FEDERAL REPUBLIC OF SOMALIA
MINISTRY OF FINANCE

GOVERNMENT FINANCIAL STATISTICS (GFS) ANALYTICAL REPORT

2016-2021 PERIOD

July 2022

For additional information or queries relating to this report, please contact: *Ministry of Finance, Economic Policy and Planning Department*

economic.policy@mof.gov.so

mof.gov.so

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Executive Summary

The Federal Government of Somalia has embarked on a serious of ambitious public financial management and public administration reforms to develop modernized and internationally recognized institutions since its establishment in 2013. The accelerated pace of these reforms from 2016, 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 is the second report by the Ministry of Finance's Economic Policy and Planning Department analyzing Government Financial Statistics data from FY2016 to FY2021. The first report covered the FY2013-FY2019. The Economic Policy and Planning Department closely works with the newly established Somalia National Bureau of Statistics to integrate this analysis with broader economic data in order to provide a holistic snapshot of Somalia's economic and fiscal trajectory. The report is deemed significant to our international partners that include the World Bank, the International Monetary Fund, the European Union, the African Development Bank, and the Islamic Development Bank, among others, in informing socioeconomic policies.

Regarding government revenues, aggregate revenue receipts have 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 significant, 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, there has been a clear increase in the total share of government spending on social goods including health, education, housing and community amenities, and social protection. Nonetheless, government spending on these social goods remain considerably lower than internationally comparable levels.

Looking forward, the COVID-19 pandemic will continue to pose a serious risk to these improvements being witnessed, particularly if development partners choose 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.

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1 Introduction

Nearly ten years (10) have elapsed since the establishment of the Transitional Federal Government of Somalia in August 2012, a critical milestone in a conflict stricken country since the fall of the Federal Government in 1990. 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 people. Since 2016, significant 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 like the African Development Bank (AfDB), the World Bank (WB) and the International Monetary Fund (IMF).

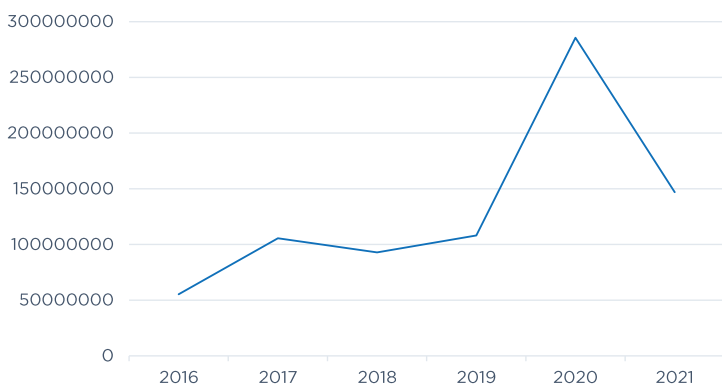
Against this backdrop, this report provides a high-level overview of the FGS's economic and financial performance from 2016 to 2021. In the interests of promoting fiscal transparency, the report draws on data publicly available from the Ministry of Finance's website, which can be downloaded in a tab-separated values format (.tsv) for the reader's own analysis. The 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. In that regard, readers are advised that final figures may be revised from the time of publication of this document and thus may 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 henceforth.

2 Revenue

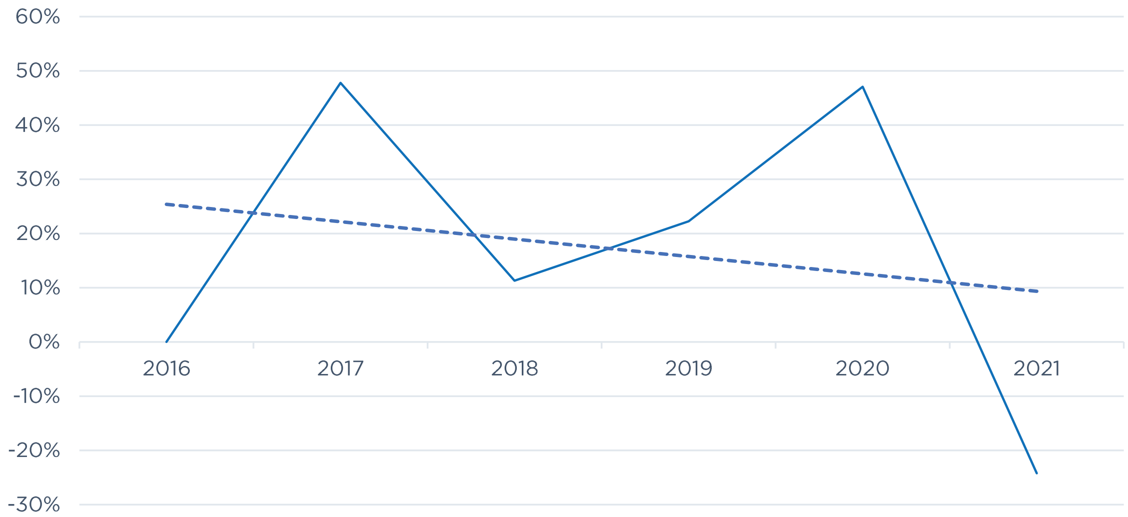
Total revenue receipts have grown by over 224 percent between 2016 and 2021, growing from a total of $167.9million to over $376.5 million during the period. This sub-section decomposes these revenue receipts into tax, grants, and non-tax own-source receipts in order to analyze drivers of growth and concludes 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 promising trend was evident as the FGS's aggregate revenue receipts grew at a fluctuating rate of over ten percent annual year-on-year growth between 2016 and 2019, and 2020 at its peak but dropped in 2021 due to low expectation of grants as evidenced in Figure 2.

