



Ministry of Finance

Federal Government of Somalia: Government Financial Statistics (GFS) Analytical Report

2013 - 2019

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EXECUTIVE SUMMARY

Since the establishment of the Federal Government of Somalia in 2013, the Government has embarked on a series of ambitious public financial management and public administration reforms to develop modernized and internationally recognized institutions. The accelerated pace of these reforms over the past three years in particular, have not only helped the country in normalizing its relations with international financial institutions, but have also resulted in significant changes to revenue and expenditure. This report is the first of its kind produced by the Ministry of Finance's Economic Policy and Planning Department, analyzing Government Financial Statistics data from FY2013 to FY2019. Moving forward, the Economic Policy and Planning Department will work with the newly established Statistics Bureau to integrate this analysis with broader economic data in order to provide a holistic snapshot of Somalia's economic and fiscal trajectory. It is our hope that such reports will increasingly be used by our international partners including the World Bank, the International Monetary Fund, the European Union, the African Development Bank, and the Islamic Development Bank, among others, to inform their policy.

On the revenue side, aggregate revenue receipts have more than doubled over the period, and a clear shift away from reliance on donor grants is evident through the increased share in actual revenue receipts coming from tax and non-tax own-source revenue sources. More importantly, the Government has been able to widen its tax base and reduce its reliance on taxes on international trade in transactions, resulting in an improved ratio of direct-to-indirect taxes, an important indicator of the pro-poor stance of a Government's tax regime.

On the expenditure side, while Government spending is primarily on compensation of employees, particularly in the security sector, a clear increase in the total share of government spending being spent on social sectors – health, education, housing and community amenities, and social protection – is evident, although this remains considerably lower than internationally comparable levels.

Looking forward, the COVID-19 pandemic poses a serious risk to these improvements being reversed, particularly if development partners chose to channel humanitarian assistance outside of Government systems. As such, it is critical that international development partners commit to a continued increase in the use of country systems, investment in the Government's Public Financial Management reform effort, particularly in the Security Sector, and that Government MDA's continue to increasingly collaborate with the Ministry of Finance to drive Somalia's post-conflict economic recovery and development.

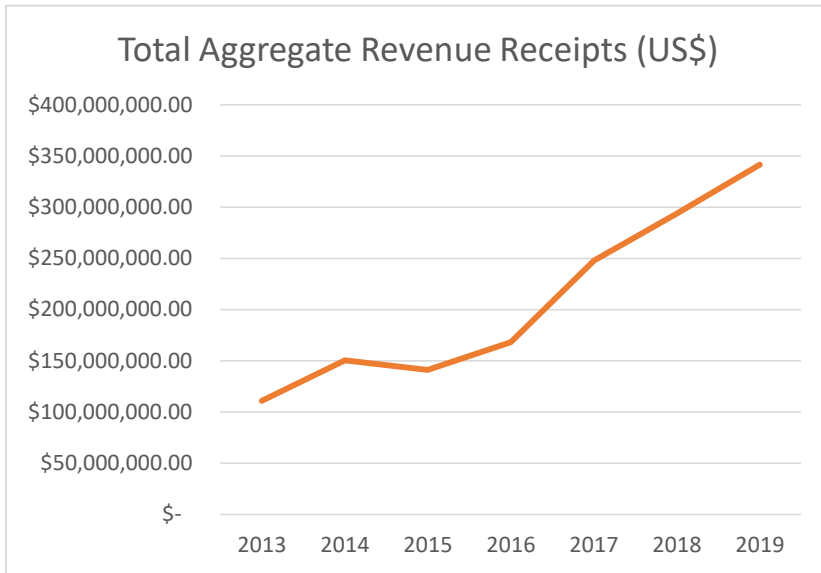
1. INTRODUCTION

Nearly eight (8) years have passed since the end of the Transitional Federal Government of Somalia in August 2012, a critical milestone in Somalia's post-conflict reconstruction and development agenda. Since the formal establishment of the Federal Government of Somalia (FGS), the Government has embarked on a series of ambitious reforms to develop modernized and internationally recognized institutions characterized by the rule of law and made serious headway in promoting a peaceful, secure, and stable Somalia for its citizens. Over the past three years in particular, profound transformation of the Government's Public Financial Management (PFM) and Public Administration (PA) systems have supported Somalia in rejoining the world and in normalizing its relations with international financial institutions such as the African Development Bank (AfDB), the World Bank (WB) and the International Monetary Fund (IMF).

Against this backdrop, this report provides a high-level overview of the FGS's economic and financial performance from 2013 to 2019. In the interests of promoting fiscal transparency, the report draws on data publicly available from the Ministry of Finance's [website](#), which can be downloaded in a tab-separated values format (.tsv) for the reader's own analysis. As this dashboard draws on real-time data drawn from the Somalia Financial Management Information System (SFMIS), and includes currently unaudited financial information for the 2019 financial year, readers are cautioned that final figures may be revised from the time of publication of this document and should refer to the Accountant General's Annual Financial Statements, also available on the Ministry's website, for definitive figures.

The report is divided into five sections. This introductory section outlines the structure of the document and identifies data sources. Section 2 provides a summary of revenue trends. Section 3 provides a summary of expenditure trends, by economic classification, administrative sectors and Ministries, Departments, and Agencies (MDAs), and by functional classification. Finally, Section 4 of this report concludes with brief examination of key opportunities and threats to Somalia's remarkable economic and financial performance reforms in 2020 and the medium-term.

2. REVENUE



Total revenue receipts have grown by over 208 percent between 2013 and 2019, growing from a total of \$110.8 million to over \$341.8 million during the period. This sub-section decomposes these revenue receipts into tax, grants, and non-tax own-source receipts in order to analyze drivers of growth and concludes by providing a comparison of tax-to-GDP ratios against available IMF benchmarks.

Figure 1 - Total Aggregate Revenue Receipts (US\$)

When expressed in percentage growth terms, a clear ameliorating trend is evident as the FGS's aggregate revenue receipts are growing at an accelerating rate of over ten percent annual year-on-year growth between 2016 and 2019, as evidenced in the trendline in Figure 2 below.

