Democracy and Governance Policy Briefs

Federal Budget 2024 Analysis

January 2024

Somalia's 2024 billion dollar budget in picture: A decline in social spending

SUMMARY

On December 9, 2023, Somalia's 2024 annual budget was approved in a joint session of parliament following a brief review and adjustment process of the proposed budget by the Cabinet in late October. The total approved budget amounts to USD 1,079,315,783 billion and comprises of USD 569.66 million in recurrent costs and USD 509.65 million in capital expenditure. A deeper look into the budget reveals both positive and worrisome signs. While the overall budget and domestic revenue have grown impressively over recent years and Somalia is slated to receive support following the completion of its debt relief process, Somalia's continued dependency on external support highlights its precarious financial situation.

The majority of Somalia's approved expenditures are allocated to recurrent costs and expenditures on social supports have been cut in this budget. Looking forward, it will be imperative for Somalia to continue to make improvements to its domestic revenue generation through tax reform and strengthening inter-governmental tariff mechanisms. Additionally, while it is positive and impressive for the Somali government to have achieved an approved budget on time, further work is needed to ensure that proper time is allocated for public participation in the process to support efforts of transparency and increase trust in government.

The below analysis provides further details on the 2024 national budget as well as recommendations for the future.

OVERVIEW OF 2024 BUDGET

In an extraordinary meeting in Mogadishu on October 28, 2023, the Cabinet of the Federal Government of Somalia unanimously approved Somalia's 2024 annual budget. The total annual budget of USD 1,025,200,115 covers the fiscal year beginning January 1 and ending December 31, 2024. According to the FPM Act of 2019, the Minister prepares the National Budget Appropriation Bill for the following year by September 30th of each year, and the Appropriation Bill approved by the Council of Ministers, along with the Minister's speech, is submitted to both Houses of the Federal Parliament by October 30th of each year.

The budget was officially submitted to the Federal Parliament on December 6, 2023, and after a quick review and a few adjustments, the total budget was approved in a joint session by both houses of parliament on December 9, 2023. The adjustments made by the Federal Parliament resulted in additional $54.1 million to the budget. That includes; addition of $38.1 million from UAE for the salaries of new Somali National Forces (SNA), $1.06 million additional revenue from Haj companies and $14.9 million new project funds for the Ministry of Education. The total revised budget enacted by the parliament amounts to USD 1,079,315,783 billion of which $569.66 million is a recurrent cost and $509.65 million is for capital expenditure.

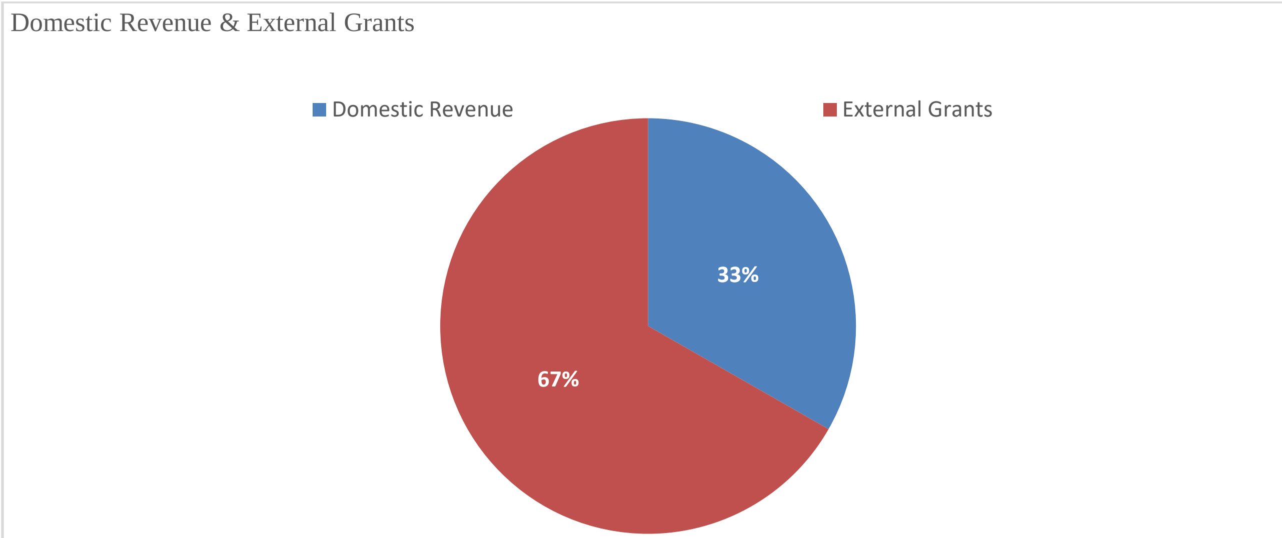
The total revenue target is $1,040,840,400 billion that will be raised through domestic revenue and grants from international donors, whereas, the total spending projection amounts to USD 1,079,315,783 registering a deficit of -$38 million. The government expects to finance its fiscal deficit from financial assistance to be provided by external donors post-debt relief process in 2024. Somalia and IMF reached post HIPC agreement on economic policies and reforms to be supported by a new 36-month arrangement of about US$100 million under the Extended Credit Facility (ECF), but much of the success will depend on effective financial transparency, and oversight by the parliament.

