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DONOR INFLUENCE AND RURAL PROSPERITY: THE IMPACT OF POLICY REFORM ON ECONOMIC GROWTH AND EQUITY IN THE AGRICULTURAL SECTOR IN SOMALIA

by

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PREFACE

This study was commissioned by the Office of Development Planning in response to a request from the senior management of the Africa Bureau. The purpose of the request was to improve A.I.D.'s knowledge regarding the impacts on economic growth and equity of policy reform programs in Africa. This study and related studies, in Mali and Zambia, constitute the field studies for Phase I of the Office of Development Planning's Policy Reform Impact Assessment activities.

Each of the three country studies was prepared in the field during January 1987 by three member teams. Teams were comprised of 2 members provided under A.I.D.'s Macroeconomics Indefinite Quantity Contract with Robert R. Nathan Associates, Inc., Development Alternatives, Inc., and Boston University. The Bureau for Africa, Office of Development Planning provided the third member for each team. A fourth report synthesizes the findings with respect to the impact of policy reform programs in Africa.

Under Phase II, analytical activities will continue to broaden and deepen A.I.D.'s knowledge of the impacts of policy reforms in Africa. These activities will continue in fiscal 1987 and 1988.

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LIST OF ACRONYMS

ABS	Annual Budget Submission
ADC	Agricultural Development Corporation
CDSS	Country Development Strategy Statement
CG	Consultative Group
CIP	Commodity Import Program
CPF	Counterpart Funds
CSBS	Commercial and Savings Bank of Somalia
DDB	Domestic Development Budget
DDD	Domestic Development Department
EEC	European Economic Community
ENC	National Trading Company
FAO	Food and Agriculture Organization
GDP	Gross Domestic Product
GSDR	Government of the Somali Democratic Republic
HASA	Hides and Skins Agency
IBRD	World Bank
IDA	International Development Agency
IMF	International Monetary Fund
LDA	Livestock Development Agency
MinAg	Ministry of Agriculture
NRA	National Range Agency
ONAT	National Tractor Rental Service
PSIP	Public Sector Investment Program
PVO	Private Voluntary Organization
SAP	Structural Adjustment Program
SDB	Somali Development Bank
SDR	Special Drawing Right
SS	Somali Shilling
UNDP	United Nations Development Program
UNHCR	United Nations High Commission for Refugees
USAID	United States Agency for International Development
USG	United States Government
WFP	World Food Program

I. EXECUTIVE SUMMARY

The purpose of this study is to assess the impacts of Somalia's donor-supported economic and agricultural policy reform programs. Emphasis will be placed on the impact of market legislation on the incomes and welfare of the small-holding farmers and transhumant herders who form the productive base of the Somali economy. The time allotted to the study was very short, and in many sectors the most basic data are unavailable. We have thus relied heavily on anecdotal evidence, USAID and other donor reports and assessments, and meetings with a wide variety of people from USAID, other donor organizations, the Government of the Somali Democratic Republic (GSDR), Somali parastatal agencies, private businessmen, Private Voluntary Organizations (PVOs), and development projects in the Bay Region.

Since 1981, the GSDR has enacted a number of key reforms.

- The exchange rate has been freed to float to a more realistic level.
- Domestic cereal and livestock marketing has been privatized.
- A stabilization program has been adopted to curtail demand expansion.
- Certain government and parastatal monopolies have been abolished, including those of the National Trading Agency to import consumer goods, the Banana Board to purchase and export bananas, the Livestock Development Agency to purchase and market animals for export and the Agricultural Development Corporation to purchase and sell domestic cereals.
- Imports of most goods, including most agricultural inputs, have been liberalized.
- Civil service reform has begun and the GSDR has ceased acting as an employer of last resort.
- The GSDR has reoriented its basic strategy from an urban/industrial to an agricultural one.

The Somali domestic economy seems relatively prosperous and has responded well to the increased opportunities for private sector activities. Those reforms that have been enacted have had a decisive effect on certain sectors of the economy:

- The dramatic increase in grain production since the liberalization of the cereals marketing process has helped Somalia become self-sufficient in maize and sorghum.

- Farmer income, based on relative prices of grain and consumer goods, has risen.

- Herder income seems to have at least kept pace with rises in consumer prices and may have risen faster.

- The private sector has reacted to decontrol and increased disposable income in many sectors of the population by expanding dramatically.

- Private sector investment as a percentage of GDP, although still low, has risen significantly.

- New stores and even new factories are springing up rapidly in most of Somalia's cities and towns.

- Small and medium scale enterprises seem to have proliferated spectacularly, although there is no quantification of this phenomenon.

- Consumer goods are available more readily, in greater variety and quantity throughout the country, in secondary cities and even in small rural villages in the irrigated zones.

- Production inputs are becoming more readily available through the private sector, including some veterinary drugs, medicines, fertilizers, agricultural chemicals and seeds, etc.

- The GSDR has started to implement a program of civil service reform, which has begun reductions in the number of officials on the payroll.

- Tax revenues have begun to rise as a percentage of GDP.

- Exports from the privatized banana sector have risen.

- Exports from the privatized livestock export sector have begun to capture new markets and to approach the level of exports enjoyed by the country before Saudi Arabia banned imports of Somali cattle.

- Agricultural wages have risen to the point where they are higher than wages for government service.

- A reverse rural exodus has begun, with urban dwellers returning to the countryside to farm, either as permanent residents or as transhumant farmers.

- The value of land has increased significantly in irrigated areas and efforts to establish legal rights in land through registration and leasing form the GSDR have increase.

- Consumer welfare in the cities has improved as legal prices for domestic foodstuffs are relatively lower than they were under socialism when almost no food was available officially and the black market supplied small quantities at excessive, speculative prices.

- Underlying all these movements is an ongoing effort to improve Somalia's balance of payments, based on efforts to float and unify the exchange rate of the country's currency -- the Somali Shilling (SS). Until recently, when Somalia called a halt to the twice-monthly public auction of World Bank-supplied hard currency, good progress had been made; the auction rate was approaching a realistic level, in addition to estabment of a floating rate for private transactions.

Nonetheless, major difficulties persist. Somalia's external debt burden is overwhelming, her balance of payments situation is alarming, her annual budget deficits are staggering, her agriculture can succumb to catastrophic drought at any time, and her public administration remains an expensive and inefficient burden on the nation's taxpayers.