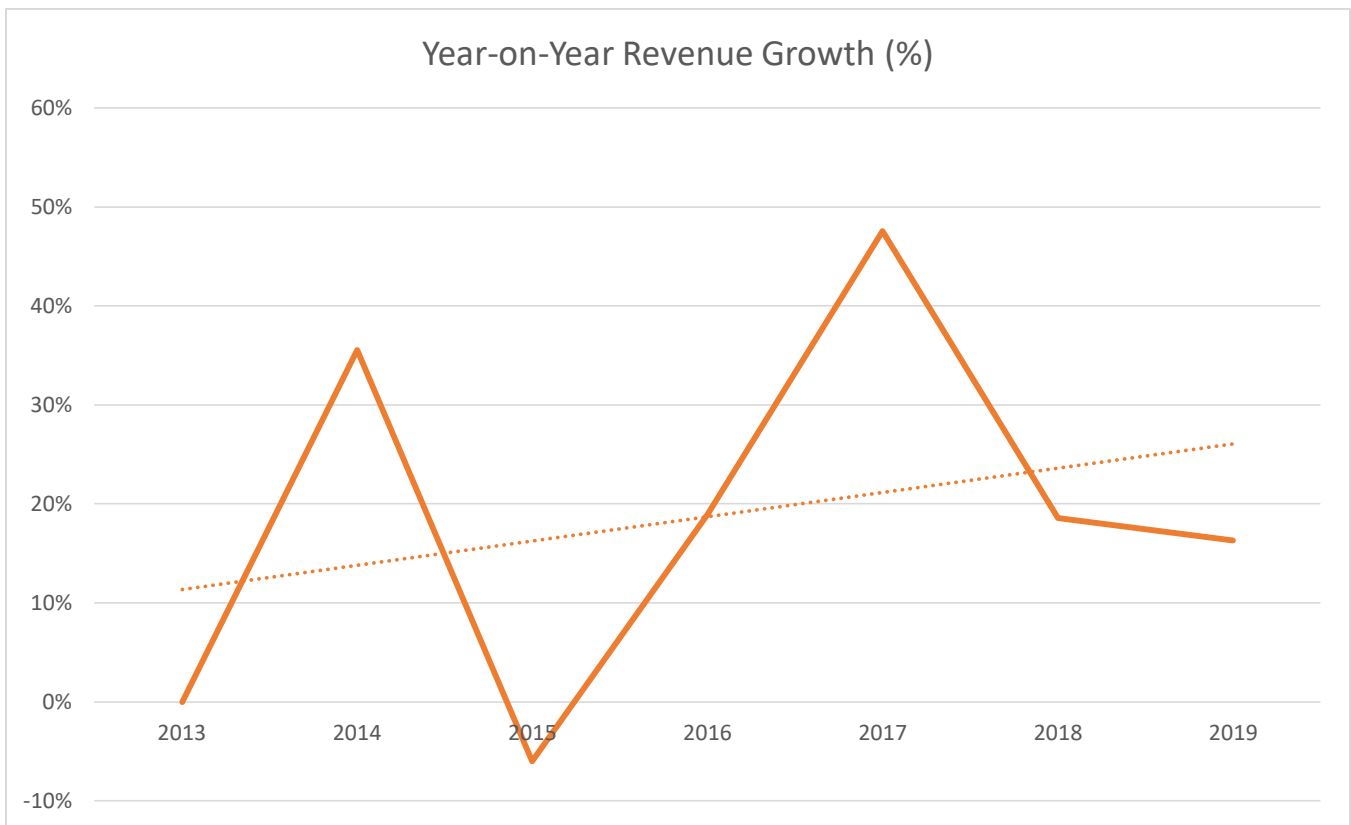


Figure 2 - Year-on-Year Revenue Growth (%)

Decomposing aggregate revenue receipts into the key revenue types: taxes, grants, and other non-tax own-source revenues paints a positive picture of the FGS’s performance; between financial year 2017 and 2019, the share of government revenue accruing from grants receipts (from foreign governments and international bi-lateral and multi-lateral organizations) is decreasing. This trend is commendable as it demonstrates that the FGS’s efforts to mobilize domestic revenue – a key component in starting to re-build State-Society relations – are rapidly yielding results.

Table 1 - Composition of Actual Revenue Receipts (% of Total Revenue Receipts)

Revenue Source	2013	2014	2015	2016	2017	2018	2019
Taxes	59%	49%	60%	53%	45%	47%	45%
Grants	38%	44%	19%	33%	42%	38%	33%
Other Own-Source Revenue	4%	7%	21%	14%	12%	15%	22%

That said, the FGS’s reliance on grants has had an impact on the quality of its revenue estimation and forecasting, particularly in financial year 2019 where donor grants were significantly less than anticipated. The Public Expenditure and Financial Accountability Framework (PEFA), assesses the quality of a Government’s revenue estimates by awarding an ‘A’ grade when the actual receipts are within five percent of the estimate, a ‘B’ grade when within ten percent of the estimate, and a ‘C’ grade when within 15 percent of the estimate. As Figure 3 below shows, the FGS’s scores had been deteriorating significantly between 2014 and 2016, with a marked improvement between 2017 and 2018 resulting in ‘A’ grade scores. Underperformance in grant receipts in FY2019, however, have brought the score for this year to a ‘C’ range, although this remains at a considerably higher level of quality than between the 2014 to 2016 period.

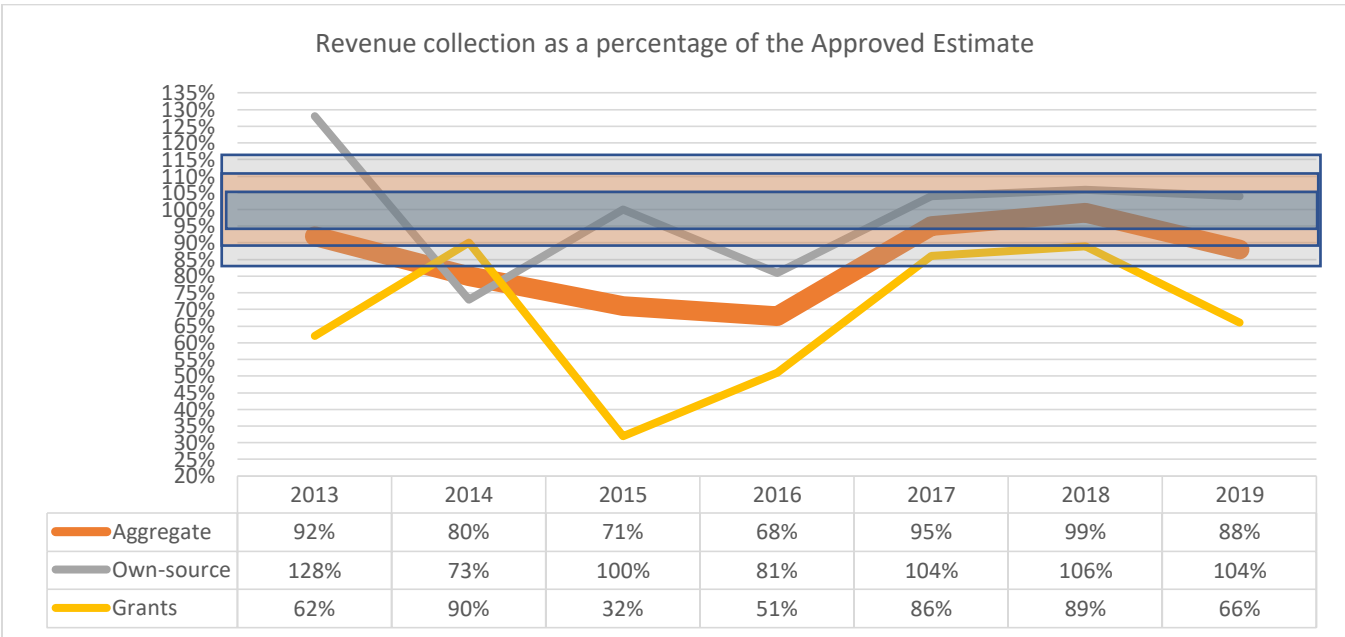


Figure 3 - Revenue deviation trends

Underperformance in grant receipts is not necessarily due to funds not being released by donors in a timely manner, as often there are conditionalities and expected reform actions the FGS must complete and evidence to donors prior to funds being released. This dependency on donor funds does, however, create significant challenges from a cash management perspective as predicting when these funds will be available for Government use has been challenging. As Figures 4 – 5 demonstrate, there is a clear clustering of grants receipts in the last quarter, although in the last three years this has been particularly concentrated in December. As the final month of Government operations during the financial year, this trend is particularly problematic for ensuring timely payments of employees and Government vendors, as well as for underwriting any capital acquisition as the FGS is often unable to disburse these funds in a timely manner prior to the annual appropriation lapsing at the end of December.