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



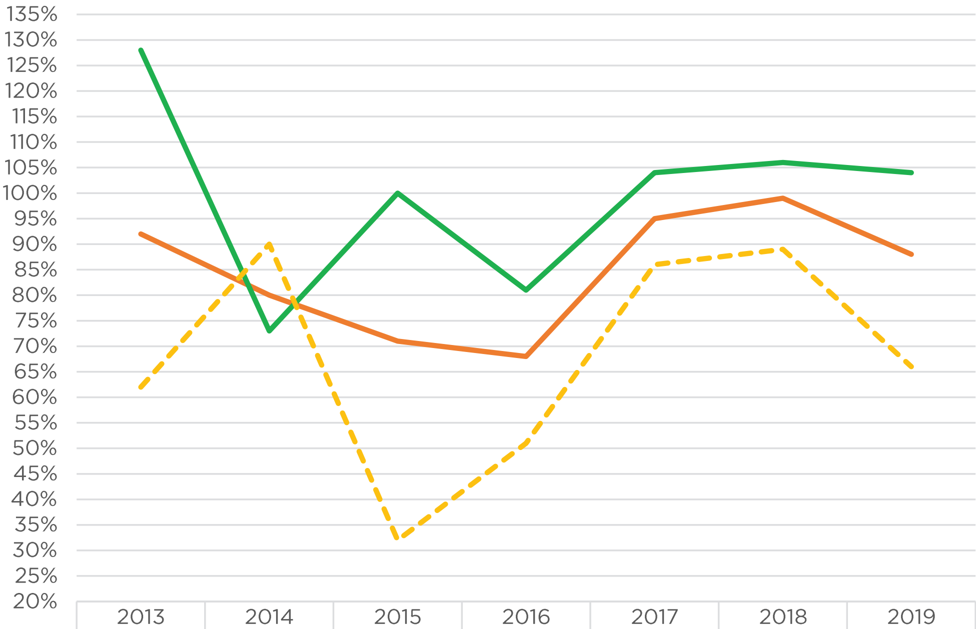
Decomposing aggregate revenue receipts into the key revenue types: taxes, grants, and other non-tax revenues paints a positive picture of the FGS's performance; between financial year 2017 and 2019, the share of government revenue accuring from grants receipts (from foreign governments and international bi-lateral and multi-lateral organizations) is decreasing (Table 1). 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 Sources	2016	2017	2018	2019	2020	2021
Grants	33%	43%	34%	32%	57%	39%
Other revenue	14%	12%	16%	22%	14%	18%
Taxes	53%	45%	50%	46%	28%	43%

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 2021 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 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/ Revenue collection as a percentage of the Approved Estimate



	2013	2014	2015	2016	2017	2018	2019
Aggregate	92%	80%	71%	68%	95%	99%	88%
Own-source	128%	73%	100%	81%	104%	106%	104%
Grants	62%	90%	32%	51%	86%	89%	66%

The underperformance in grant receipts is not necessarily due to funds not being released by donors in a timely manner, but often there are conditionalities and expected reform actions the FGS must complete and present 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 becomes an inherent challenge. As Figures 4 – 5 demonstrate, there is a clear clustering of grants receipts in the first quarter, although in the last three years this has been particularly concentrated in December, this trend is particularly promising 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 (2020)