Among the most urgent remaining reforms are:

- Remaining state or parastatal monopolies and monopsonies must be rationalized.
- Civil service reform must be pursued.
- GSDR expenditures must be reduced to the level of potential revenues and budgeting improved.
- The GSDR must begin assuming responsibility for recurrent costs of projectized activities.
- The privatization of key economic sectors, such as banking, insurance and petroleum imports, should be encouraged.
- The official exchange rate should reach a realistic level.
- Rules, codes, and regulations governing land use and tenure, foreign and domestic investment, taxation and incentives, and customs, must be simplified and codified.
- Effective decentralization of governance and revenue generation and use must be studied and implemented.

II. INTRODUCTION

Policy in the Somalia Context

How can we best help the countries of Africa achieve real agricultural development? Should we concentrate on rural projects for farmers and herders or on policy dialogue with central governments? Which of these is the fastest, most cost-effective and sustainable path to real improvement of the quality of life of the people of Africa? Both approaches can be rewarding or frustrating, effective or futile.

Advocates of people-to-people participatory development know that farmers must sell their crops to improve the quality of their lives. At the same time, supporters of policy dialogue know that bureaucrats, even guided by the best of policies, cannot grow food in their offices. Policy without participation is an empty exercise in economic theory. The influence of policy dialogue on agricultural growth and the welfare of farmers and herders often remains obscure. Nonetheless, participatory projects in a hostile policy environment are doomed to failure.

Somalia is a particularly appropriate country in which to assess the impact of policy dialogue with a central government on growth and equity in the agricultural sector. Although considered a model of democratic government and economic liberalism (Lewis, Ch.VIII, passim) from independence in 1960 through the decade, in 1969 a military coup profoundly altered the direction the nation had taken. After the "October Revolution," the state adopted a controlled "Scientific Socialist" economy based on government control of all productive activities, marketing, and foreign exchange transactions. Government policy oriented the nation's economy towared industrial development.

Backed by ever-growing Soviet assistance, no significant economic difficulties arose until the Ogaden War of 1977. This conflict, which followed a severe drought in 1975, led to the severing of relationships with the Soviet Union, to extraordinary military expenditures, and to balance-of-payments and fiscal problems of unprecedented gravity. Western donors began slowly to replace Somalia's socialist benefactors and started working with the country to implement a far-reaching structural adjustment program.

But until 1981, the basic orientation of the Somali economy remained socialist, statist, and urban/industrial. The United States Agency for International Development (USAID) East African Country Profile #4 of 1980 could still write "Today Somalia continues committed to its goals of Scientific Socialism" (p. 17).

At first, the Western donors and financial institutions, led by USAID, the International Monetary Fund (IMF), and the World Bank (IBRD), were unsuccessful in altering the basic approach of the Government of the Somali Democratic Republic (GSDR) to development. The hopes for success of their agricultural and livestock programs were stifled by state-controlled marketing monopolies and monopsonies and by inefficient parastatal input suppliers. The first major crack in the socialist facade appeared in 1981 when the Livestock Development Agency (LDA) was abolished, after protests from the politically powerful rural stock feeders and exporters who earned over 90 percent of Somalia's foreign exchange. At the same time, the state abolished the National Trading Agency (ENC) monopoly on the import of consumer goods, permitting private traders to replace it; and began the process of eliminating the Agricultural Development Corporation (ADC) monopoly on cereals marketing in the countryside.

In 1982, a fortuitous combination of circumstances helped the donors to achieve a major breakthrough. Two years of drought and severe foreign exchange shortages led the GSDR to fear widespread famine and political disaffectation. They agreed to implement a long-standing donor policy reform request to completely liberalize the cereals market in the interior of the country. The result was an explosion in the quantities of sorghum and maize on the market and a significant improvement in rural welfare.

The rest of the policy reform program, presented in Chapter III of this paper, followed the successes of these first experiments in privatization.

The increases in grain production and in rural incomes have contributed to a general orientation of the Somali economy away from state-owned industries to private sector agriculture. This reorientation is among the most important successes of the policy dialogue process in Somalia, although it cannot be documented by any specific GSDR decision at a

given point in time. Today the GSDR proclaims its intention to base its future prosperity on the agriculture sector. This is a major achievement of the policy dialogue process.

USAID Objectives and Program

The USAID Program in Somalia has shown the way toward an effective combination of rural agricultural projects and policy dialogue. The FY 1987 Country Development Strategy Statement (CDSS) and the FY 1988 Annual Budget Submission (ABS) state that the mission objective is "to provide balance of payments support, reduce public deficit, and support (on a trial basis) promising areas of future growth." USAID wishes to arrive finally at a diversified, outward-oriented economy, built on a productive, sustainable economic foundation.

The strategy is based on three development themes: private sector development, policy reform, and outward orientation. In the area of policy reform the ABS states that the mission's agenda includes five priority areas:

- Macroeconomic stabilization
- Increased privatization
- Banking system reform
- Civil service reform
- Rationalization of trade procedures and business regulations

In addition, USAID has shared the lead with the IMF and the IBRD in attempting to establish donor coherence on policy issues and coordination of donor investment policies through the Consultative Group (CG) and regular donor meetings. Although there is a certain amount of donor agreement on most policy issues (see Appendix D), much effective coordination of donor investment programs has yet to occur. The GSDR Public Sector Investment Programs (PSIPs) have remained ex post justifications of individual donor projects rather than integrated programs of synergistic development activities.

Somalia Economic Profile

The Macroeconomic Setting

Somalia, which is about the size of Texas and has only five million people, is among the UN's least developed countries. The country is highly dependent on external support, which funds 100 percent of the national investment budget, close to half the domestic operating budget, land significant technical assistance to all sectors of the economy. Economic infrastructure is relatively underdeveloped. Less than 10 percent of the populace has a primary education and life expectancy is only 46 years.