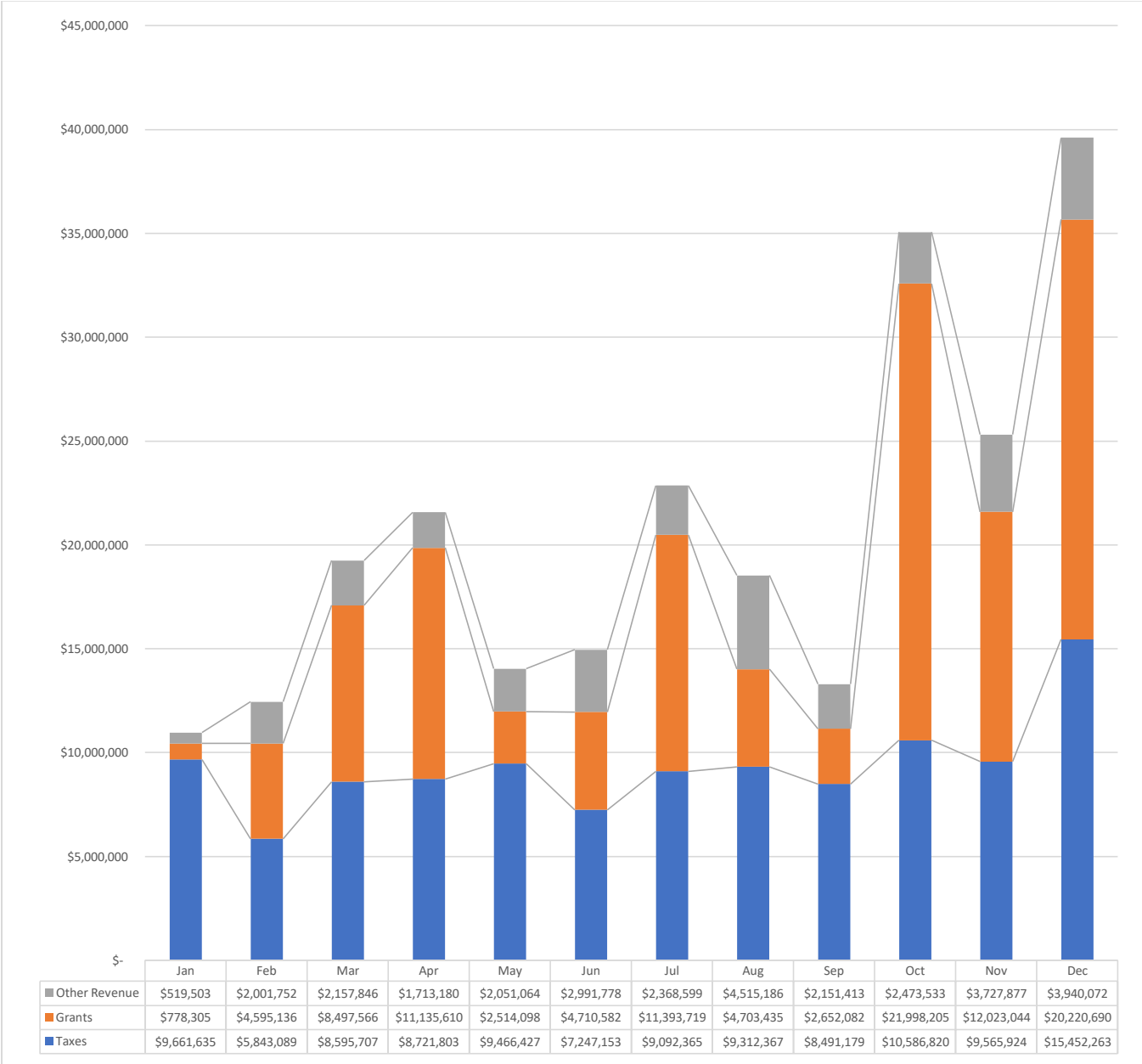


Figure 4 - Revenue Seasonality by Month (2017)

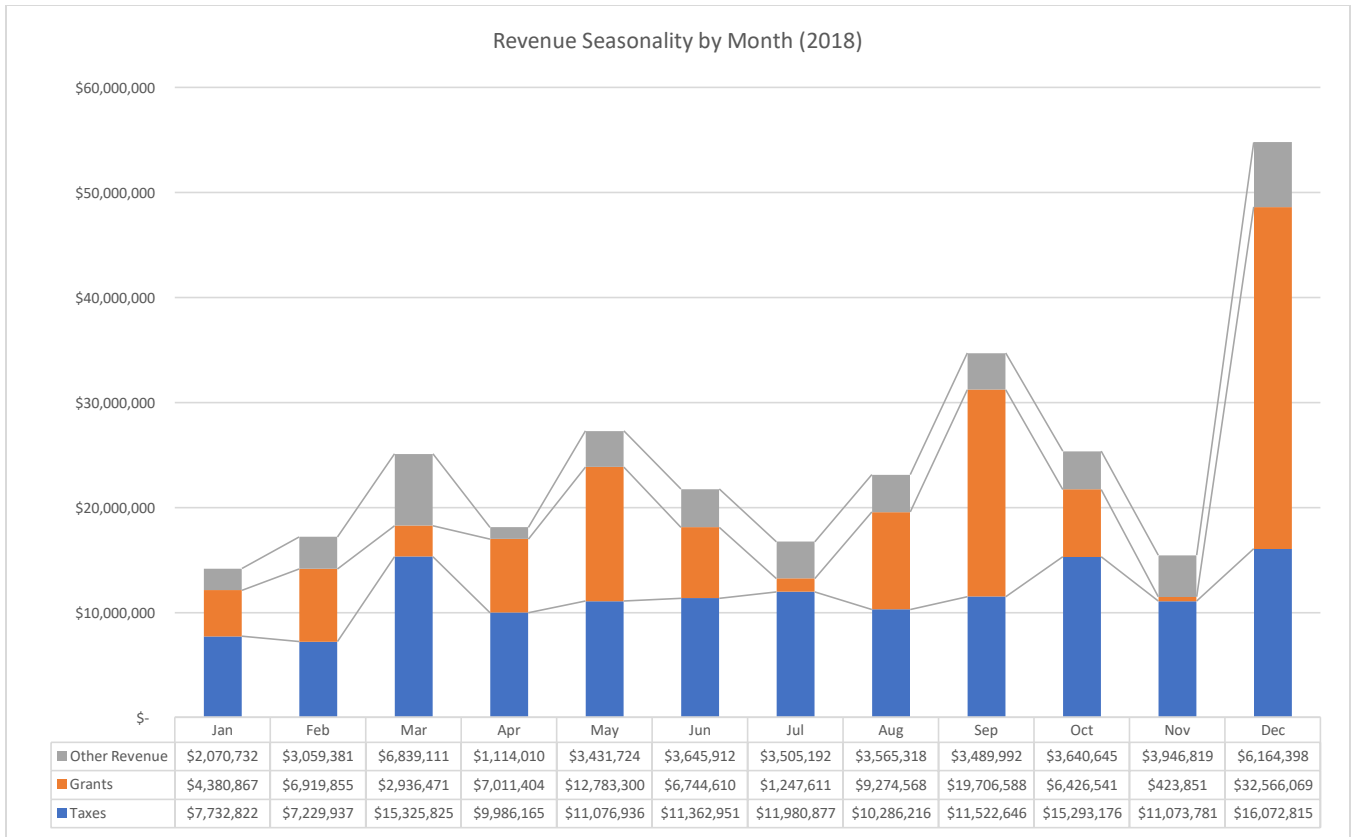


Figure 5 - Revenue Seasonality by Month (2018)