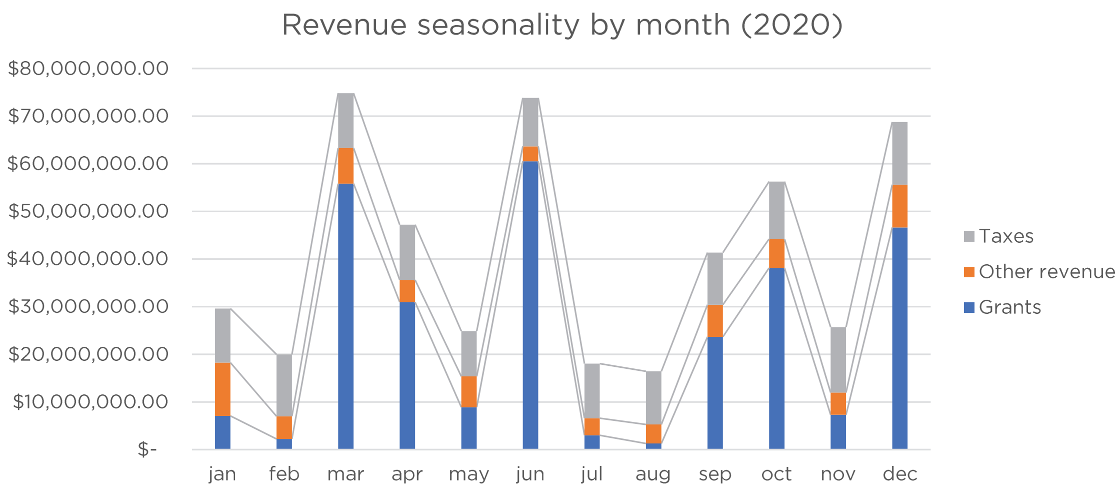
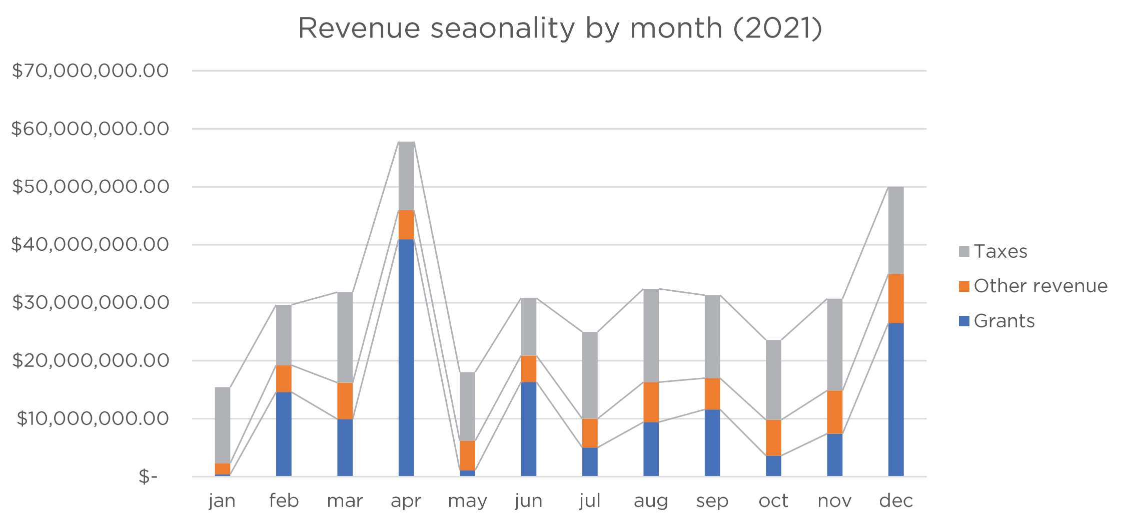


Figure 5 - Revenue Seasonality by Month (2021)



While the FGS will continue to be reliant on grant receipts from international organizations, the Government has made a great effort to improve domestic revenue collections, which are accounting for an increasing share of Government aggregate revenue as demonstrated in Table 1. 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.

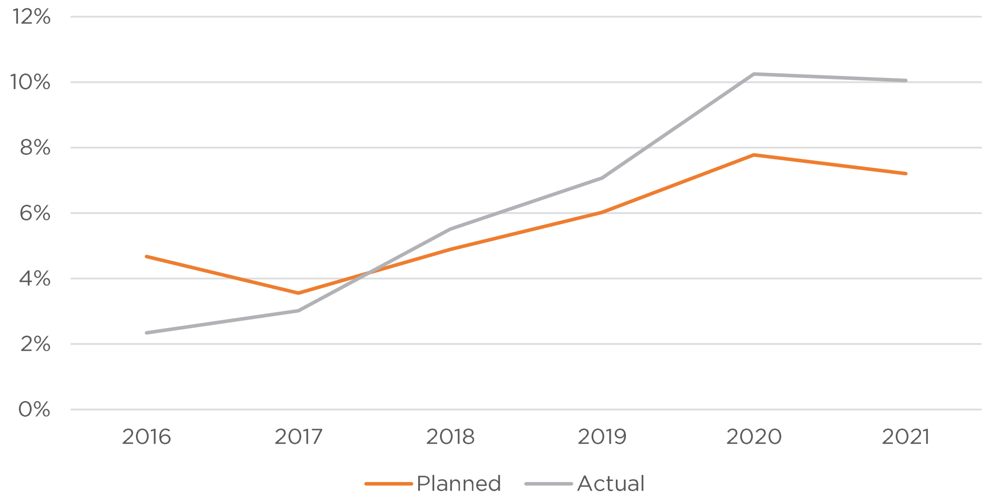
Table 2 - Composition of Own-source Revenues