Somalia gets most of its foreign exchange from official transfers. Livestock and banana exports and worker remittances constitute the country's other sources of external income. The thin range of exports leaves the economy vulnerable to exogenous disturbances. Hence, the 1983 Saudi ban on Somali livestock exports, invoked to curb the possible spread of disease, threw the economy into a tailspin, severely exacerbating debt-servicing difficulties. Disbursed external public debt now exceeds Gross Domestic Product (GDP) and the debt to service ratio is approaching 90 percent. While government expenditure is not excessive (less than 18 percent of GDP), the tax base is extremely narrow -- 5 percent of GDP -- producing fiscal difficulties. Moreover, although inflation has come down from near triple-digit levels in 1984, it remains high -- roughly 34 percent in 1986.

Manufacturing accounted for only 5 percent of GDP in 1986. The sector is inefficient, dominated by parastatal enterprises. Banking, insurance, and portions of import and export trade remain the province of inefficient public sector monolpolies.

The Agriculture Sector

Agriculture, consisting of a commercial sector and a large subsistence sector, is the predominant economic activity in Somalia. The sector contributes more than 55 percent of GDP, accounts for 80 percent of employment, and provides 100 percent of merchandise export earnings.

Although the Somali climate is harsh, agriculture is possible over a not inconsequential area and is limited primarily by rainfall, which varies from 100 to 500 mm a year. Current agricultural practices use few inputs beyond water, land, and labor. Yields, even in the irrigated subsector, are well below those achieved in similar environments elsewhere in Africa.

Following the decontrol of cereal marketing in 1982, crop production improved dramatically after a decade of decline and stagnation. Somalia seems to have surpassed self-sufficiency in maize and sorghum -- its two principal staple crops. However, it remains dependent on food imports for rice, sugar and wheat.

Livestock Herding

Transhumant livestock herding constitutes the principal source of food and income for 70 to 80 percent of the population, produces 40 percent of domestic food production on a caloric basis, and accounts for 90 percent of merchandise export earnings. At one time, it held first rank as a source of livestock imports to the whole Arabian peninsula. While that position declined with the Saudi ban on livestock imports, exports are once again rising. The Saudis have lifted bans on some classes of livestock and markets are being developed in other states, particularly Egypt. The subsector also provides fresh milk and other dairy products to the burgeoning urban populations of Somalia.

Dry Land Production

Somalia's major dry land crop is sorghum, although farmers cultivate small quantities of others such as safflower and sunflower. The dry land crops in any one season cover 500,000 to 700,000 hectares. Sorghum and maize, the latter grown largely in irrigated areas, are produced almost entirely by small-scale farmers. Sorghum represents 45 percent of total grain production. Despite increased use of hired tractors for plowing, current dry land cultivation practices use few inputs. Most farmers could achieve improved yields with better cultivation practices and certain commercial inputs.

Irrigated Production

Of a total cultivable area of 150,000 hectares in the Shebelle River Valley, 54,000 hectares are under flood irrigation. In the Juba River Valley, about 120,000 hectares are under controlled irrigation with an additional area of undetermined size under flood irrigation. Large-scale private and state farms produce rice, bananas, and sugar, while smallholders grow maize and sesame in rotation and cultivate bananas for export.

Maize has become the major domestic grain marketed in Somalia; total maize production now represents 55 percent of domestic grain output. Better water management, expanded use of fertilizer, and improved cultivation practices are required to generate yield increases.

After livestock, bananas constitute Somalia's second most important merchandise export. Bananas are marketed through a joint venture, SOMALFRUIT, owned 60 percent by De Nadai, a multinational headquartered in Italy, and 40 percent by the GSDR. SOMALFRUIT's strong role in marketing helps ensure that appropriate export quality is maintained.

Sugarcane yields have fallen in recent years and are now about what they were in 1950. Production of sugarcane, a government owned and managed irrigated crop, has been impeded by controlled prices, extreme shortage of foreign exchange, and major difficulties in operating the irrigation systems.

Fisheries

Somalia's fishing resources are still undeveloped. Somalia has over 3,000 kilometers of coast line and apparently large ocean fishing resources. At the present time, about 2 percent of the population is involved in the fishing sector and the sector's contribution to exports and domestic value-added is negligible. Expensive experiments in state-controlled deep sea fishing, fish processing and storage were unsuccessful, but attempt to stimulate artisanal fisheries have had encouraging results. Fishing lacks infrastructure, markets, and support services.

Inputs

Even by African standards, demand for commercial agricultural inputs in Somalia is still at a very low level. Even where demand exists, commercial inputs have generally not been available in rural areas. The banana subsector has been the major crop activity to use modern agricultural inputs.

Tractors are the major improved input in common use in rural Somalia. At the end of 1984, about 2,000 tractors were in operation; about 370 of these were owned by the public tractor rental service company (ONAT). Because of the artificially low official exchange rate, ONAT has been able to provide services at roughly half their market costs, thereby discouraging private operators from providing similar services. Under the IBRD Agricultural Sector Structural Adjustment Program (ASSAP), ONAT will be required in the future to achieve full cost recovery for tractor rentals.

The GSDR has been responsible for the distribution of fuel oil, which was subsidized. Control of the fuel market has not resulted in an adequate supply of fuel, even for the limited mechanization already in place. Fuel prices through the official channels have been artificially low and rationing systems ineffective in ensuring fuel supplies for agricultural uses. The GSDR has promised to eliminate fuel subsidies and is being encouraged to allow private fuel distribution in the near future.

Veterinary services are provided free by the GSDR to the livestock sector. Unsatisfied demand for services exists at present subsidized prices. The GSDR is now encouraging private sector provision of animal health products and services by increasing the number of non-prescription veterinary drugs classified as safe for private imports.

Production Enterprises

Since the early 1970s, the GSDR has become involved in a wide range of production enterprises in the agricultural sector, including industries, state farm projects, and settlement programs. The GSDR has set up 16 industries, which have been inefficient. Studies are under way to determine which of these enterprises should be privatized, which discarded, and which maintained as public interest activities.

The GSDR organized and managed the production on 18 major state farm projects. The process of breaking up these costly and inefficient farms has begun and private farmers have gained access to land. However, the tenure regime is very unclear.

The performance of the agricultural enterprises in the public sector, on balance, has been dismal. On some occasions, the enterprises inhibited development and in other cases they failed to deliver needed services. The enterprises have proved to be unproductive investments and have been a drain on the public coffers. The output of most agriculture enterprises has stagnated, declined, or ceased altogether in recent years. Some of the losses have been spectacular, e.g., the deep sea fishing attempts, the urea plant, and most of the state farms. Only the flour and pasta factory is operating at a reasonable level of plant utilization -- 33 percent in 1983 and 68 percent in 1984. Others are operating at 30 percent or less capacity utilization and many are closed.