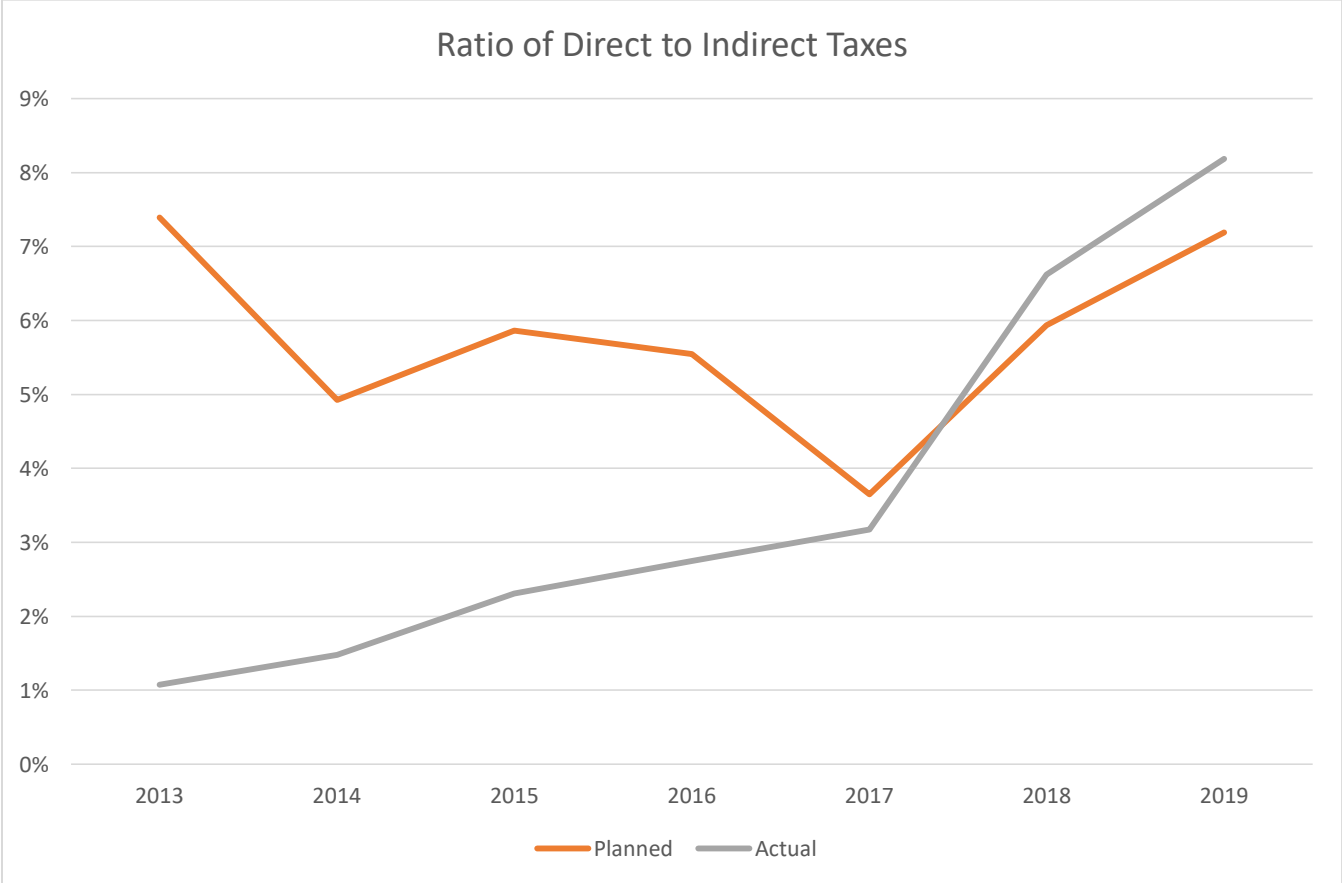
While the FGS will continue to be reliant on grant receipts from international organizations, the Government has made a considerable effort to improve domestic revenue collections, which are accounting for an increasing share of Government aggregate revenue as demonstrated in Table 1 above. Indeed, since 2017, the share of aggregate revenue coming from grants receipts has decreased by nine percent, pointing to a significant improvement in mobilizing domestic revenues and decreasing the FGS’s dependency on foreign sources.

Table 2 - Composition of Own-source Revenues

Revenue Stream	2013	2014	2015	2016	2017	2018	2019
Taxes on International Trade and Transactions	85%	76%	64%	68%	68%	55%	47%
Sales of Goods and Services	6%	12%	26%	21%	21%	24%	33%
Taxes on Goods and Services	8%	6%	4%	9%	4%	12%	11%
Other Taxes	0%	4%	4%	0%	5%	4%	5%

Contrary to popular perception, this improvement in domestic revenue mobilization has not entirely been driven by increases in taxes on international trade. As Table 2 above demonstrates, this revenue source has been declining as a share of Government own-source revenue between 2017 (68% of total own-source revenue) and 2019 (47% of total own-source revenue). This trend is positive from an economic perspective as taxes on international trade are widely understood to have distortionary effects – that is, they disproportionately increase the price of imported goods which most Somali citizens rely on and as such reduce their purchasing power. Instead, over the past three-year period, the FGS has made a concerted effort to increase the share of own-source revenue accruing from the sales of public goods and services, particularly through harbor fees, telecommunication spectrum fees, fisheries licenses, and overflight fees.

These efforts have also resulted in an increasingly pro-poor tax regime. The ratio of direct to indirect taxes is used globally as a measure of the pro-poor nature of a Government’s tax regime. Direct taxes, such as taxes on individual and corporate income, take into account the individual circumstances of taxpayers. Conversely, indirect taxes, such as taxes imposed on goods and services, do not consider individual taxpayer circumstances. As such, an increase in the ratio of direct-to-indirect taxes. As Figure 6 below demonstrates, annual appropriations passed between 2013 and 2016 showed a concerning trend, with an increased reliance on indirect taxes planned for in the Government’s Budget. Since 2017, however, FGS revenue collection plans have been purposively designed to reduce the reliance on indirect taxes, which adversely affect the country’s poor, and the results of this are evident in the marked increase in the ratio trend for actual revenue collections



between 2017 and 2019.

