



The World Bank

Somalia Second Inclusive Growth DPO (P179307)

Program Information Document (PID)

Concept Stage | Date Prepared/Updated: 27-Apr-2023 | Report No: PIDC36017



BASIC INFORMATION

A. Basic Project Data

Country Somalia	Project ID P179307	Project Name Somalia Second Inclusive Growth DPO (P179307)	Parent Project ID (if any) P174889
Region EASTERN AND SOUTHERN AFRICA	Estimated Board Date Jul 27, 2023	Practice Area (Lead) Macroeconomics, Trade and Investment	Financing Instrument Development Policy Financing
Borrower(s) FEDERAL REPUBLIC OF SOMALIA	Implementing Agency Ministry of Finance, Federal Government of Somalia		

Proposed Development Objective(s)

To promote inclusive growth by strengthening intergovernmental fiscal relations and transparency as well as enhancing economic resilience and investment.

Financing (in US\$, Millions)

SUMMARY

Total Financing	75.00
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DETAILS

Total World Bank Group Financing	75.00
World Bank Lending	75.00

Decision

The review did authorize the preparation to continue

B. Introduction and Context

1. **Somalia continues to face multiple and overlapping shocks that affect economic growth and contribute to widespread poverty.** Repeated climate shocks, such as recurrent drought and floods, and other crises, like the COVID-19 pandemic, rising commodity prices due to the Russian invasion of Ukraine, and frequent security incidences have contributed to negative per capita growth rates. Between 2017–22 economic growth rates averaged only 2.2 percent, compared with a population growth rate of 2.9 percent. Labor force participation rates are exceptionally low with only one third of men and 12 percent of women actively engaged in the labor market. Somalia is in the throes of its longest drought on record. Five consecutive poor rainy seasons have dramatically eroded households' asset base (through massive livestock deaths) and purchasing power at a time when global food prices have spiked. The first comprehensive



household survey undertaken in over 30 years shows that in 2022 an estimated 55 percent of the Somali population lived below the national poverty line of US\$741 per person per year, with nomads and rural dwellers worse affected.

The Somali authorities are implementing a comprehensive reform program, supported by this proposed operation, to establish the foundations for addressing the multiple challenges that the country faces. Following parliamentary and presidential elections in mid-2022, the newly elected government has remained committed to the reform agenda rooted in the ninth National Development Plan (NDP9) and is demonstrating strong ownership of the debt relief process. The reforms supported in pillar 1 advance the federal agenda, which is critical for state-building. Measures such as harmonizing customs regimes across the FGS and the FMS and improving accountability for public resources are contributing to revenue raising and trust building between the regions as well as with citizens. Policy reforms in pillar 2 strengthen the government's shock responsive social safety net (Baxnaano), increase financial inclusion, improve job creation in high potential sectors such as fisheries, and strengthen the environment for private sector growth.

Relationship to CPF

2. Somalia continues to face multiple and overlapping shocks that affect economic growth and contribute to widespread poverty. Repeated climate shocks, such as recurrent drought and floods, and other crises, like the COVID-19 pandemic, rising commodity prices due to the Russian invasion of Ukraine, and frequent security incidences have contributed to negative per capita growth rates. Between 2017–22 economic growth rates averaged only 2.2 percent, compared with a population growth rate of 2.9 percent. Labor force participation rates are exceptionally low with only one third of men and 12 percent of women actively engaged in the labor market. Somalia is in the throes of its longest drought on record. Five consecutive poor rainy seasons have dramatically eroded households' asset base (through massive livestock deaths) and purchasing power at a time when global food prices have spiked. The first comprehensive household survey undertaken in over 30 years shows that in 2022 an estimated 55 percent of the Somali population lived below the national poverty line of US\$741 per person per year, with nomads and rural dwellers worse affected.

3. The Somali authorities are implementing a comprehensive reform program, supported by this proposed operation, to establish the foundations for addressing the multiple challenges that the country faces. Following parliamentary and presidential elections in mid-2022, the newly elected government has remained committed to the reform agenda rooted in the ninth National Development Plan (NDP9) and is demonstrating strong ownership of the debt relief process. The reforms supported in pillar 1 advance the federal agenda, which is critical for state-building. Measures such as harmonizing customs regimes across the FGS and the FMS and improving accountability for public resources are contributing to revenue raising and trust building between the regions as well as with citizens. Policy reforms in pillar 2 strengthen the government's shock responsive social safety net (Baxnaano), increase financial inclusion, improve job creation in high potential sectors such as fisheries, and strengthen the environment for private sector growth.

C. Proposed Development Objective(s)

To promote inclusive growth by strengthening intergovernmental fiscal relations and transparency as well as enhancing economic resilience and investment.