III. THE REFORM PROGRAM

The Donors, Their Roles, and Programs; The Consultative Group

The key players promoting macroeconomic and agricultural policy reforms in Somalia have been the IMF, the IBRD, and USAID. Generally speaking, all have agreed on the major economic issues, although from time to time they have diverged on the timing and pace of the reform effort. The donors support the common themes of strengthened public finances; parastatal reform; adoption of a realistic exchange rate; easing of foreign exchange controls; relaxation of price and import controls; promotion of private sector activity; and encouragement of agriculture production.

Some disagreement, however, has arisen over specific reforms under these broad themes, including exchange rate float and unification; livestock export tax; surrender requirements; and disposition of the ADC.

While all donors support the establishment of a realistic exchange rate, USAID would opt for a floating exchange rate regime and the IMF and IBRD for a managed exchange rate system. USAID feels that the GSDR is incapable of managing an exchange rate system; the Fund and the Bank assert that the volume of the foreign exchange market is low and a floating rate system would produce significant exchange rate volatility.

In 1981, at the urging of the IMF, the GSDR imposed a 25 percent export tax on livestock exports. The tax was subsequently adjusted downward significantly through specific levies -- taxes per head rather than on value. All the donors including the IMF acknowledge that any export tax discourages exports. However, the IMF viewed the tax as necessary to support Somalia's flagging public finances and felt that the ongoing depreciation was providing ample incentives for livestock exports.

All the donors would like export surrender requirements to be as minimal as possible. However, in view of the country's fragile foreign exchange position, the IMF required the GSDR to increase requirements from 35 to 50 percent in 1986. Nonetheless, the 50 percent requirement which still amounts to almost a 30 percent tax in light of the differential, between the free market and official exchange, represents an improvement from the 100 percent requirement imposed before 1985.

As for the ADC, USAID would like to see it wither away. The IBRD supports its continued existence as a mechanism to minimize risk for both farmers and consumers through reduction in price variability.

The IMF has played a pivotal role in supporting structural adjustment in Somalia. The Fund's efforts have concentrated primarily on strengthening the public finances, curbing monetary expansion, increasing revenue, promoting appropriate exchange rate adjustments, improving external debt management, liberalizing prices, and providing increased incentives for agricultural production. The Fund provided successive stand-by arrangements of Special Drawing Rights (SDR) 11.5, 43.1, and 60 million over 1980-82 (1 SDR=$1.20). Generally speaking, the arrangements were successful in promoting reforms. Most significant were the substantial and ongoing devaluation of the shilling, de facto liberalization of producer and consumer prices, and significant reduction in government borrowing from the domestic banking system.

A new IMF stand-by program of SDR 20.1 million came into effect on February 22, 1985. At the same time, a compensatory financing facility arrangement of SDR 32.6 million also became available. The objectives of the new stand-by program have been met broadly, although th GSDR continues to encounter problems in making external prepayments, including to the IMF. Highlights of the GSDR reform efforts under this most recent stand-by arrangement are the adoption of a freely floating system for determining the exchange rate of private transactions, the elimination of virturally all trade restrictions, restraints on further external borrowing, official dismantlement of all price controls, improvement of revenue collection, and a hike in interest rates.

The large sized of the IBRD portfolio for Somalia has accorded the Bank a significant role in promoting reform. Primarily through its soft loan window International Development Agency (IDA), the IBRD has provided Somalia credits of $249.8 million, of which $199.3 million has been disbursed.

The IBRD adjustment efforts at the macro level have emphasized rationalization of the Public Sector Investment Program (PSIP) and parastatal enterprise reform. The IBRD, as well as many of the other donors, feels that the PSIP has been largely donor-driven and that the Somalis have been pushed into undertaking projects that were not economically viable.

In June, 1986, the IBRD's $63 million Agricultural Sector Adjustment Program took effect. The Program calls for the establishment of an auction system for the allocation of foreign exchange, the elimination of subsidies on diesel fuel and tractor rentals, the further liberalization of agricultural marketing, the expansion of private sector participation in supplying and distributing inputs to the economy, the improvement of interest rate regimes for agricultural credit, GSDR commitment to an acceptable PSIP, and improvement in the efficiency of the marketing of hides and skins. Program monies were used recently to initiate the foreign exchange auction.

The Bank also has played a key role in organizing the Consultative Group (CG) for Somalia. CG meetings took place in late 1984 and November 1985 and a CG is scheduled for Spring 1987, subject to GSDR agreement to a new IMF arrangement. Under the aegis of the CG, balance of payments gap-filling exercises took place in January and November 1985.

The CG has provided important support for economic policy reforms. Little disagreement on major policy reforms has been in evidence among the donors, although the intensity of their commitment to implementing them may vary. On the other hand, the CG has been less successful in achieving rationalization of the PSIP. Donors implement their "pet" projects without consideration of economic viability and recurrent costs.

USAID has been active in the promotion of reform across a wide spectrum of issues. Until recently, USAID has been Somalia's most important bilateral donor. In 1986, commitments totaled $88 million, of which roughly three-fourths was in the form of nonproject assistance. The nonproject assistance has been USAID's primary vehicle for promotion of economic reform. Macro reforms have been encouraged under Commodity Import Program (CIP) I in FY 1982, CIP II in FYs 1983-84, CIP III in FY 1985, and in FY 1986 through the Somalia Cash Sales Program, while PL 480 Title I arrangements have promoted reforms in the agricultural sector and also at the macro level.

An important component of the USAID stabilization efforts at the macro level has been support of the IMF; both CIP I and II included convenants requiring adherence to ongoing IMF standby arrangements. Promotion of private sector activity, including

rationalization of parastatal enterprise and liberalization of import and export licensing, also has been an overriding theme. Results have included a revised draft private foreign investment law, theoretical authorization of the private sector to import petroleum products, and the preparation of a law allowing the formation of private commercial banks.