Figure 6 - Ratio of Direct to Indirect Taxes

There is, however, considerable room for improvement with regards to domestic revenue mobilization. While tax-to-GDP ratios have grown from 1.22 percent to 1.91 percent between 2013 to 2019, this ratio is still significantly below international averages. This ratio is of particular concern, as the IMF has identified that countries where tax-to-GDP ratios are below 12.75% tend to have sub-optimal economic outcomes as Government's tend to be increasingly reliant on volatile donor funding and unable to respond to macroeconomic, climate-related, and health shocks without further increasing their reliance on foreign revenue

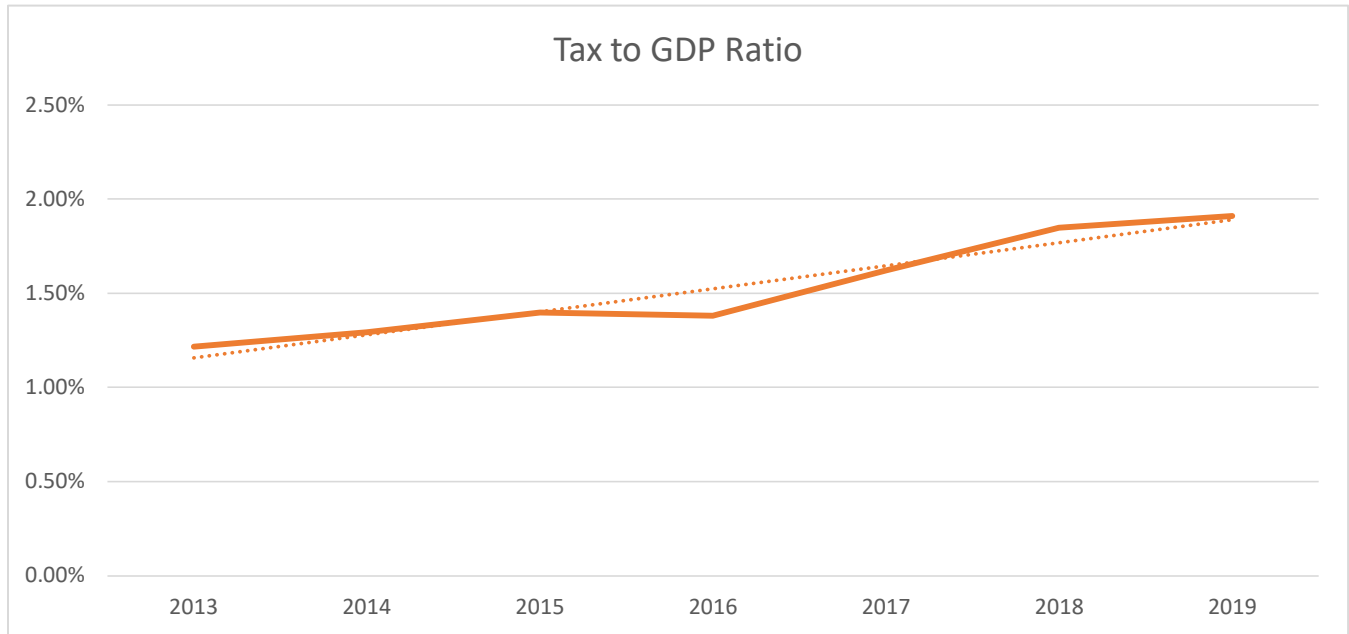


Figure 7 - Tax to GDP Ratio

sources.

3. EXPENDITURE

The increase in revenue receipts described in Section 2 above has translated into increased Government spending over the period, as demonstrated in Figure 8 below.

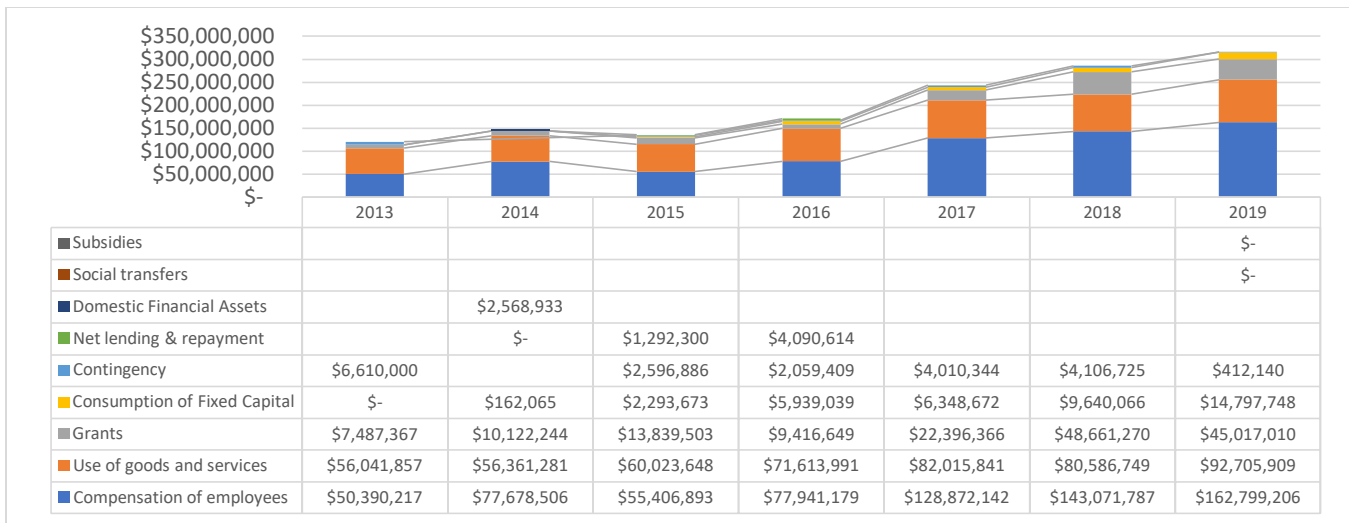


Figure 8 - Actual Expenditure, FY2013 – 2019

When preparing annual budgets, expenditure is largely concentrated in compensation of employees, accounting for 48 percent of the Government’s planned expenditure in 2019.

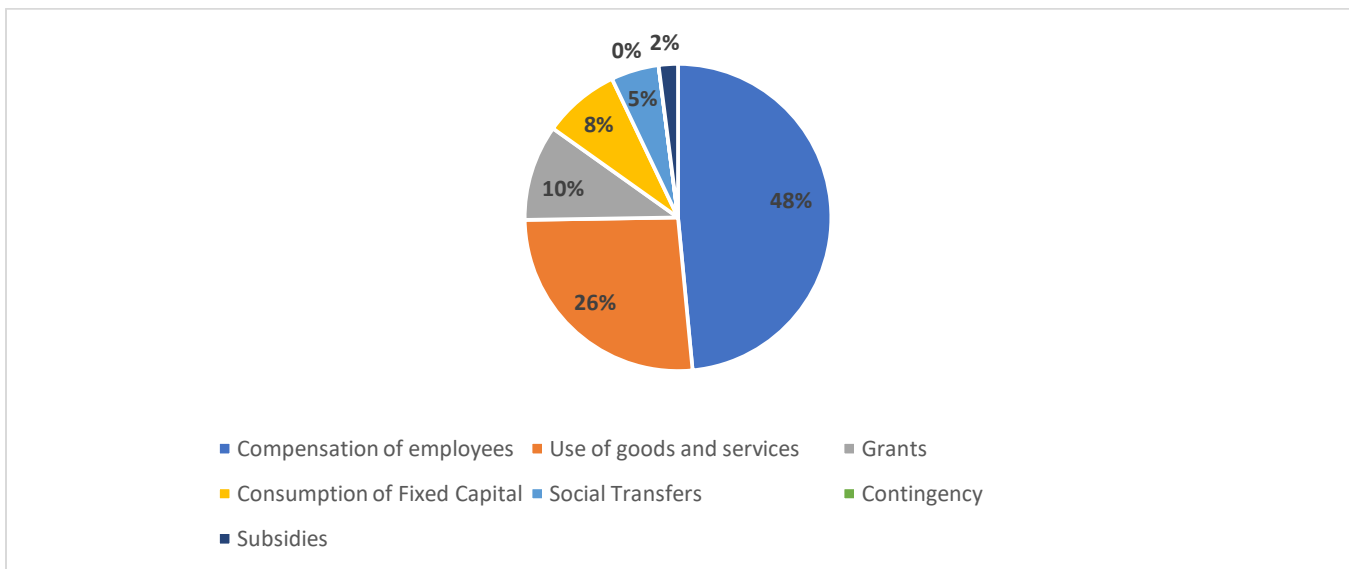


Figure 9 - Expenditure Composition in the 2019 Approved Budget

Underperformance in revenue collections, identified as due to shortfalls in anticipated grant receipts in Section 2 above, has however meant that a greater than anticipated share of Government spending has been spent on compensation of employees (52 percent of actual expenditure compared to 48 percent of the planned budget), use of goods and services (29 percent of actual expenditure compared to 26 percent of the planned budget), and grants to the Federal Member States (14 percent of actual expenditure compared to 10 percent of the planned budget). This has largely come at the expense of capital expenditures, which accounted for only five percent of actual government spending compared to eight percent of planned expenditure and the crowding out of all other types of government spending.