Revenue stream	2016	2017	2018	2019	2020	2021
Taxes on goods and services	3%	6%	13%	11%	11%	11%
Taxes on international trade and transactions	69%	67%	57%	49%	47%	51%
Sales of goods and services	22%	22%	25%	34%	37%	31%
Other taxes	6%	5%	5%	5%	6%	7%

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 demonstrates, this revenue source has been declining as a share of Government own-source revenue between 2016 (69% of total own-source revenue) and 2021 (51% 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.

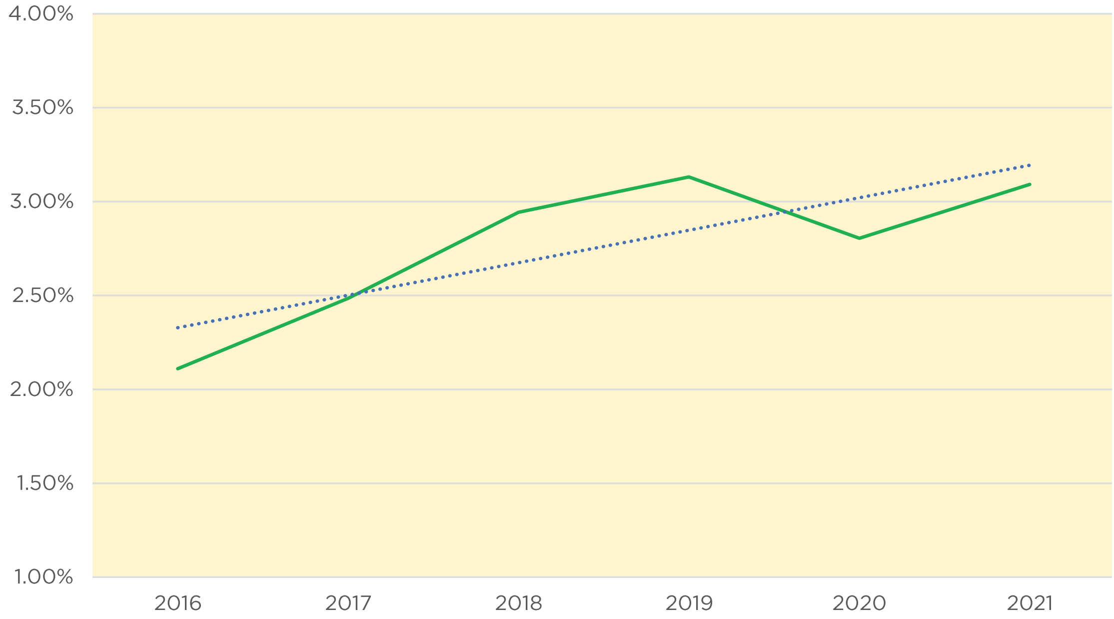
These efforts have also resulted in an increasingly pro-poor tax regime. The ratio of direct to indirect taxes is used globally as a measure of the pro-poor nature of a Government's tax regime. Direct taxes, such as taxes on individual and corporate income, take into account the individual circumstances 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 demonstrates, the 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 2.22 percent to 3.32 percent between 2016 to 2021 (Figure 7), 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 sources.