While the self-help measures incorporated in the PL 480 Title I arrangements have been exceedingly wide ranging, their primary focus has been the liberalization of internal marketing and elimination of price controls for many crops, especially cereals; and a reduced role for public sector institutions. The GSDR is reviewing the operations of public enterprises in the agricultural sector with an eye to operating those enterprises that are economically viable through management contracts, and to selling to the private sector or dissolving those which show no promise for profit. Title I also has been used to encourage much-needed civil service reform. For instance, the policy of guaranteeing jobs in the civil service to high school graduates has been discontinued.

The only other donor to show any interest in economic policy dialogue is West Germany. West Germany will only undertake projects in a milieu that is conducive to private sector development, but it imposes no conditionality on its aid to Somalia. Italy, now the most important bilateral donor, pays the least attention to coordination with other donors. Because of a recently instituted emergency package of $250 million, most of the Italian program falls entirely outside the PSIP. Although Italy has significant amounts of private capital invested in Somalia -- nearly $20 million in the banana industry alone -- it has not participated in efforts to impose crucial reforms on the GSDR. France, the most important of the group of lesser bilateral donors, specifically avoids policy discussions with the GSDR, although it supports the general direction of donor community initiatives.

Chronology of Reforms to Date

Somalia's ambitious structural adjustment program (SAP), which began in earnest in 1981, springs from a difficult economic situation made immeasurably worse by the Ogaden War of 1977-78. Government expenditures shot up 50 percent in 1979; domestic revenues increased, but by much less; and external budgetary support was inadequate to fill the gap. The resultant demand explosion together with a drought in 1980 led to a serious

financial crisis, with large budgetary and balance of payments deficits and high inflation.

The GSDR response was a structural adjustment that included (1) a major shift in policy towards liberalization, including the promotion of the free play of market forces, and (2) the adoption of a stabilization program to curtail demand expansion and provide incentives to commodity producing sectors.

A number of reforms were introduced over 1981, 1982, and the first portion of 1983. Specific macroeconomic measures included dramatic depreciation of the currency (140 percent in 1982 alone); the closure of three parastatals; liberalization of private sector imports; a hike in interest rates; discontinuance of the practice of automatic civil service employment for all high school graduates; and authorization for all Somali nationals owning foreign exchange abroad to open external accounts.

Even more significant were the numerous agriculture policy reforms. First, all marketing was liberalized:

- The LDA was abolished in April 1981; livestock trade is now conducted primarily by private traders.

- The requirement that all farmers sell their main staple products to the ADC, which had held a monopoly over the domestic grain trade, was waived in 1982.

- After 1981, the GSDR discontinued the requirement that fishermen sell their catch directly to the parastatal SOMALFISH.

- The ENC, since 1981, no longer exclusively distributes imported foodstuffs to the private sector.

Second, in response to the liberalization of marketing, producer prices for most agriculture products were increased. In 1981 alone, the increases ranged from 30 to 50 percent; for bananas the hike was 100 percent.

Third, the parastatal National Banana Board was transformed in August 1983 into a joint venture company with a private overseas partner.

The impact of these reforms on agricultural production was dramatic. However, in late 1983 and into 1984, the GSDR failed to consolidate the progress made in previous years and did not

confront the remaining structural and institutional problems facing the economy. More expansionary fiscal policies, together with the 1983 Saudi ban on Somali livestock exports and a bad drought, resulted in sharp deterioration in fiscal and balance-of-payment accounts and a resurgence of inflation. Resulting debt-service difficulties were sufficiently serious to require the IBRD to convene a special gap-filling exercise among Somalia's external "friends," in January 1985.

Backed by a new IMF stand-by arrangement, the GSDR moved in 1985 to restore public confidence in the movement of the economy toward free market enterprise. Over 1985/86, a number of reforms have been implemented. First, a key theme has been promotion of private sector activity:

- A Chamber of Commerce has been established; the private sector also may form trade associations.

- A revised private and foreign investment law has been approved at the technician level; the law will reduce regulations and give concessions to private firms.

- A law allowing the formation of private commercial banks and insurance institutions has been prepared.

Second, the GSDR continues to adjust the official exchange rate; it was depreciated 63 percent in 1985. A freely floating system for most private transactions was established in 1985 and, although suspended recently on a temporary basis, a foreign exchange auction utilizing IBRD commodity import program proceeds was started in September 1986. The auction rate was rapidly approaching the free market rate, giving hope for unification at a realistic exchange rate in the future. Third, while surrender requirements for foreign exchange export earnings were hiked to 50 percent from 35 percent in 1986, they had been lowered from 100 percent in 1985. Fourth, a de facto elimination of most price controls took place in 1985. While price controls remain for petroleum products, the price of gasoline now exceeds import parity and the price of diesel reached import parity in June 1986. Fifth, the GSDR continues to hike interest rates in an effort to attain positive real rates. The most recent increase of interest was 4 percent in nominal terms on deposits in September 1986. Finally, the GSDR also is moving to improve the tax collection effort, altering specific tax rates to an ad valorem basis; broadening the coverage of excise duties; basing the calculation of import duties on a more realistic exchange rate; implementing extensive staff and

administrative improvements; and imposing new taxes. Tax collections in 1986 rose to 4.6 percent of GDP from 3.9 percent in 1985.

Reforms also continue in the agricultural sector. Privatization is a dominant theme, especially in the distribution of inputs:

- The GSDR has promised to permit private individuals to obtain licenses to import diesel fuel for distribution through private channels.

- ONAT will be required to achieve full cost recovery, thereby reducing its competitive advantage vis a vis private concerns.

- The GSDR is increasing the number of non-prescriptive veterinary drugs classified as safe for private imports.

- The GSDR continues to hike agricultural prices for those commodities where free market forces do not operate. For example, at the beginning of 1985, banana prices were increased 38 percent in real terms; they were increased again by almost 45 percent at the beginning of 1986. Floor prices for freely marketed agricultural commodities also have risen.

IV. THE IMPACT OF THE REFORM PROGRAM

Introduction

The economic and agricultural policy reforms undertaken by the GSDR since 1981 have reverberated throughout every aspect of life in Somalia. Although progress has varied from region to region and sector to sector, the general impact of the reform package has been positive. Real gains in public welfare have been achieved.

This chapter examines the impact both of specific reforms and of the constructive economic climate engendered by liberalization on specific activities in Somalia. We have concentrated primarily, though not exclusively, on analyses of activities in the agricultural sector: crops and livestock.