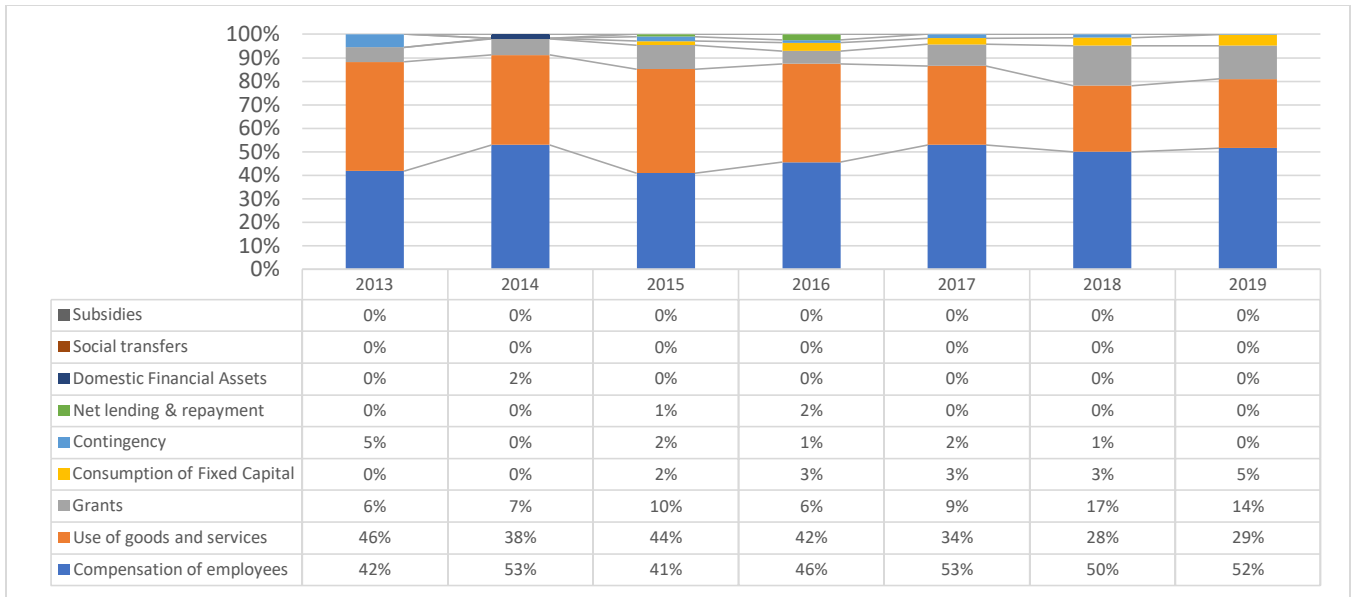


Figure 10 - Actual Expenditure Composition

The seasonality of revenue discussed in Section 2 above has a significant impact on Government’s expenditure, as expenditures are closely aligned to revenue receipts and as such are highly concentrated in the final quarter of the financial year and increasingly in December as shown in Table 3 below.

Table 3 - Expenditure Seasonality by Month, in US Millions (2019)

Expenditure Item	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sept	Oct	Nov	Dec
Compensation of Employees	4.1	10.6	14.5	13.3	14.4	12.5	12.7	15.7	17.7	12.7	6.7	27.9
Use of Goods and Services	0.3	2.9	7.4	6.5	6.1	7.1	6.4	6.9	7.6	8.4	7.6	25.5
Grants	1.6	3.0	2.2	3.9	3.7	2.4	4.3	3.7	2.8	6.8	2.6	8.0
Consumption of Fixed Capital	0.0	0.3	1.4	0.8	0.3	0.9	0.4	0.7	5.2	0.4	1.2	3.2
Contingency	0.0	0.03	0.0	0.2	0.0	0.0	0.005	0.02	0.0	0.0	0.0	0.1

Given that the FGS is currently in its start-up phase, still working on developing a public administration, and that the country’s security situation necessarily requires a significant investment in maintaining armed forces, the concentration of spending on compensation of employees is not surprising and is broadly in-line with a benchmark level of no more than 50 percent of total government spending being allocated to compensation of public employees.

Analyzing expenditure by sector and function, however, is more relevant in the case of Somalia for understanding improvements in spending trends over time. For accounting purposes, the FGS groups its MDA’s into four functional sectors: Administration, Security, Economic, and Social. As shown in Figure 11 below, spending in the Administrative Sector – which includes core Executive, Legislative, and Judicial MDAs, decreases

as a share of total spending between 2013 and 2017, and has been fairly constant since. Slight decreases in spending in the security sector since 2017, have allowed for a notable increase in social sector spending, which includes key citizen services like health and education.

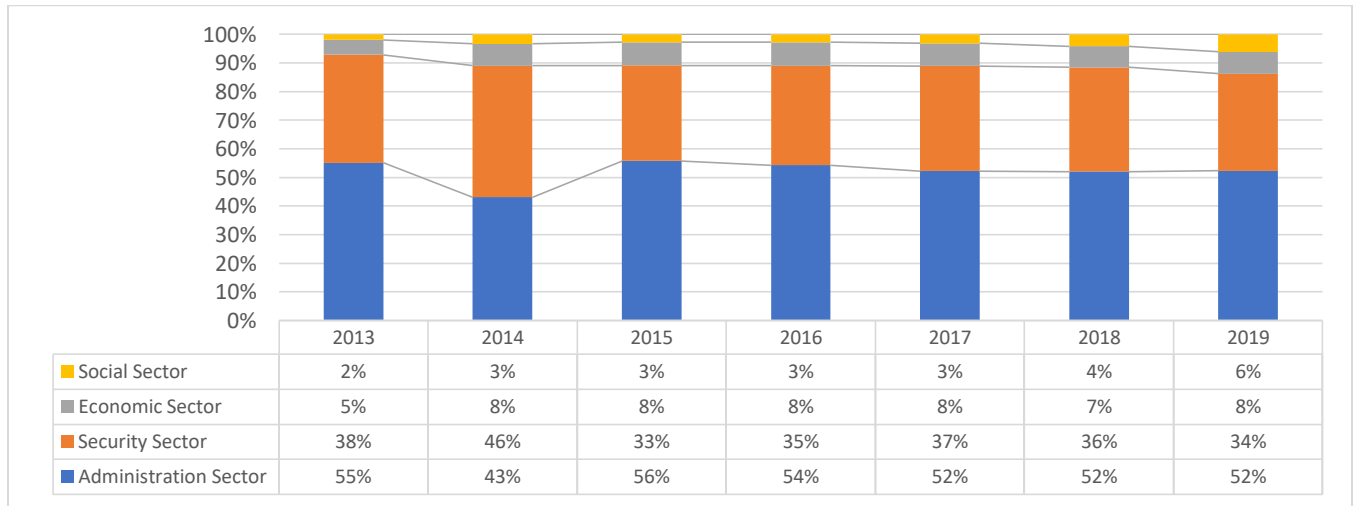


Figure 11 - Actual Expenditure by Sector

Cross-classifying sectoral spending with the economic purpose of spending allows us to demonstrate that the majority of Government’s spending on compensation of employees is devoted to maintaining the Government’s army and police forces, a critical asset to promoting a peaceful, secure, and prosperous Somalia as show in Figure 12 below.