4. Strengthening intergovernmental fiscal relations and accountability for public resources to support state-building and enhancing economic resilience by addressing structural barriers to growth are prerequisites for stimulating growth and creating jobs. Strengthening intergovernmental fiscal relations, and accountability for public resources more broadly, is critical for addressing the drivers of state fragility and providing a predictable environment for private sector growth. Enhancing economic resilience is an urgent priority given Somalia's susceptibility to shocks including



increasingly frequent climate-related disasters.¹ Adapting to climate change requires developing coping mechanisms for the most vulnerable and diversifying sources of livelihoods. Climate mitigation can be supported through following a low-emissions pathway for future growth, for example by encouraging investment for electricity generation from renewable sources. Providing opportunities for Somalis to access jobs and obtain a meaningful income to escape poverty requires alleviating structural constraints through supporting financial inclusion, expanding access to affordable and renewable energy supply, and developing the formal private sector. The proposed operation would be the first in a programmatic series of two operations, which supports Somalia's progress in reaching the HIPC Completion Point milestone at which point the country will be eligible for full and irrevocable debt relief.

Key Results

5. Reforms aim to strengthen intergovernmental cooperation to enhance stability as well as promote economic resilience that can support climate adaptation and mitigation. Harmonizing customs regimes and sharing data can help to build trust and encourage dialogue between the Federal Government of Somalia (FGS) and the Federal Member States (FMS). Special audits on health and education expenditures at subnational level can inform the dialogue with government, civil society, and development partners on how public resources are used to support service delivery. More broadly, the new legislative framework will safeguard independence of supreme audit institution, strengthening accountability for the use of public resources. Reforms to enhance economic resilience and investment are expected to contribute to both climate adaptation and mitigation. Improved targeting of households that receive cash transfers from the government's Baxnaano safety net program is expected to enhance coping mechanisms to shocks including climate-related disasters and reduce the gender gap as women are disproportionately affected by multiple crises and food insecurity. Enhancing the enabling environment of the fisheries sector is expected to support sustainable fishing, while also contributing to climate adaptation and mitigation through the protection of healthy fish stocks and the critical marine habitats on which they rely, enhanced resilience of marine resources to the effects of increasing sea temperatures and acidity, as well as improving carbon sequestration in coastal habitats. Supporting renewable energy generation through developing the enabling environment is expected to harness Somalia's substantial solar and wind energy potential; and facilitate a low-emissions pathway for future growth. Reforms to advance the AML/CFT agenda and improvements to the business environment are expected to enhance access to finance and encourage investments which will benefit sectors such as fisheries and energy, as well as support the growth of firms and formal wage employment.

D. Project Description

6. The proposed operation is the second in the series of two Development Policy Operations to support inclusive growth in the Federal Republic of Somalia. The proposed operation is rooted in Somalia's ninth National Development Plan (NDP9), which was developed through an extensive participatory process. The first pillar aims to strengthen intergovernmental fiscal relations and transparency as building blocks towards advancing the state-building agenda. The second pillar aims to enhance economic resilience and investment, as Somalia works towards climate adaptation and mitigation.

¹ Somalia has endured multiple droughts since 1965. The 2011 drought led to the demise of 260,000 people. The 2016/17 drought left over 6 million people food insecure. The current drought is contributing to internal displacement and widespread food insecurity. Somalia is also vulnerable to severe flooding. In 2019-20, floods displaced more than a million people, and following high precipitation and abnormal vegetation growth, the desert locust outbreak decimated crops and affected more than 2.6 million people. It is expected that incidences of droughts and flooding will increase, as indicated by the IPCC Working Group I report, https://www.ipcc.ch/report/ar6/wg1/downloads/report/IPCC_AR6_WGI_SPM_final.pdf



7. Actions in the first pillar strengthen intergovernmental fiscal relations and governance environment more broadly. The harmonization of import duties in the main ports of Somalia was supported in the first year, while the current operation focuses on the issuance of regulations on Customs Reference Values and Customs Declarations. The harmonization of customs duties is a HIPC Completion Point trigger. As fiscal space expands and transfers to the FMS continue to increase, accountability for public spending on service delivery at the subnational level must be safeguarded. A new legislative framework, in the form of a modern Audit Bill, regulates the external audit and the relationship between the federal and state Offices of Auditor General. In addition, special audits of conditional fiscal transfers are planned to inform an understanding of how resources support service delivery at the FMS level.

8. Actions in the second pillar aim to support the resilience of the Somali economy and people. A Data Protection and Data Privacy Bill was enacted to facilitate adequate safeguards concerning the public use of private data. The Data Protection and Data Privacy Bill will support the enabling environment for the government's AML/CFT reforms which includes the publication of a National Risk Assessment and the enactment of the Digital Identification Bill. To support the availability of affordable energy from renewable sources, the Electricity Bill was enacted, which is also a HIPC CP trigger, followed by regulations to the Electricity Act. A prior action is included to enact the Federal Bill on Fisheries to parliament to support sustainable fishing and issue implementing regulations. Finally, under this pillar there are actions to support the development of the formal private sector through the enactment of a new law that will improve the environment for foreign investment, which can help to attract private financing to develop sectors such as renewable energy and fisheries.