The total domestic revenue of $346.2 million is anticipated to grow by 62.9 million (22.2%) compared to the previous year, and represents 32% of the entire expenditure. The domestic revenue to foreign grants ratio continues to be low this year. FGS anticipates receiving external grants of $694.6 million for the 2024 fiscal year. Revenue from grants comprises budget support of $185 million and; donor-funded projects of $509.7 million. The total external revenue projection in 2024 is $60.7 million (9%) more than the revenue received in 2023. Although external grants appear on the budget each year, these grants are not realized as pledged.

Regarding the expenditure allocations, FGS spending agencies are categorized into four sectors. Administrative sector will receive the largest portion of the budget allocation with $382.9 million (35%) followed by Defense and Security sector with $255.6 million (24%). Economic and social sectors will receive the lowest allocations $232 million (22%) and $208.7 million (19%) respectively. All sectors made a notable increase compared to last year allocation with exception to the social sector which experienced a reduction of $36 million.

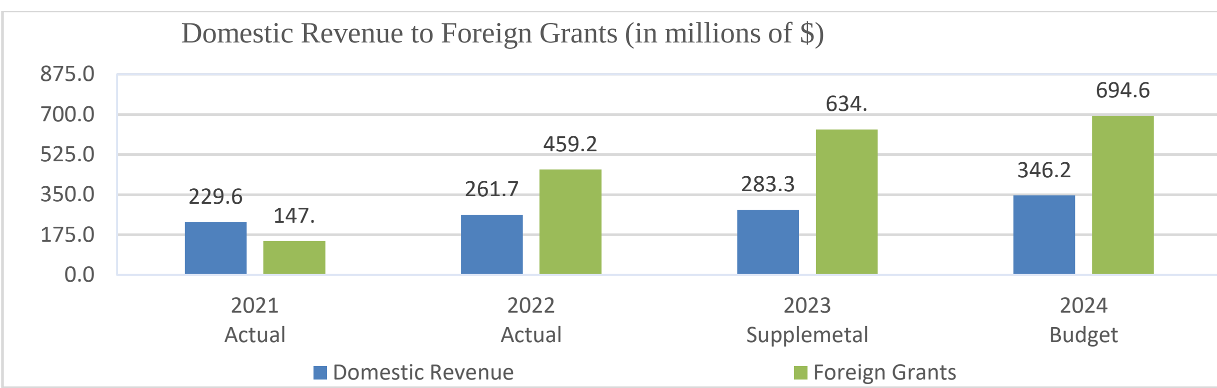
REVENUE STATUS IN 2024

Revenue and spending make up the annual budget. Total revenue is forecast to surpass USD **1,040,840,400** for the first time in fiscal year 2024, marking a $123.6 million (12%) increase over last year. Domestic revenue and external grants climbed at comparable rates of $62.9 million and $60.7 million respectively. Although the domestic revenue foresees substantial growth during 2024 fiscal year, the FGS's revenue mobilization capability remains low, leaving the budget 67% dependent on foreign aid.



Domestic revenue has increased proportionally over the last few years; however, it has never kept pace with external grants. During his speech at the Parliament, the Minister of Finance stated that the domestic revenue has made considerable progress during 2023 and is predicted to hit $324 million at the end of the year instead of $283 million reported in the supplementary budget.