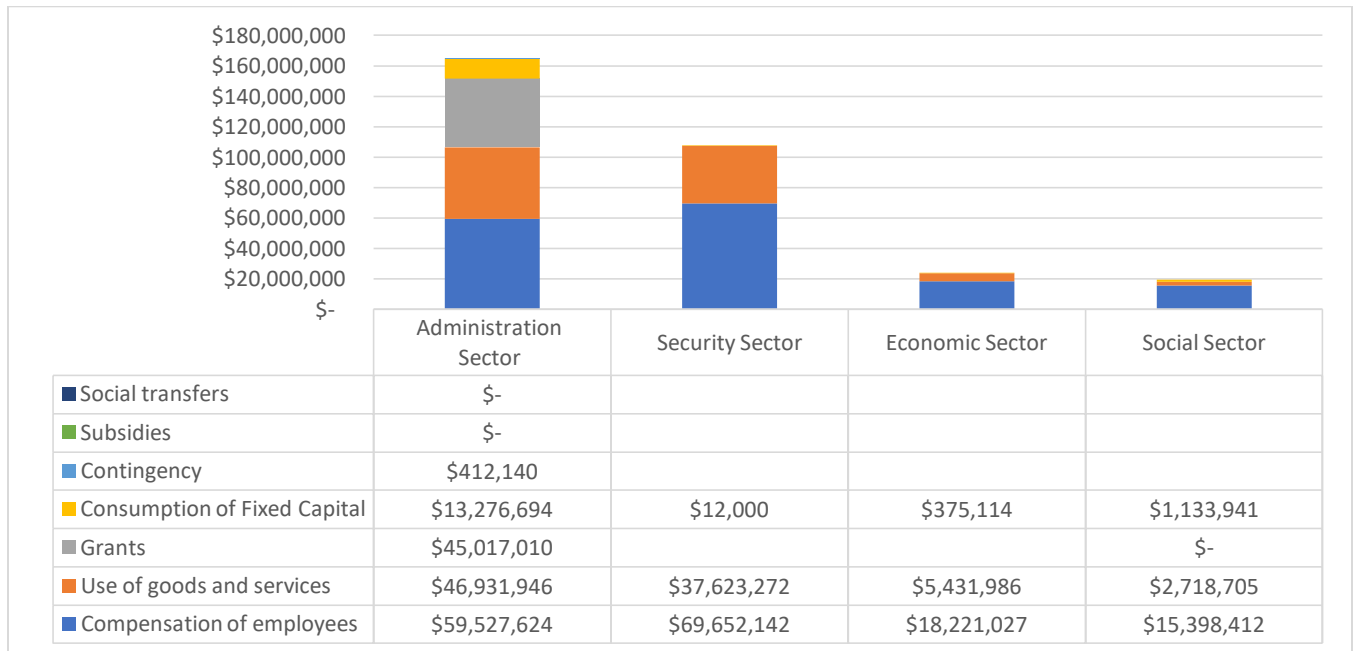
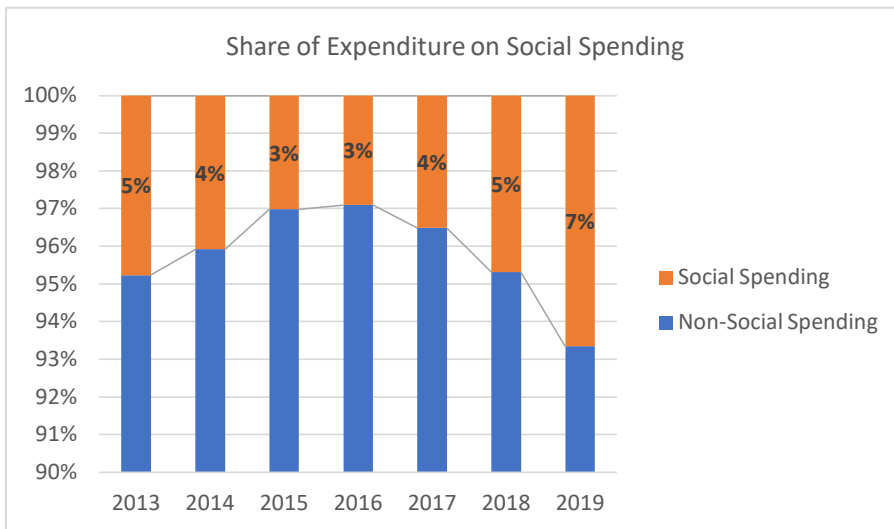


Figure 12 - Cross-classification analysis of Actual Expenditure, by Sector and Economic Type (2019)

The increase in social sector spending is even more apparent when the system of Classification of Functions of Government (COFOG) developed by the UN and IMF is used to classify spending.



As Figure 13 adjacent shows, the share of total spending classified as social spending (defined as health, education, housing and community amenities, and social protection) decreased from five percent in 2013 to three percent in 2016. Since 2017, however, this trend has reversed, with nearly seven percent of total government spending in 2019 being classified as social spending-oriented using COFOG.

Figure 13 - Share of Expenditure on Social Spending

While the Government remains committed to increasing allocations to these sectors, it is important to be realistic in our aspirations. Based on a benchmarking exercise analyzing 47 fragile, low income, and OECD countries we find that FGS spending is on a trend path towards converging with its peer group fragile countries, where government expenditure is primarily concentrated in collective consumption public goods and services including security and general public services. As such, while future budgets will aim to achieve a similar profile to our peer fragile and low-income countries, it is neither likely nor realistic to expect spending to mirror OECD economies until significant structural economic transformations leading to an amelioration in incomes have occurred.