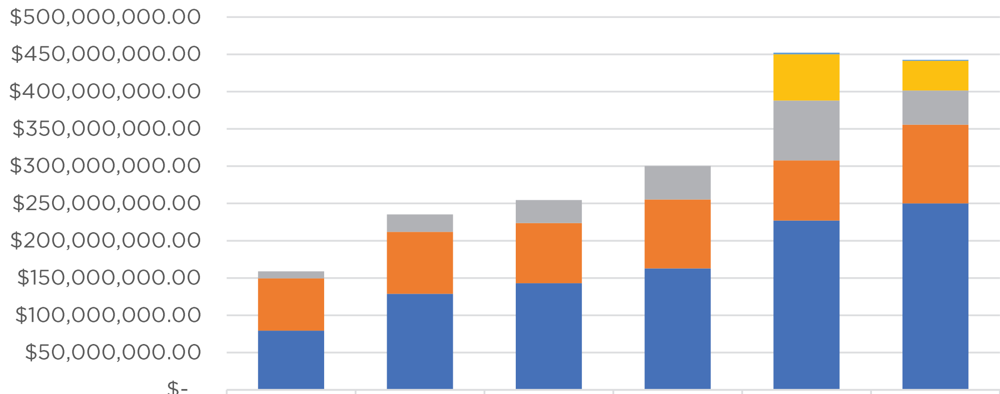
Figure 7 - Tax to GDP Ratio



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.

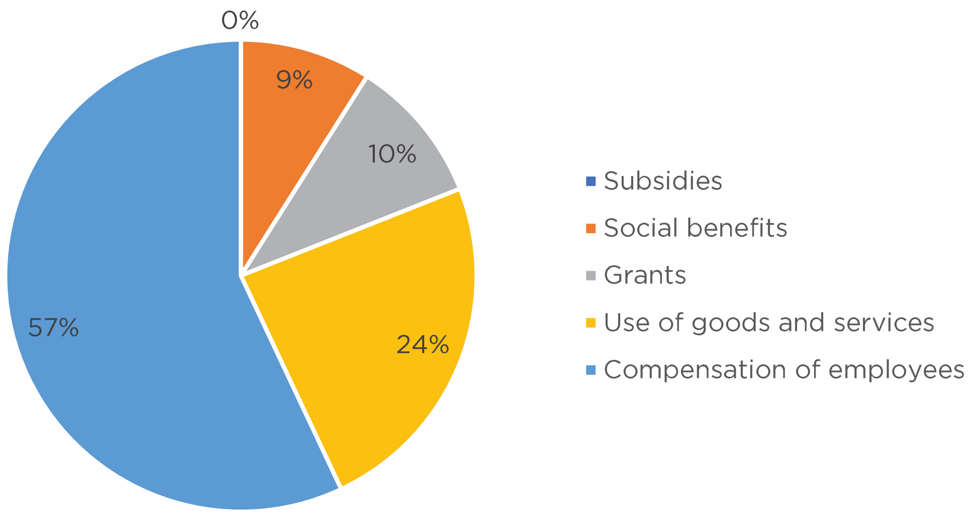
Figure 8 - Actual Expenditure, FY2016 – 2021



	2016	2017	2018	2019	2020	2021
Subsidies				$-	$2,161,91	$1,271,69
Social benefits				$-	$62,135,1	$39,864,8
Grants	$9,416,64	$23,397,5	$30,837,5	$45,007,4	$80,283,3	$45,850,5
Use of goods and services	$70,287,3	$82,947,5	$80,639,5	$92,393,0	$80,696,0	$105,536,
Compensation of employees	$79,314,0	$128,860,	$143,071,	$162,862,	$227,014,	$250,098,

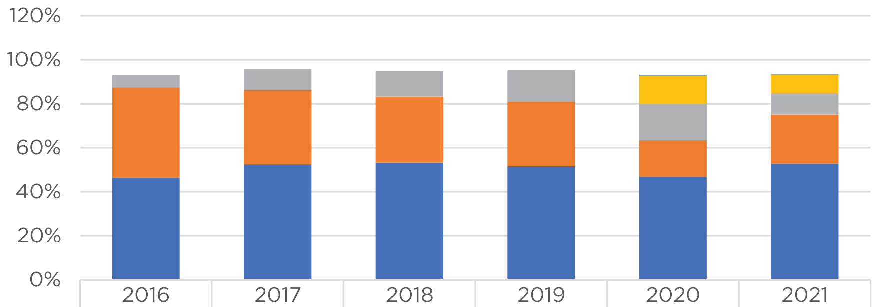
When preparing annual budgets, expenditure is largely concentrated in compensation of employees, accounting for 57 percent of the Government's planned expenditure in 2021.

Figure 9 - Expenditure Composition in the 2021 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 (57 percent of actual expenditure compared to 48 percent of the planned budget), use of goods and services (24 percent of actual expenditure compared to 26 percent of the planned budget), and grants to the Federal Member States (10 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



	2016	2017	2018	2019	2020	2021
Subsidies	0%	0%	0%	0%	0%	0%
Social benefits	0%	0%	0%	0%	13%	8%
Grants	6%	10%	11%	14%	17%	10%
Use of goods and services	41%	34%	30%	29%	17%	22%
Compensation of employees	46%	52%	53%	52%	47%	53%

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.