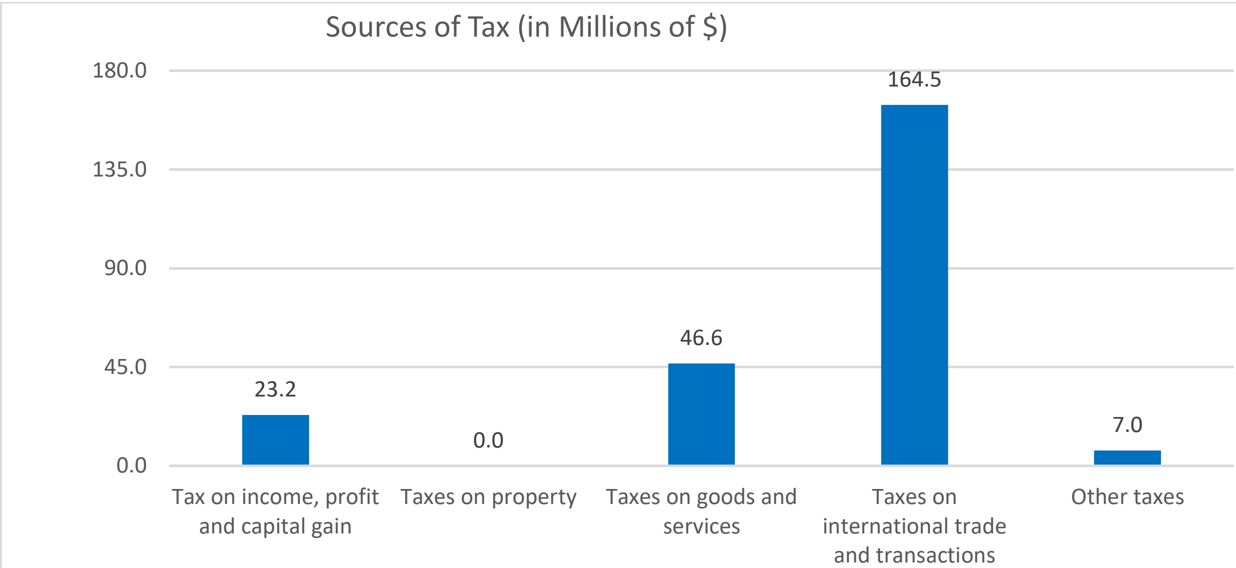
As illustrated in the graph below, reliance on foreign donations has increased significantly over the last three years in comparison to local revenue growth. The government's steadily rising spending and ongoing reliance on foreign assistance could be cause for concern.



Grants are obtained through bilateral and multilateral assistance. Bilateral grants totaling $68.1 million are projected this year, with Turkey contributing $30 million in form of budget support, followed by the United Arab Emirates offering $38.1 million. Multilateral grants, on the other hand, account for the majority of external funds, totaling $626.5 million.

REVENUE FROM TAX

The FGS tax revenue sources are quite limited. The Benadir region generates the majority of the tax revenue through indirect taxation. The revenue from taxes does not include any revenue from Federal Member States due to absence of unified tax collection system in the whole country. Similarly, there are numerous revenue sources such as the sales tax, corporate tax and telecommunication tax from which the government could have collected significant amounts of money, but none have. Similarly, tax laws and tariffs that could be used to raise more domestic revenue are out of date such as sales, corporate, income tax laws and must be revised.