Reliable data on economic activities in Somalia are as scarce at the level of national accounts as they are at the level of the rural farm. Our interpretation of the impact of economic and agricultural policies is thus based on extensive interviewing of Somalia's bilateral and multilateral donor, parastatal, and private sector actors in Mogadishu and Baidoa. We have tried to evaluate and interpret what data we found in light of our impressions from these meetings.

Economic Impact of the Reform Program

While the large, unabating influx of refugees, the droughts in 1980 and 1983, and the 1983 Saudi ban on Somali livestock exports complicate the analysis, on balance the policy reform program has had positive economic impact. Generally speaking, macroeconomic indicators reflect the positive impact on the economy of the initiation of the reform program in 1981, the negative effect of the backsliding over 1983/1984, and the favorable impact of the arrest of the backsliding over 1985/86.

In contrast to a growth of minus 3 percent per annum over 1978-1980, with the start-up of the reform program growth spurted to 11.2 percent in 1982, sputtered at 2.4 percent per annum in 1983/84 due to the drought and Saudi ban on livestock exports, and recovered to 10.2 percent in 1985 and 5.0 percent in 1986.

In contrast to previous years, domestic savings were positive in both 1981 and 1982. Domestic savings once again were negative in 1984 with the relaxation of reform program implementation.

Tax revenues as a share of total expenditures can be used as an indicator of fiscal performance. Over 1981-83, tax revenues covered almost 50 percent of total expenditures, up from 38 percent in 1980. With a relaxation of financial discipline, public finances worsened significantly in 1984. Tax revenues covered but 26 percent of expenditures in that year. More recently, some improvement has been recorded, thanks primarily to tax collection improvements.

The country's reform efforts in the early 1980s were successful in bringing monetary growth down. Monetary growth, which exceeded 30 percent annually over 1977-79, was running at only 6.2 percent in 1983. A cut in GSDR borrowing from the banking system in both 1982 and 1983 contributed to the reduction. With a relaxation of financial discipline, monetary growth was once again moving up; by 1985 it was growing a whopping 80 percent a year. The monetary expansion was associated with increased GSDR borrowing from the banking system. The GSDR has since moved to stem the borrowing from the banking system and this should augur well for lowered monetary growth in the future.

The GSDR reform and stabilization efforts also have been successful in curbing inflation. Inflation, which had surged from just under 10 percent in 1977 to almost 60 percent in 1980, was brought down to 22.6 percent in 1982. Inflationary pressures resurfaced in 1983 as the GSDR relaxed monetary policy control and the currency was depreciated. By 1984, inflation was nearing triple-digit levels. A return to more stringent financial policies has succeeded in once again lowering inflation. Inflation was roughly 30 percent in 1986 and was expected to fall further still in 1986.

The balance of payment data reflect improvement with the onset of the reform program. The current account deficit, excluding grants, fell as a share of GDP from 21.3 percent in 1980 to 17.8 percent in 1981. The balance of payments worsened under the Saudi ban on livestock exports. It continued to deteriorate in 1985 due to a decline in remittances related to the fall in oil prices, and high interest rate payments associated with the country's severe debt servicing difficulties. By 1985, the current account deficit excluding grants stood at 30.6 percent of GDP.

Impacts of Policy Reform on Agricultural and Livestock Production

Cereal Production in Somalia

In Somalia, cereal production has traditionally ranked behind animal husbandry as a prestigious and viable agricultural activity. The majority of the rural population practices herding and depends primarily on the meat and milk of their animals for food. Most sedentary farmers own livestock.

During the 1970s, GSDR policy maintained low cereal prices, eliminating farmers' incentive to produce any surplus grain. Production and marketing of sorghum and maize, the primary cereal crops, stagnated during this period, resulting in increasing cereal imports, which peaked in 1981.

Market Liberalization

The cereal shortage that occurred in 1981 threatened to lead to famine and political upheaval in the urban areas of Somalia. This forced the government to close its eyes to private sector cereal marketing activity. This activity, which had existed as a thriving black market in cereals, was now officially accepted. The result was an immediate and dramatic rise in farm-gate prices and a flood of sorghum and maize into the urban markets. The food crisis was averted and the GSDR recognized the effectiveness of the private sector in this domain.

The ADC had to follow the private sector and by the end of 1981 their producer prices for sorghum and maize had increased 50 percent over the previous year.

Market liberalization was not officially legislated until 1985, and in some provincial areas government officials continued to enforce price control and the ADC's monopoly. However, throughout the country, private sector trade continued to grow and prices moved toward a free market level. Private sector traders are now free to participate in cereals marketing without restriction on prices, volume or administrative frontiers.

The improved production of sorghum and maize in 1981 and 1982 was due to the liberalization of marketing policies as well as to good weather conditions. In addition, farmers probably took from their very effective traditional storage pits (bekkar) the unmarketed, clandestine surplus they had built up during the period of the ADC monopoly.

Table 1. Production of Sorghum and Maize
(Thousands of metric tons)

Year	Sorghum	Maize
Average 1970s	139	107
1981	222	143
1982	235	150
1983	120	235
1984	221	270
1985	260	280

The dramatic improvement shown in Table 1 is primarily a result of an increase in area planted, although yield growth for maize and sorghum also contributed. Farmers have invested more labor in both irrigated and rainfed fields as prices have risen.

The ADC and Market Liberalization

The government created the parastatal ADC in 1971 to stabilize cereal prices, as well as to create buying points in producer areas. In the 1970s, ADC annual purchases of sorghum and maize were between 20 percent and 30 percent of production. As the government began to relax its restrictions on private trading of cereals and allowed prices to move to a free market level, the ADC began to lose its share of the market to the private sector, until in 1984 it bought only 1.6 percent of production.

The ADC has tried to adapt quickly to its new role which calls on it to maintain stable cereals prices for both producers and consumers, act as a buyer of last resort of domestic cereal production, and maintain a national security stock of cereals.

