Fostering Economic Growth in Somalia

Forum: Advisory Panel
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Introduction
Notwithstanding the years of conflict followed by the collapse of the regime of President Mohamed Siad Barre, the economy of Somalia has succeeded in recovering from the effect of the civil war. However, due to limited financial resources, insecurity, and vulnerability to natural disasters, its economy still remains fragile. Moreover, the country’s narrow economic base—its dependence on agriculture and livestock—and its heavy reliance on international development remittances have also intensified the country’s vulnerability to external price shocks. As a result, Somalia remains the 5th poorest country where about 4.7 million Somalis are in desperate need of livelihood support.

Background
Since the collapse of the Siad Barre’s regime in 1991, Somalia has experienced two decades of conflict and humanitarian crisis. This crisis had a detrimental effect on the stability of Somalia, and about 450,000 to 1.5 million Somalis have died from violence and hunger since the outbreak of the civil war. Although the economic growth persisted until 2015, Somalia’s trade deficit has expanded to $3 billion, which left Somalia dependent on international development remittances to finance the deficit and its high consumption rates. In order to reduce the growing deficit, Somalia has to increase its financial inflows. However, this is difficult for Somalia, a country where livestock is the major export commodity that accounts for more than 80% of its total exports. While the livestock industry is able to generate a good amount of foreign currency, it is challenging for the industry to compete on the international stage as Somalia lacks national quality-control regulations. Moreover, since Somalia is highly dependent on a small number of export commodities such as livestock and agriculture, it’s only linked with a few overseas markets, which indicates that a single disruption can pose a great threat to the inflows of the country.

Besides the civil war, the recovery of Somalia’s economy is also hampered by its vulnerability to natural disaster. More than 200,000 Somalis were killed by the 2011 famine, and about one million Somalis are still suffering from large-scale food insecurity. Period of drought

Somalia’s imports have exceeded its exports by a factor of more than four, creating huge deficits

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had lingering impacts on Somalia’s economy: crop failures and reduced rural employment opportunities, increased livestock mortality due to the lack of water resources, and the rise of staple food prices. As a result, Somalia lost $1.3 billion to $1.7 billion due to deceased livestock, and it lost $600 million in crop production. Other than the threat from natural disaster, the high unemployment hinders the economic growth in Somalia. While Somalia has the sixth youngest population in the world, most of the young Somalis intend to leave the country due to unemployment or a low pay in their current jobs. The country’s lack of job opportunities and the young Somalis’ lack of employable skills are the main reasons for unemployment, which is not a surprise in a country where adult literacy is only 38%, with 5 million children being out-of-school.

Unemployment often leaves youth to join militia and radical groups, which further threatens the stability of Somalia. Even if Somalis succeed in finding jobs, which are usually related to the agriculture industry, their job satisfaction rate is relatively low as the work in agriculture is labor-intensive and has low pay.

Yet, Somalia has the potential to strengthen its economy—it has significant oil and gas reserves, solar power and hydropower, marine resources, charcoal, frankincense, and livestock. Therefore, foreign direct investment is increasing annually, suggesting the promising future of economic growth in Somalia. The key to this success, however, depends on the international assistance from the MEDCs and humanitarian institutions, and on the ability of the Federal Government of Somalia (FGS) to create and enforce the effective policy framework.

International Actions

Since 1991, the United Nations (UN) has been working with the FGS to promote peace and security in the country. In June 2013, the UN’s Department of Political Affairs (DPA) has established the UN Assistance Mission in Somalia (UNSOM), a field operation that intends to support political reconciliation and peacebuilding of the nation. This mission is directed by the Security Council, which works with the FGS and federal member states to provide helpful advice on the political aspects of peacebuilding and state-building, to monitor the human rights situation, and to help coordinate the efforts of the international community. UNSOM is currently supporting the efforts of the FGS and federal member states to further improve the security, governance, and economic recovery of Somalia. On the same year in 2013, the FGS and the European Union (EU) hosted a conference in Brussels to endorse the New Deal Compact. At the signing of this compact, the members of the international community pledged $2.4 billion to support Somalia’s reconstruction, which was followed by further pledges of $8 billion in 2014. The New Deal is helping Somalia to become more responsive to the needs of its citizens.
Today, the international community is still engaged with Somalia to support the country in its efforts. In 2017, the international community has attended the London conference to adopt the Security Pact and New Partnership, which sets out agreed goals for peacebuilding and state-building of Somalia. Moreover, it promotes mutual accountability between Somalia and the international community.

Problem Raised

Heavy Imports

While Somalia has slowly recovered from cycles of conflict and period of drought, its economy still remains vulnerable. One of the most serious problems at hand is that Somalia’s exports cannot meet the increasing imports—more than two thirds of GDP accounts for imports, while exports account for just 14.5% of GDP, creating a large trade deficit that is funded by foreign remittances. Due to the damage of vital infrastructure, security checks required to prevent violence, and the shutdown of trade routes, it has become difficult for Somalia to export from the country. These high trade costs set barriers to the small and medium-sized enterprises, which lack the skills and resources to overcome the challenges. Moreover, as Somalia’s exports are concentrated in a few commodities (mainly livestock) and exported to only a few countries, it is highly vulnerable to external shocks, such as the current export ban of livestock due to the disease outbreak.