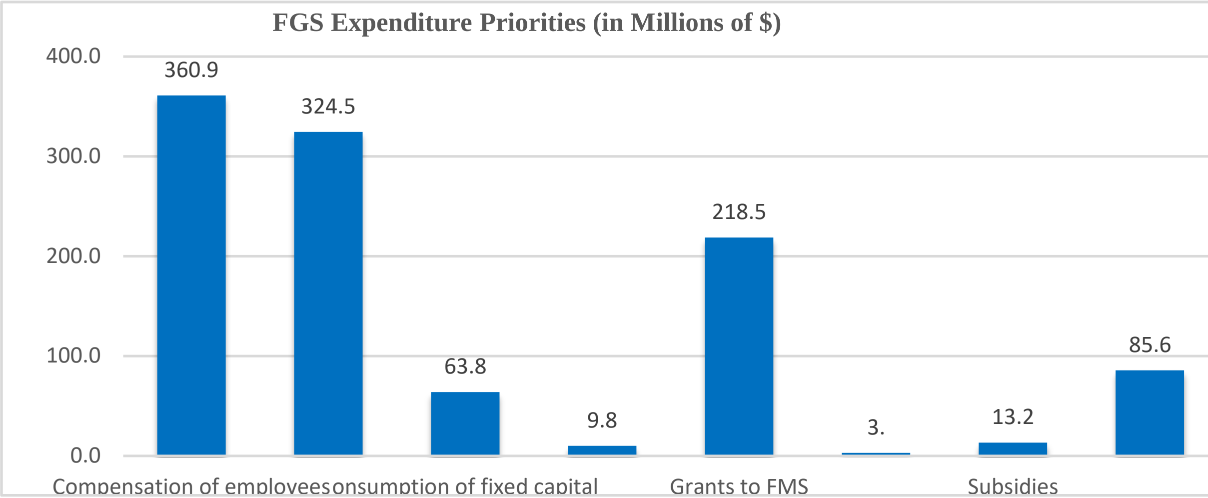


The most revenue is generated by taxes on international trade (customs and khat), which total $164.5 million (68%), followed by taxes on goods, which total $46.6.1 million (19%). Despite tremendous growth in the construction sector and property rents in Mogadishu in recent years, the budget shows that the government would not receive revenue from property tax this year.

EXPENDITURE ALLOCATIONS

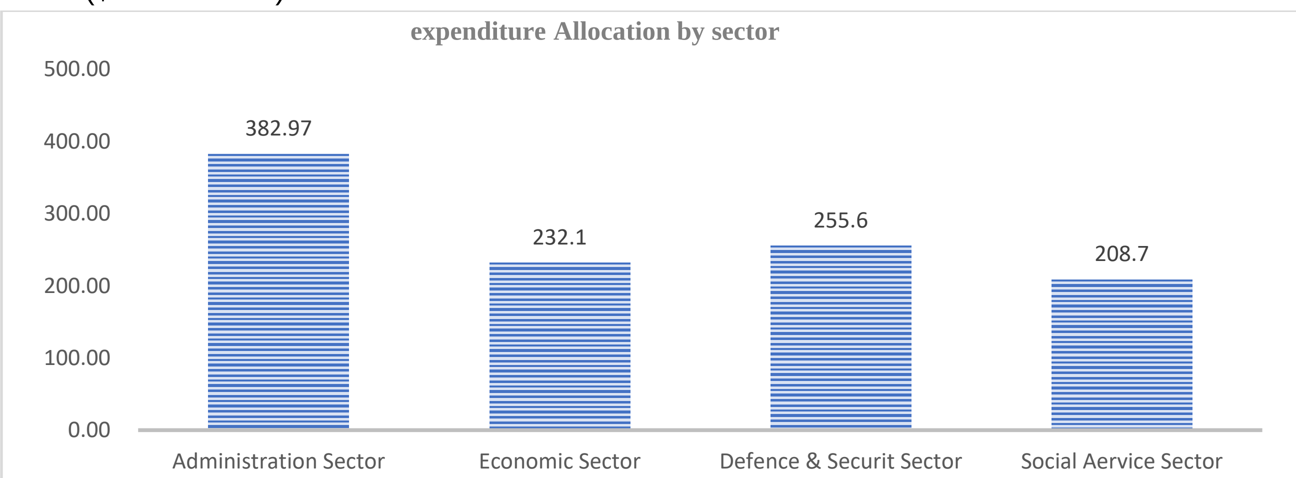
FGS spending plans for 2024 fiscal year rises to $ 1,079,315,783, of which $569.7 (53%) million is recurrent expenditure and $509.7 (47%) million is capital expenditure. Though FGS budget has steadily increased over the years, it is important to emphasize that domestic revenue remained insufficient to cover recurrent expenditure, and little amount is allocated to public service delivery.

Recurrent expenditure of $569.7 million is allocated to public sector salaries, allowances, and operational costs in the fiscal year 2024. The remaining $509.7 million goes to donor-funded projects. As shown in the table below, the FGS's spending priorities are employee compensation and operational costs, which account for 63% of total expenditure, followed by grants to Federal Member States (20%). Only 8% of the budget is set aside for social benefit projects.



EXPENDITURE BY SECTOR

The 2024 budget's expenditure allocation is based on four government sectors: administration sector ($382.9 million), defense and security ($255.6 million), economic ($232.1 million), and social ($208.7 million).



Administrative agencies receive the highest budget allocation out of these sectors. The Ministry of Finance alone would receive $224.5 million, (59% of administration sector budget), with the Ministry of Planning receiving $35.9 million (10%). The Administrative Sector budget has been increased by $48.3 million over the previous year.