Table 2. ADC Market Share of Combined Sorghum and Maize Production

Year	Percentage of market
1981	8.0
1982	2.6
1983	3.5
1984	1.6

In 1984 and 1985, good rains led to a bumper crop of maize and sorghum; this began to drive down the market price. The ADC's floor price, set by the GSDR on the advice of the IBRD, was suddenly higher than the market price. Thus the ADC in 1985 and 1986 purchased between 15 percent and 20 percent of the crop. These purchases were financed by credit from the state-owned Commercial and Savings Bank of Somalia (CSBS). The ADC ran up a debt of more than Somali Shilling (SS) 600 million, which it has been unable to repay. The ADC has refused to sell its stocks at a loss and the market price has remained below the level at which it had purchased them. ADC purchases thus act as a direct transfer of income to farmers. Inadequate ADC storage practices exacerbate the corporation's precarious financial situation, as losses in warehouses are estimated between 40 percent and 60 percent.

There is significant disagreement among donors and the GSDR as to the need for the ADC and the role it should play. All agree however, that it is badly managed, both administratively and technically.

Bananas

Bananas, Somalia's second largest export commodity after livestock, have also shown a production increase after the initiation of policy reform. Production and export of bananas declined during the middle and late 1970s, because of inadequate producer prices, an overvalued exchange rate, and unavailability of foreign exchange for vitally needed inputs. However, this trend was reversed in the latter part of 1983 because of the depreciation of the currency, increased input availability, and improved marketing and shipping facilities. The formation of a joint venture company between the Government's Banana Board and a foreign corporation has played a significant role in the improvement.

Table 3. Production of Bananas[a]

Year	Metric tons (thousands)
1969-74	127
1981	69
1982	72
1983	85
1984	106
1985	110

a. See Appendix F for detailed discussions of the banana industry, including production for the local market.

In 1983 the area planted in bananas increased by about two thirds over the previous year. In 1984 the area planted increased another 17 percent. Yield levels show a slight decline due to the entry of inexperienced planters into the market and expansion onto less fertile, less watered land after the increases in banana prices.

Sugarcane

Sugarcane is a government owned and managed irrigated crop, with government controlled prices. Thus, this important import substitution crop has not shared in the production growth of other major crops. Yields have been declining. There have been major management problems and difficulties in operating the irrigation system.

Livestock Production

Livestock production contributed an estimated 40 percent of the GDP in 1984. It is also Somalia's principal foreign currency earner activity through the export of live animals. Hides and skins, which should contribute significantly to export earning, have stagnated under the continued control of a parastatal corporation which has monopsony power over all purchases for export.

There has not been any significant change in the rate of growth of the livestock sector in the 1980s. Policy reforms have touched the livestock production sector less than the crop sector. The GSDR attempted to control livestock exports in the

1970s through the LDA, but the transhumant herders and small-scale middlemen were difficult to control. In addition, their political ties to leading Somali poltiicians gave them better protection from official rules than did those of the less well-connected traditional crop sector. Climate and range conditions have remained the main determinants of herd size and offtake among Somalia's husbandmen.

Nonetheless, the sector has showed some increased dynamism under the reform policies. Livestock exports, which plunged after the Saudi ban, have recovered significantly as private traders and associations of traders have opened up new markets and expanded old ones.

Trade Balance

Among the primary objectives of the policy reform program which began in 1981 was the improvement of the trade balance. Indeed, some elements of the trade balance have improved since the start-up of the reform program. The overall trade deficit fell from $327 million in 1980 to $301 million in 1985. Certain reform measures can be associated directly with the improvement.

A key factor has been the depreciation of the currency. Since 1982, the GSDR has adopted a flexible exchange rate policy; in the previous eight years the currency had been pegged to the U.S. dollar at a fixed rate and had become significantly overvalued. The official exchange rate was depreciated 140 percent in 1982, 15 percent in 1983, 48 percent in 1984, and 63 percent in 1985. A freely floating rate was started under the 1985 financial program with the IMF. Also this past fall, an auction system -- now temporarily suspended -- was put in place to assist in the movement toward a more realistic foreign exchange rate. The depreciation of the currency has had a favorable impact on exports and constrained imports.

In addition, the GSDR has introduced a score of liberalization measures to encourage repatriation of foreign exchange and this, undoubtedly, has permitted foreign exchange earnings from agriculture to rise. These measures include allowing export traders to open external accounts; the opening of export promotion accounts denominated in foreign currencies by Somali nationals and foreigners; and the reduction in surrender requirements from exports of goods from 100 to 35 percent in 1985, since increased to 50 percent in 1986.

A number of commodity-specific measures also have been introduced, which have liberalized export trade and had positive impacts on Somalia's major foreign exchange earners: livestock and bananas.

In addition, the GSDR is now considering implementing a number of further reforms, including relaxation of export licensing, a review of the banana export industry, studies on livestock marketing and the export market for hides and skins, deregulation of the myrrh and frankincense trade, and improvement of clearance procedures for exported goods.

The gains in the agricultural trade balance involve both export promotion and import substitution. On the export side, bananas, in particular, have advanced and some import substitution has taken place with respect to grains.

After livestock, bananas are Somalia's most important merchandise export. Banana exports, which were down to 34.3 thousand tons in 1981 from 81.8 thousand tons in 1975, advanced more than 75 percent over 1982/83, reaching 62.4 thousand tons. While banana exports fell back somewhat over 1984/85, they still were almost 30 percent higher by the end of 1985 than they were in 1981, the year the reform program commenced. The increase in U.S. dollar terms of banana exports also was significant. Exports reached $16 million in 1986 after having stood at only $6 million in 1981.

Who is benefitting from the increase? SOMALFRUIT is clearly doing well. Over the past couple of years, it invested $20 million and already $10 million has been recovered. We have seen an exodus of people out of urban areas into the irrigated banana-growing lands in the Juba and Shebelle River Valleys and small holders in the subsector are demanding significant credit.

Livestock exports have recorded some gains from the program, though these were interrupted by the Saudi ban in 1983. Over 1981/82, livestock exports in U.S. dollar terms rose from $98.0 to $105.7 million. In quantity terms, exports of sheep, goat, and cattle rose 6.5, 5.7, and 35.3 percent, respectively. The impact of the Saudi ban, however, was severe. Livestock exports were down to $33.1 million in 1984 and exports in quantity terms of sheep, goat, and cattle fell respectively 46.8, 49.7, and 95.0 percent. By 1985, the backsliding was arrested. The reform program, together with the lifting of bans on small ruminants by the Saudis and the identification of new markets, e.g. Egypt, was responsible. Livestock exports recovered to $66 million in 1985 as exports in quantity terms of goats and sheep rebounded.