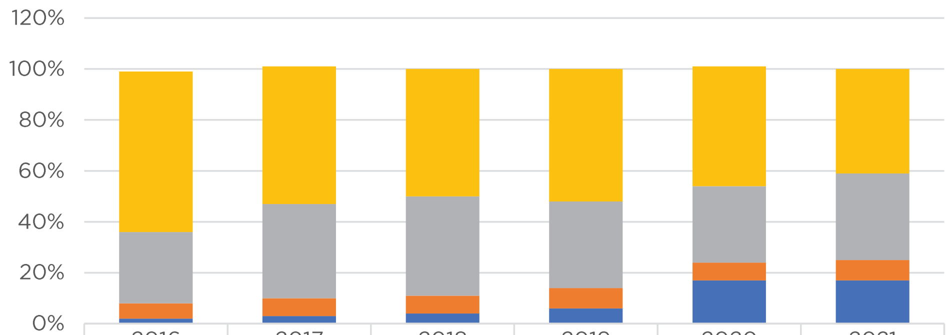
Table 3 - Expenditure Seasonality by Month, in US Millions (2021)

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, spending in the Administrative Sector – which includes core Executive, Legislative, and Judicial MDAs, decreases as a share of total spending between 2016 and 2021(from 63% to 41%). Slight increases in spending in the security sector since 2016, have allowed for a notable increase in social sector spending (from 2% to 17%), which includes key citizen services like health and education.

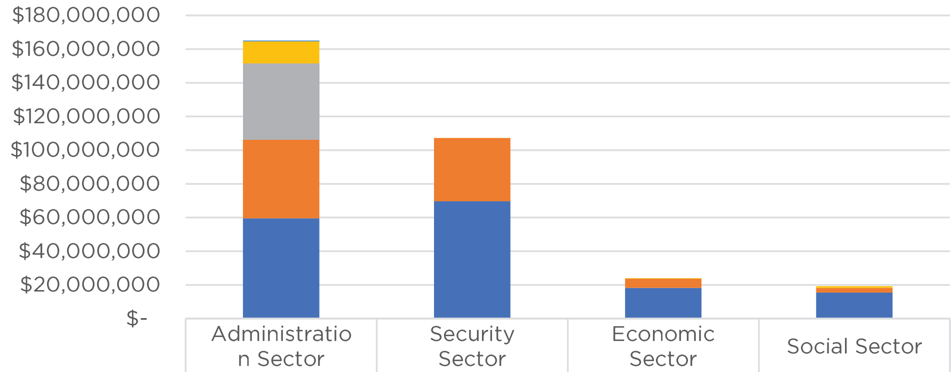
Figure 11 - Actual Expenditure by Sector



	2016	2017	2018	2019	2020	2021
Adminstration	63%	54%	50%	52%	47%	41%
Defense and security	28%	37%	39%	34%	30%	34%
Economic Sector	6%	7%	7%	8%	7%	8%
Social Sector	2%	3%	4%	6%	17%	17%

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.

