorities intend to use the proceeds of the first disbursement to repay the bridge financing required to clear Somalia's arrears to the IMF, while the additional access envisioned under the program is intended to be used to strengthen the central bank's reserves.[2]

9. **The program is intended to guide reforms during the interim period between the HIPC Decision (DP) and Completion points (CP)**. These will be anchored on further strengthening PFM, improving domestic revenue mobilization, continued deepening of central bank capacity, and enhancing governance. Reform commitments under the new program have been designed to complement the preliminary set of floating Completion Point triggers as discussed with the authorities.

10. **May 2020 SBs will be carried forward into the new Fund arrangement, with some adjustment.** Specifically, although work is advancing well, technical and capacity challenges are likely to lead to a short delay in implementation of HS codes and completion of work on modelling ad valorem tariffs. Enacting the *Targeted Financial Sanctions Law*[3] will be more challenging, especially given the 2020 parliamentary schedule will likely be shortened by election preparations.

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[1] Assuming that Somalia pays its quota increase under the 14th General Review and that Somalia clears its arrears to the Fund.

[2] SDR 242 million would be needed to repay the bridge financing needed for arrears clearance. All GRA access will be disbursed upfront and therefore subject to full debt relief at the HIPC Completion Point.

[3] These laws are related to the prevention and suppression of terrorism and terrorist financing that many countries adopt as part of their AML-CFT regimes and recommended by Financial Action Task Force and UN resolutions.

11. **Risks around the outlook remain to the downside reflecting continuing security, political, and climate vulnerabilities**. These risks are mitigated by national efforts and international support.

OTHER DEVELOPMENTS

12. **Work is ongoing to prepare for the HIPC Decision Point.** These include ongoing efforts to mobilize adequate assurances to finance the Fund's share of debt relief. Efforts are also ongoing on clarifying specific details around select claims in order to finalize the debt reconciliation.[4] Any new information will be integrated into the debt relief analysis presented in the Decision Point document, but staff do not envisage any substantive changes. Staff is also planning, together with World Bank colleagues, to provide some debt management capacity building ahead of the expected negotiations on debt relief.

[4] About 99.9 percent of the total value of debt has been fully reconciled, and staff is following-up on claims from two creditors worth about $6.5 million.