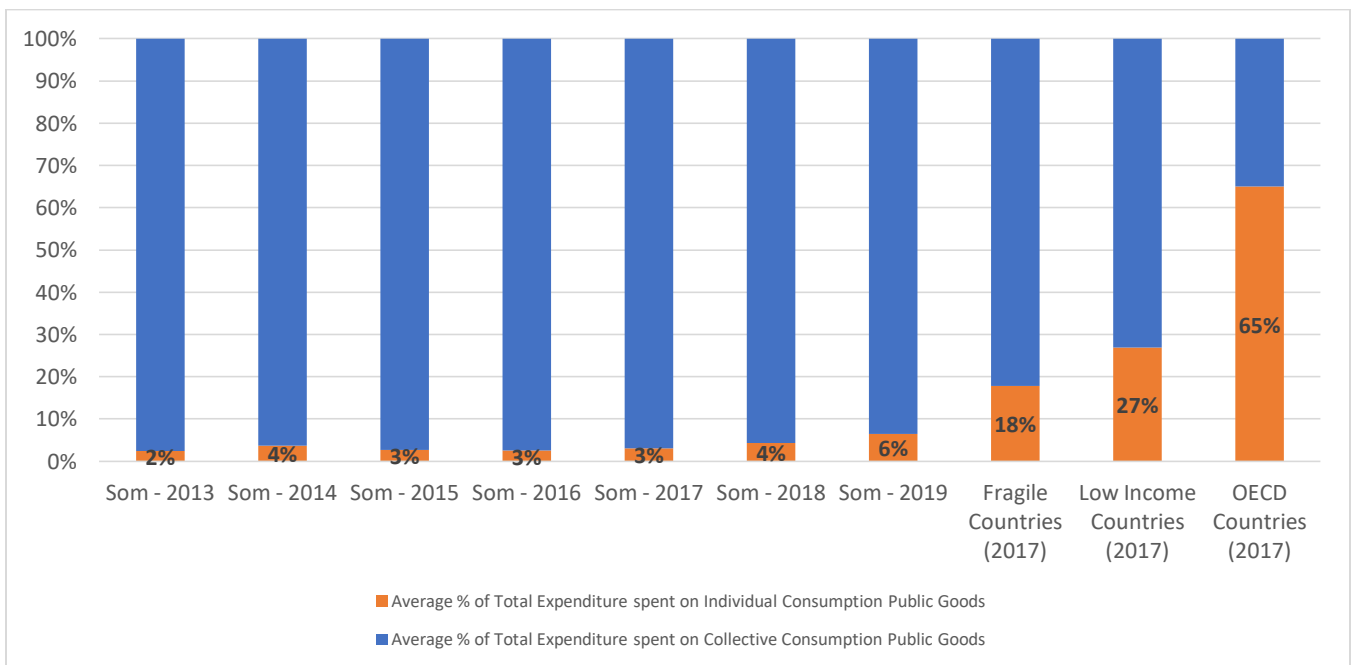


Figure 14 - Shares of total expenditure compared to Fragile, Low Income, and OECD Countries

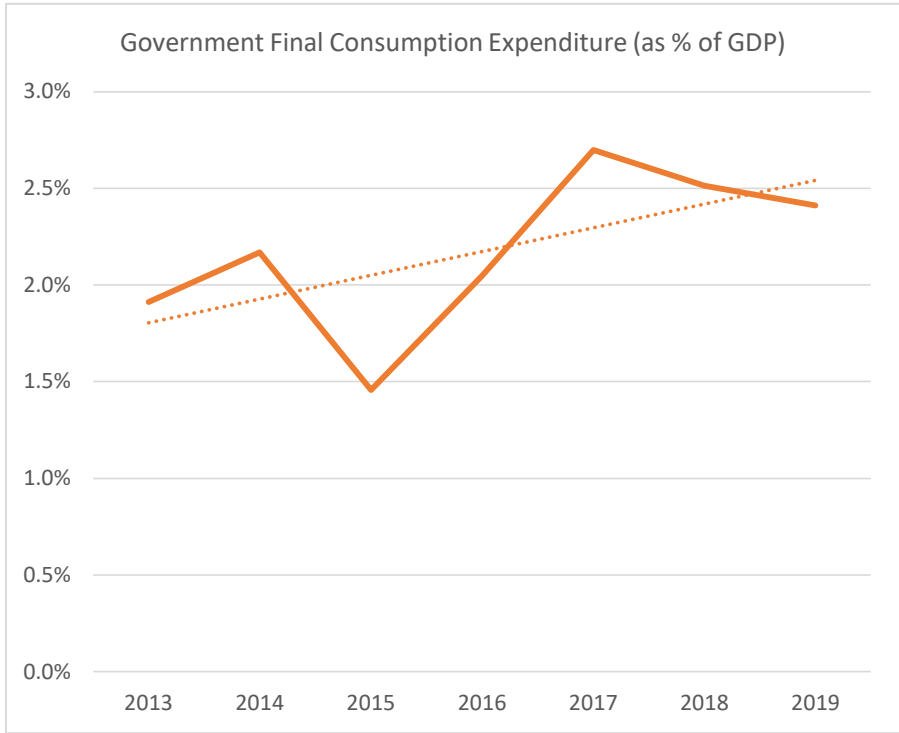


Figure 15 - Government Final Consumption Expenditure

In order to achieve this improvement in increased social spending, however, is a long-term objective. Currently, total government final consumption expenditure accounts for only 2.4 percent of GDP. While this has risen somewhat from 1.9 percent in 2013, it remains significantly below the world average of 16 percent of GDP and as such suggests that the Government plays a very small role currently in Somalia's overall economic activity.

4. LOOKING FORWARD

The analysis in Sections 2 and 3 above give grounds for considerable optimism for Somalia's prospects of post-conflict recovery and development. Revenue collections have more than doubled since the establishment of the Federal Government, and, since 2017, show signs of a clear improvement in mobilizing domestic revenues in a pro-poor manner. On the expenditure side, while obligations to the security sector will continue to account for a significant share of government total spending, there is evidence to suggest that an increased share of government spending is being allocated to social spending sectors. Looking forward, the COVID-19 pandemic will seriously curtail the country's growth prospects. Furthermore, political uncertainty in the lead up to the elections coupled with continuing insecurity signal a slow return to peace in many parts of the country and a profound draft on the country's economic growth and development. To ensure that the remarkable progress described above is not reversed, the Ministry of Finance makes the following recommendations:

- 1. Prioritization of IMF ECF/EFF structural benchmarks:** As a critical requirement to achieving debt relief under the enhanced Heavily Indebted Poor Countries initiative, the new IMF Extended Credit Facility/Extended Fund Facility (ECF/EFF) program requirements the Federal Government to undertake a series of critical reforms targeting domestic revenue mobilization, public financial management, debt management, petroleum, anti-money laundering and counter-terror financing, governance and corruption, sustainable growth and development, human capital development, improving macroeconomic and financial data, and social sector reforms. Completion of these structural benchmarks and completion point triggers are critical to ensuring Somalia's debt relief, creating the fiscal space needed to begin addressing the complex policy challenges facing the country;
- 2. Use of Country Systems:** Important strides have been made towards increasing the use of country systems by development partners, in itself a reflection of improvements made by Government in reforming its public financial management. Historically, humanitarian assistance has tended to bypass country systems and this pandemic poses a serious risk to this end. Development partners must continue to support the development of country systems and continue to increase the share of their developmental expenditure using these arrangements;
- 3. Capacity building for Public Financial Management:** Further reform will need to be supported by effective and efficient technical public financial management capability, at both Federal and sub-national levels. Reforms to date have, in no small part, been the result of fruitful partnerships with the World Bank, the IMF, and the European Union. That said, considerable support is still necessary to further improve diversification of the tax base, mobilize domestic revenue, and support robust, transparent, public financial management. Within the Federal Ministry of Finance, the MoF has prioritized the development of public assets information and debt statistics, which will be used to inform further updates to this report;
- 4. Security Sector Reform:** The security sector will continue to account for a significant share of Government's total expenditure throughout the post-conflict recovery period. As such, it is critical that security reforms are implemented alongside public financial management reforms to ensure accountability and transparency in this sector;
- 5. Government coordination:** From 2020 onwards, the FGS has committed to moving from a line-item annual budgeting process towards program-based multi-year expenditure planning. This reform is expected to re-orient government strategy away from inputs and towards results. This reform will be challenging, and will require a concerted effort by all MDAs to collaborate more closely with the Ministry of Finance to ensure that annual plans and in-year spending are driven by strategic priorities enshrined in the Government's National Development Plan.