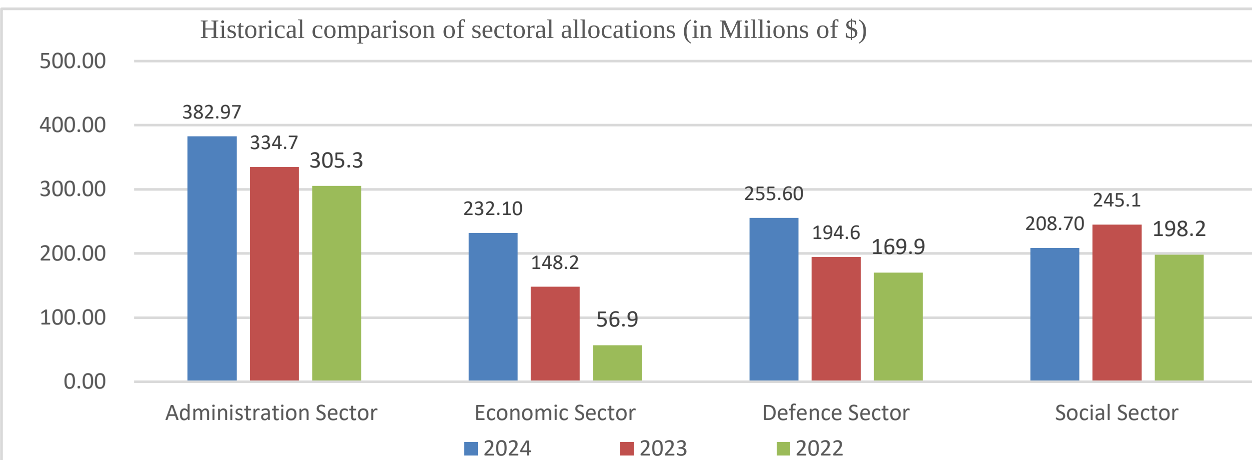
The administrative sector has always received the largest budget allocation, and the administrative agency budget has increased by approximately $48 million in the fiscal year 2024. This is due to a $5.9 million salary increase for parliamentarians and a $1.07 million allocation to the Ministry of Religious Affairs.

Defense and Security sector is receiving the second largest portion of the budget with $61 million growth from previous year. This growth is partially attributed to $38.1 million grants from UAE meant to cover salaries of new military cadets to be recruited for SNA.

Economic sector spending has increased by approximately $84 million since last year, but this increase is primarily due to donor-funded projects under the Ministry of Water and Energy, which increased from $14.7 million to $62.7 million, and those under the Ministry of Agriculture, which increased from $2.8 million to $48.3 million. Aside from these projects, no notable growth can be seen from regular spending of the economic sector agencies.

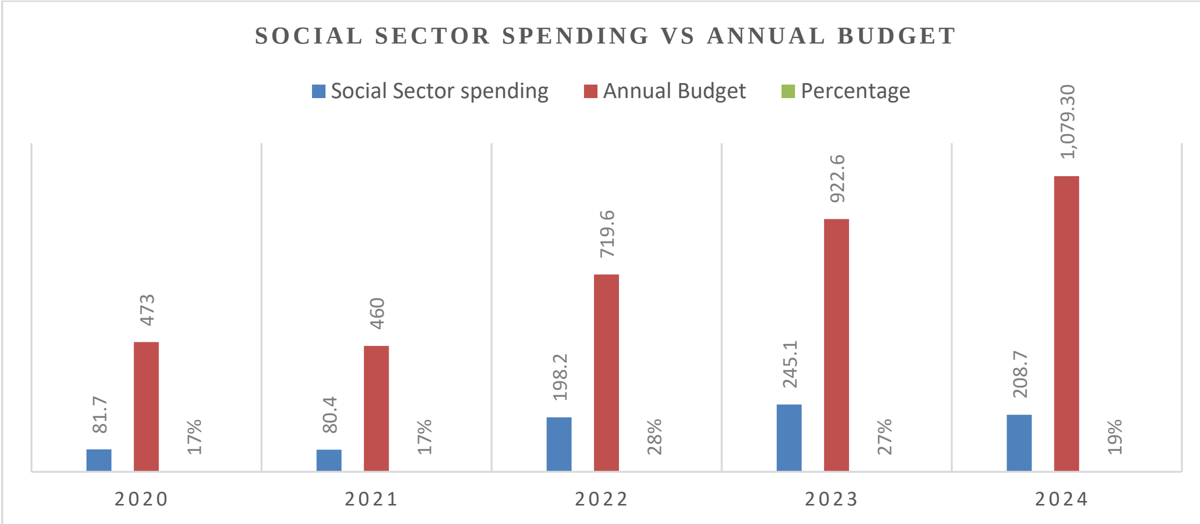
In 2024 fiscal budget, $208.7 million (19%) is assigned for the service delivery ministries. Five ministries are under this sector, namely, the Ministry of Labor and Social Affairs, the Ministry of Education and Higher Education, the Ministry of Health, the Ministry of Women and Human Rights Development and the Ministry of Youth and Sport. In 2024, the social sector figures experienced a decline of $36.4 million (-15%) from 2023 allocation of $245.1 million.