E. Implementation

Institutional and Implementation Arrangements

9. The Ministry of Finance has the lead responsibility for the coordination, monitoring, and ensuring ultimate completion of the prior actions. Monitoring of results from the proposed operation will build on mechanisms that the ministry has developed for managing the IMF ECF arrangement and the HIPC Completion Point commitments. Recognizing the government's capacity constraints, prior actions for the proposed operation were selected to complement the ongoing support provided under WB, IMF, and EU projects to minimize the additional workload associated with monitoring the actions in this proposed operation.

F. Poverty and Social Impacts, and Environmental, Forests, and Other Natural Resource Aspects

Poverty and Social Impacts

10. Many of the actions supported by the proposed operation are expected to have significant positive poverty reduction and welfare enhancement impacts. Reforms are expected to speed the pace of poverty reduction by enhancing the stability of the state and increasing economic resilience. Actions under pillar 1 are expected to enhance intergovernmental fiscal relations and accountability, which can provide a foundation for inclusive growth. The special audit on the social sectors is expected to enhance the dialogue on how public resources are used to support service delivery. Reforms under pillar 2 are expected to enhance resilience, spur growth, and help to create jobs. Improving the targeting of beneficiaries for the Baxnaano program can help to ensure that the poorest and most vulnerable receive cash transfers to mitigate shocks, including women, which can have broader benefits for social inclusion. Reforms to enhance access to finance (through advancing the AML/CFT agenda) and support to the enabling environment in sectors such as fisheries, electricity as well as the development of the broader private sector can strengthen Somalia's tradition of entrepreneurship, help to create formal wage employment, and enhance resilience. Furthermore, lowering the cost of



electricity is expected to increase access to energy for the poor.

Environmental, Forests, and Other Natural Resource Aspects

11. The institutional basis for improving environmental management is being established. The Environmental Management and Coordination Bill is currently being reviewed by the Somali Parliament. The House of the People approved the Bill in March 2023 and further reviews by the Senate are expected in May 2023, during the next parliamentary session. Once enacted, the Environmental Management and Coordination Bill is expected to improve environmental governance and intergovernmental cooperation, as well as lay a foundation for undertaking environmental and social impact assessments in the country. The procedures for environmental and social impact assessments have already been elaborated in regulations that have been issued by the Ministry of Environment and Climate Change (MoECC).² The MoECC has commenced negotiations with departments and ministries in charge of the environment from the various Federal Member States, with a view of sharing responsibilities for managing environmental issues, including licensing procedures for development projects. Furthermore, an institutional capacity and structural assessment of the MoECC is underway with the support of the World Bank and the United Nations Environment Program.

12. Four actions in this proposed operation are expected to substantially contribute to three key climate objectives under Somalia's Nationally Determined Contribution (NDC). Prior action 3 supporting data protection and privacy, including its application to adaptive social safety nets, is expected to support poor and vulnerable households cope with the effects of climate change. Prior action 5 on the new fisheries law seeks to strengthen the status of fish stocks and marine ecosystems through enhanced regulation and implementation monitoring. Supporting healthy marine ecosystems is the most effective single measure for countering the impacts of climate change on coastal resources. Furthermore, the development of the fisheries sector presents an alternative source of income and nutrition. Prior action 6 on the enabling environment in the energy sector, combined with prior action 7 on investor protections, is expected to contribute to higher investment levels in least cost renewable energy generation, harnessing Somalia's substantial wind and solar power potentials to address its acute affordable energy challenges.

G. Risks and Mitigation

13. Overall risks to this operation are high. The protracted election period reflects the country's fragility, which can undermine the reform momentum. The Finance Ministers Fiscal Forum, supported by the World Bank, has provided an important channel for advancing technical reforms by encouraging dialogue to help mitigate political and governance risks. The HIPC initiative is a broader framework for risk mitigation by providing incentives for political leaders to collaborate around breaking the vicious circle of weak state capacity, conflict, and persistent vulnerability. High macroeconomic risks reflect the government's limited policy options to respond to multiple shocks such as extreme climatic events, the COVID-19 pandemic, the impacts of the war in Ukraine and regular security incidences. Strengthening the capacity of the state and enhancing fiscal sustainability through implementing reforms anchored in the HIPC initiative can help to maintain macroeconomic stability. The government's engagement in the IMF's ECF arrangement as well as WB IPFs and advisory support are helping to strengthen the mobilization of domestic revenues and improve expenditure controls. Strengthening fiduciary systems remains an ongoing government priority. The new Audit Bill will contribute to a reduction of fiduciary risk, as will continued support from the recently approved Somalia Enhancing Public Resource Management Project (SERP, P177298). Institutional and capacity risks are substantial. Somalia's policy agenda is crowded

² The elaboration of the Environmental Management and Coordination Bill and supporting regulations have been informed by the Somalia Country Environmental Analysis, published by the World Bank in 2020.



and competing demands from domestic and external stakeholders could overwhelm the authorities' limited capacity to implement the reforms needed to achieve the operation's expected results. Risks are mitigated by extensive financial and technical support from international partners, including the World Bank Group

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APPROVAL

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