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

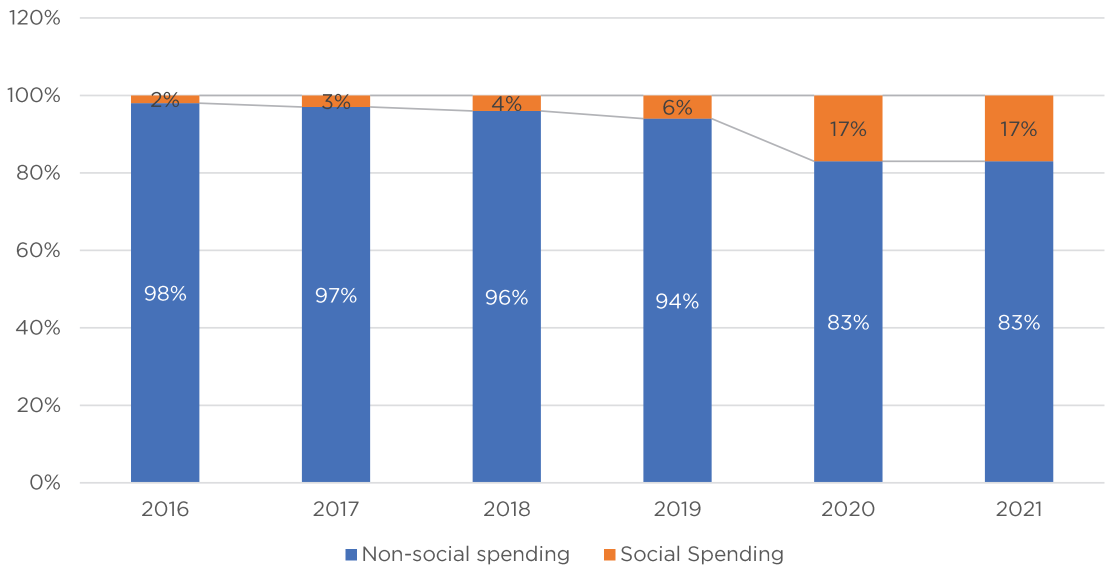


	Administration Sector	Security Sector	Economic Sector	Social Sector
Social transfers	$-			
Subsidies	$-			
Contingency	$412,140			
Consumption of Fixed Capital	$13,276,694	$12,000	$375,114	$1,133,941
Grants	$45,017,010			$-
Use of goods and services	$46,931,946	$37,623,272	$5,431,986	$2,718,705
Compensation of employees	$59,527,624	$69,652,142	$18,221,027	$15,398,412

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) increased from two percent in 2016 to seventeen percent in 2021. This is a considerable effort on the part of the government to increase in social spending to improve the well-being of its citizens.

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

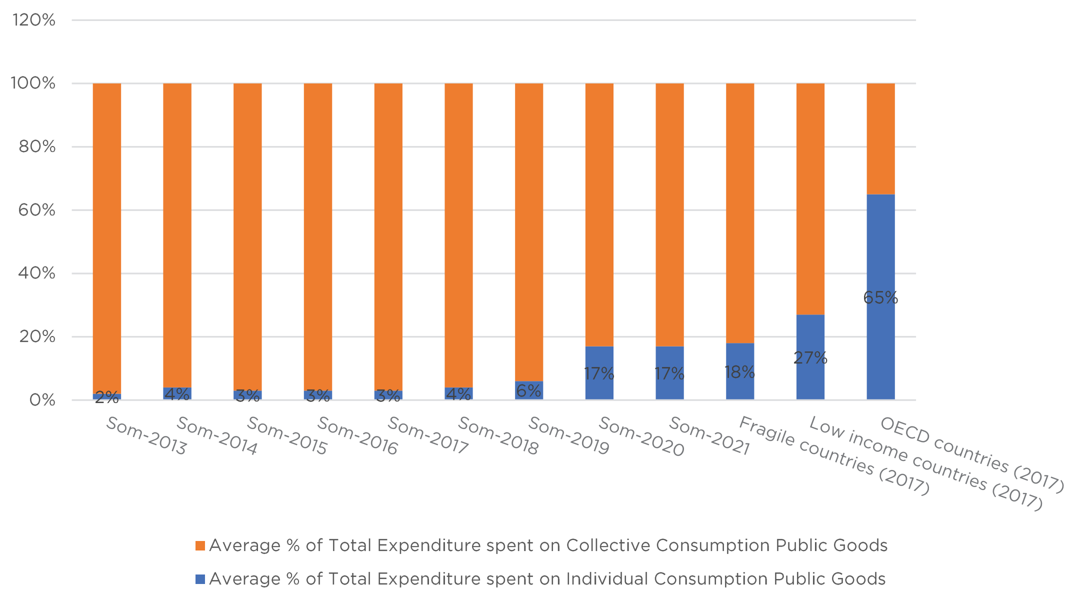
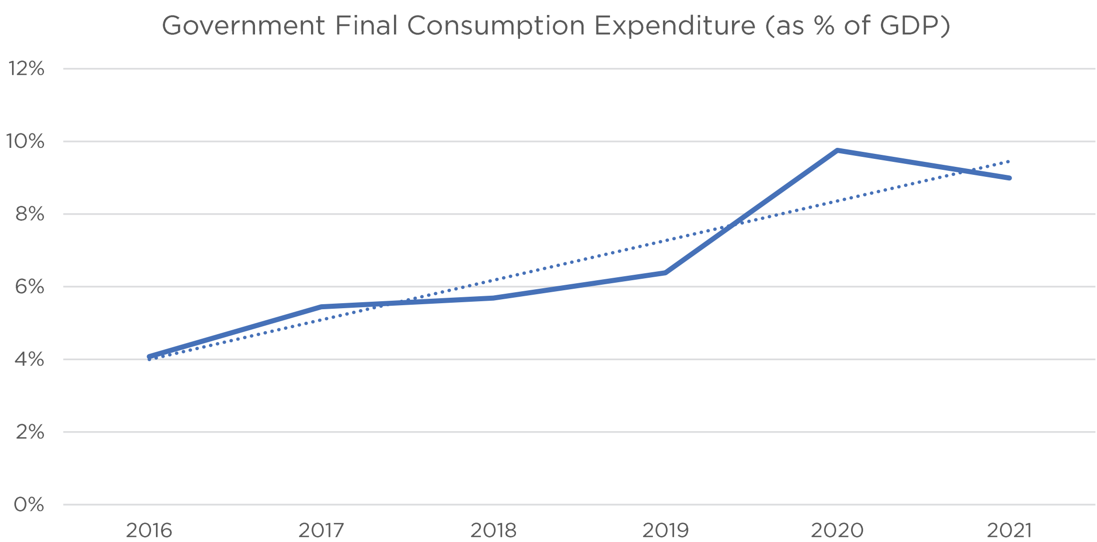