The vast majority of social sector expenditure is financed by external grants from the World Bank's International Development Association (IDA). However, the annual budget for 2024 saw a sharp decline in external revenue for those programs. The Shock Responsive Safety Net for Human Capital, (also known as Baxnaano) program funded by the World Bank, for instance, dropped from $122.1 million to just $69.7 million. Under the Ministry of Labor, the program was meant to provide cash transfers to targeted poor and vulnerable households and establish the key building blocks of a national shock-responsive safety net system.



Similar to 2023, the SOMCOVID-19 project, delivered by the Ministry of Health, was hit hard by receiving allocations that were $15 million less than last year's spending. Similarly, the Ministry of Higher Education's Education Strengthening and Training Project has seen a slight decrease in spending of $810.6 thousand compared to 2023 spending. The Ministry of Labor's Emergency Locust Response project has seen a $3 million decrease from the previous year. The SAGAL project has been reduced by $767.1 thousand (93%). While all other projects under social service agencies have seen slight growth, the startling decline in overall spending can be attributed to a reduction in World Bank grants for capital projects.

When comparing social spending to annual budgets over the last five years, it is apparent that social spending hasn't gone up significantly enough to keep pace with annual budget growth. Social spending remained constant at 17% in 2020 and 2021, rising to 28% and 27% in 2022 and 2023, respectively. Nevertheless, social spending is expected to decline to 19% in 2024.



WAY FORWARD

Over the last few years, FGS's annual budget has grown at a rapid pace. However, as impressive as the budget appears to be, it contains numerous flaws. Domestic revenue collection is extremely limited to a few sources and covers only thirty-two percent (32%) of total expenditure. The reliance on foreign aid seems to be increasing rapidly. FGS needs to update its tax laws and build a strong and robust taxation system to boost tax revenue. Similarly, the federal government should develop an inter-governmental fiscal mechanism to harmonize the tax tariffs across the country as well as adopt and apply a single import duty tariff schedule at all ports. In addition, introduction of telecommunication tax laws may regulate the booming sector and further increase the domestic revenue.

Though the Federal Government of Somalia (FGS) budget increased progressively over the years, it is noteworthy to mention that the majority stake of the government allocations are dominated by administrative and recurrent expenses, with little allotted to the public services delivery. Moreover, if this disparity continues to exist in the fiscal budget, the capacity of FGS to address shocks and support longer term recovery, development and livelihoods of the public will be minimal. However, this points to the need for the FGS to strengthen the management and utilization of limited available funds to scale-up the demanding priorities in the public service delivery.

Public participation in the budgeting process is one of the most effective indicators of the transparency and accountability of government budgets. The legislature approved the 2024 annual budget without taking into account any public input. This reduces budget accountability and transparency. Furthermore, according to the PFM Act of 2019, the FGS annual budget must be scrutinized by the legislature for at least two months prior to enactment. This did not occur in the 2024 fiscal budget, where the parliamentary debate lasted only four days. Similarly, funding for effective public service delivery programs is limited to a few donor-funded projects with inadequate implementation on the ground.

Perhaps one of the most commendable achievements by FGS is the completion of debt relief process in December 13, 2023, where the Executive Boards of the International Monetary Fund (IMF) and the World Bank's International Development Association (IDA) approved Somalia's Completion Point under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative. Debt relief help Somalia reduce its external public debt from US$5.3 billion at end-2018 to US$0.6 billion at end-2023.

This step will also enable Somalia to take more loans to strengthen its infrastructure programs. However, the decision on how much additional debt would be taken as well as what these loans would be used for solely lies with FGS. If Somalia takes more loans without a clear repayment strategy, it will undoubtedly create even more burden for the generations to come.