Fiscal Policy

Another challenge for Somalia to face is the effective implementation of Fiscal Policy. Domestic revenue accounts for just 2.8% of GDP, which hinders the provision of social services by the FGS. Poor collection ability, a weak public finance management system, a narrow tax base, and the absence of essential regulatory frameworks governing revenue collection and administration have created a tax gap of 70-80% of revenue collections. Therefore, social services are underfunded, remaining at just 2% of the budget in 2016. About 85% of the total expenditure goes to the administrative and security sectors, while the economic and social services sectors account for just 10% of total spending.

Dollarization

While dollarization has contributed to the containment of inflation, it deprived the Central Bank of Somalia (CBS) of its capacity to manage the national currency. Somalia has no
capacity to directly affect the volume of foreign currency in circulation, and it cannot influence interest rates or affect the money supply by changing bank reserve requirements. This is a serious problem as all major transactions in Somalia are undertaken in US dollars.

**Threat to National Security**

The security issues, including the ongoing conflict in central and southern Somalia, are also hampering the growth prospects. Al Shabaab terrorists continue to pose a great threat to the security of Somalia, and these terrorist activities have scared away both domestic and foreign potential investors. Also, this threat has resulted in the FGS’s massive spending toward the security sectors, reducing the government expenditure on social services.

**Stance of the P5 Nations:**

**United States of America (US)**

As one of the largest provider of development assistance to Somalia, the US has been engaged in Somalia over the past three decades. Led by US President George H.W. Bush, the US has initiated the 1992 Operation to Restore Hope in Somalia, which succeeded as a short-term humanitarian mission (though it failed to support the state-building and restoration of legal frameworks in Somalia). Recently, the US is focusing on counterterrorism in Somalia. The US is also trying to ensure full diplomatic relations with Somalia, mainly because of Somalia’s unexploited energy and other natural resources.

**United Kingdom (UK)**

UK is among the largest donors of Somalia. UK has also pledged contributions to UN joint programs, the programs that were presented to support the state-building of Somalia, over three years. UK was reportedly the first donor to channel funding to the World Bank Multi-Partner Fund for Somalia, which triggered the support from other donors.

**France**

France’s support in the effort of Somalia is mainly channeled through the UN and the EU. In 2008, France has worked with the US and UK in drafting UN resolution to fight piracy off Somalia and other regions.

**China**

China has been active in supporting the financing and construction of roads, hospitals, schools and the largest stadium in Somalia (In 2014, China has provided $2 million in development assistance to Somalia). Furthermore, China was also one of the first countries to reopen its embassy in Mogadishu, the capital of Somalia. Together with Turkey and the Gulf countries, China is currently investing in various service industries in Somalia.
Russian Federation

Not so much is known about the Russian Federation’s engagement in the situation in Somalia. However, it is known that Russia is among the active humanitarian aid providers to Somalia.

Possible Solutions:

Although the economy of Somalia is recovering from a period of conflicts and drought, more actions have to be taken in order to strengthen national institutions and to build sustainable livelihoods. The major problems that need to be addressed are the (1) insecurity of the nation and (2) the absence of an effective policy framework.

One solution is to increase the support from the international community to combat terrorisms and violence in Somalia. Once the security is ensured, it would allow the FGS to tilt its expenditure from security sectors to social services, and it would attract more domestic and foreign investors. Another solution is to design proper business regulations with the help from UN, which will create a business climate that fosters investment and increases job opportunities for Somalis. This also applies to the implementation of Fiscal Policy—there should be an effective framework to govern revenue collection and administration, through ways such as the mobilization of revenue that is sequenced over time. Lastly, since Somalia is a nation with considerable natural resources (such as oil & gas reserves and marine resources) that have been underexploited, another way to foster Somalia’s economy would be taking advantage of these resources to increase its exports, which can only be accomplished with the assistance from international community to help develop a quality control and sanitary certification system.

Glossary

Dollarization: the process when a foreign currency (the US dollar) is used along with or instead of the domestic currency

Fiscal Policy: the use of government revenue collection (taxes) and expenditure (spending) to influence the economy of a nation

New Deal Compact: an organizing framework (2014-2016) that articulates national priorities and lays the foundation for building reliable, transparent, and functioning state institutions, and for protecting the fundamental rights and equality of the citizens
**Remittance:** the sending of money as a gift to a recipient at a distance

**Tax gap:** the difference between taxes actually paid and taxes that should be paid based on existing laws

**Trade deficit:** a trade deficit occurs when a country’s imports exceed its exports. In this case, the country has to borrow from foreign states to pay for the deficit

**Timeline:**
1991 – The collapse of Siad Barre’s regime, leading to decades of conflicts
1992 - The UN Security Council approved Operation to Restore Hope, which was led by the US to support food and supplies to Somalia
2006 - The UN issued an urgent plea for aid to support 2 million Somalis suffering from drought
2008 - The EU appealed for more help from the international community to deal with piracy in Somalia
2011 - Somalia was hit by a severe famine, and it allowed foreign aid agencies to access some regions
2013 - The UNSOM was established in Somalia to support political reconciliation and peacebuilding of the nation; the FGS and the EU have signed the New Deal Compact at a conference in Brussels
2015 - Somalia’s economy has managed to grow by 3.7% with 1% inflation
2017 - Somalia and the international community have attended the London conference to adopt the Security Pact and New Partnership
Sources