Figure 15 - Government Final Consumption Expenditure (as % of GDP)



Over the years, the government has been recording an upward trajectory of the government final consumption expenditure as % of GDP. In 2020, the FGS recorded the highest final consumption expenditure to GDP of over 9%. As for year 2021, total government final consumption expenditure accounts for only 8.7 percent of GDP. While this has risen somewhat from 4.0 percent in 2016, 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. In order to achieve this improvement in increased social spending, substantial growth in government revenue supported by significant economic growth, increased in own government revenues and widened tax base is required. However, this ambition is a long-term objective.

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, data 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 surrounding transfer of powers after May 15th 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. **Own revenue creation:** Considering rising government expenditures, the FGS to enhance the generation of own revenue via domestic revenue mobilization reforms. The reforms should target the revitalization of agriculture sector that accounts over 65% of the country's GDP. The reforms in the agricultural sector to target livestock industry, fishing, cereal crops (maize and sorghum), commercial crops (banana, sugar cane, rice grape fruits among other crops). The support of the agricultural sector to revolve around the expansion of irrigation facilities in the country, provision of subsidized livestock and farm input and creation of competitive market system of agricultural related products. In addition, the FGS to support the industrial and service sector by creating a secure and conducive working environment, infrastructural enhancement in terms of transport, telecommunication and energy development.

2. **Taxation:** As a means of raising government revenues, the taxation system in the country to focus more on expanding tax base, reducing tax levied on international trade with aim of promoting foreign direct investments into the country. Uncheck taxation on international trade increases the price of imported goods into Somalia reducing purchasing power of ordinary Somali citizens. The FGS to also promote favourable tax regime that is considerate to local business enterprises, factors of production and ordinary Somali citizens. Moreover, the taxation for big corporations including telecommunication, energy corporations among others to be increased up from the current 5%. Increasing tax on big corporations will cushion individuals against high taxations and also help in augmenting government own revenues.

3. **Government spending:** The GFS analytical report has indicated government spending heavily skewed to the compensation of employees particularly in the security sector. With increased government own revenue, government spending should target social goods including health, education, housing and community amenities, social protection, infrastructural particularly transport, telecommunication, energy, irrigation systems and agricultural product marketing channels.

4. **Aid and Grants:** The FGS has been more reliant on aid and grants form multilateral and bilateral organisations since the fall of the FGS in 1990. The FGS to reduce the reliance on aid and grants and refocus on the creation of her own revenue through economic growth reforms targeting the agricultural, industrial and service sectors as stated in first recommendation. Overreliance on aid and grants are more binding, restrictive and conditional that make the country more loyal to the donor with no or minimal room for the country to decide on their own socioeconomic destiny.

5. **MDAs coordination:** There is need to promote the efficient coordination of government functions with the aim of enhancing the delivery of public goods and services. Proper and efficient coordination of Ministry of Finance with other government Ministries, Departments and Agencies is key to the achievement of core government goals targeting socio, economic and political reforms. In addition, proper and efficient coordination among the MDAs is meant to enhance the proper channeling and use of government own revenues.

6. **Capacity building for Public Financial Management:** There is need for continuous technical training targeting public fund management through fund monitoring and evaluation systems aimed at ensuring proper channeling and use of donor funds and government funds. For donor funds, World Bank, the IMF, European Union, AfDB among other funders to closely monitor the utilization of funds or equipment donated with support from government and local communities. For government funds, political goodwill guided by transparency and accountability virtues are required in promoting the efficient beneficial channeling of the public funds.

7. **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.

8. **Somali National of Bureau of Statistics (SNBS):** The bureau to actively participate in collecting own socioeconomic and geopolitical data from the various data sources in the country. The other authorized organizations like the World Bank, IMF, AfDB and United Nations among other authorized organizations may also independently collect the socioeconomic and geopolitical data. The data collected by SNBS and the authorized organisations can thus be harmonized to reflect the true and definitive data useful in the formulation of viable socioeconomic and geopolitical policies.