How are the gains distributed? Export prices received by the nomadic herders seem to have gone up at least as fast as inflation. Also exports are continuing, and these are not distress sales arising from drought. Livestock exports shot back up in 1985, and further modest increases were anticipated in 1986. These sales would not take place if there were no profits to be made. On the other hand, an attempt is underway to have livestock export marketing conducted more profitably; the private

sector is seeking to organize a livestock marketing board. We understand that 90 percent of livestock export traders are in debt, and some have left the trade. There is a shared view that gains from the livestock trade have not been as robust as they should have been. In the past, the specialized livestock traders made good, but not spectacular, profits.

The minor exports, fish, frankincense, and myrrh, also advanced with the implementation of the reform program. Fish exports, which were $0.3 million in 1980, reached $3.0 million in 1982; myrrh exports rose from $3.7 to $6.3 million over the same period. Subsequently, exports in U.S. dollar terms for both products, however, have fallen back. In the case of myrrh, the parastatal monopsony persists. Hides and skins, a potentially important export, continues to stagnate under the control of the parastatal Hides and Skins Agency (HASA).

Depreciation of the currency appears to be constraining agriculture imports. In real local currency terms, imports of agriculture foodstuffs fell 28 percent over 1981-85.

The most important foodstuff imports are cereals and cereal products, which account for 68.1 percent of the total, followed by sugar and sugar products (12.8 percent), animal and vegetable oils (7.8 percent), and fruits and vegetables (5.7 percent).

Cereals imports in the 1980s have consisted of, in descending order of importance, wheat, maize, rice, and sorghum. With implementation of the SAP, cereals imports have declined over 1981-85 more than 16 percent in quantity terms, from 386.8 to 325.0 thousand tons. The decline is remarkable on two counts. One, population growth has been rapid, approaching 3 percent annually. Hence, the decline on a per capita basis has far exceeded 16 percent. Two, there has been a large influx of refugees into the country. Over 1981-85, wheat imports have declined 50 thousand tons to stand at 150 thousand tons at the end of the period; rice imports fell from 85 to 75 thousand tons; and sorghum imports were nil in 1985, after having stood at 11 thousand tons in 1981. For their part, maize imports were up marginally -- 10 percent -- and were in the neighborhood of 100 thousand tons in 1985. The maize imports went to refugees.

The impact of the SAP on other foodstuff imports is at best inconclusive. While sugar imports declined almost 50 percent in 1982, they surged over 1983/84 and by 1984 were more than 40 percent higher. In addition to low global sugar prices, the inability to cut sugar imports may be an outgrowth of difficulties at the country's two sugar factories -- Jowhar and Juba. The Jowhar sugar factory and plantation requires complete refurbishment. While the Juba sugar processing facility is considerably more efficient than the Jowhar factory, it utilizes only 50 percent of its capacity.

Employment

The structural adjustment program (SAP) seems to have influenced employment positively. Granted, there are no comprehensive data on employment; there also are no wage data. Nonetheless, employment appears to be picking up especially in the urban areas, where informal and small business activity in the private sector appears to be booming.

The reforms most responsible for any increases in employment consist of (1) the exchange control liberalization measures beginning in 1981 (see matrix in Appendix C for further details), (2) easing of import controls in the early 1980s, (3) de facto elimination of price controls in 1985, and (4) price and marketing liberalization in agriculture. These reforms are reducing the costs faced by private concerns in doing business in the country. The price and marketing liberalization in agriculture may be especially important, resulting in higher rural incomes with important spread effects.

On a nationwide basis, the GSDR produces a Manpower Statistics Bulletin. While inaccurate, the Bulletin provides data on a yearly basis on the number of job seekers and of those job seekers the number that secure jobs. Placements of job seekers seem to have expanded significantly, especially over 1981-84.

Employment could come from four main areas -- livestock herding, dryland crop production, irrigated crop production, and private sector activity in the urban areas. The GSDR, which was an employer of last resort for Somali secondary school and university leavers, stopped hiring all new graduates in 1983. They have also ceased hiring agents to replace functionaires who leave the civil service. Thus, the current expansion in employment is entirely a private sector phenomenon.

We do not have any information, even anecdotal, on employment effects in livestock. The team did have an opportunity to visit Baidoa, a dryland crop production area. We learned that some people, encouraged by price liberalization of sorghum, have moved back to farming in the area when rains have been ample. In any event, sorghum production increases suggest that at the very least underemployment is declining in the region. We also had a chance to visit the Shebelle irrigated area. The vigor of economic activity in the area was visibly impressive. There has

been a rush of people into the area to take advantage of the opportunities afforded by the SAP. The number of people engaged in crop production was striking.

Even more impressive, however, is the rapid expansion of private sector activity and associated employment in the urban areas, especially in the capital city Mogadishu. This expansion, driven by Somalis rather than expatriates, is especially important since a large portion of the Somali populace lives in the major urban areas. The registration of small establishments, mostly family-owned and operated, and of market stalls shows a significant increase in recent years; these establishments may have an employment capacity of 100,000 or more in Mogadishu alone. There are food supermarkets in Mogadishu where none had existed before. Four modern hotels have been constructed privately in the capital city since 1983. Many more mini-buses are being operated. Drug stores, which numbered only 20 several years ago, now are in the hundreds.

Sketchy real wage data also suggest that Somalia may be making some inroads against unemployment in Mogadishu and the other urban areas. Higher real wages imply that unemployment and underemployment are declining. Real wages appear to have increased significantly in recent years in Mogadishu. Surveys undertaken by the World Bank to determine wage rates for local staff in the capital city show fourfold to sixfold increases in nominal wages since the beginning of 1984. Over this period inflation was on the order of only 172 percent.

Gains in employment arising from the SAP, however, would have been even more impressive if it were not for a number of factors. These factors include:

- The recession in Middle East oil producing states. Many Somali construction workers are returning home. At one time, Somali workers numbered 200,000 in Saudi Arabia, 60,000 in Kuwait, and 30,000 in UAE

- Cuts in civil service employment

- A continuance of negative real interest rates, which encourage capital-intensive rather than labor-using technologies

The decision in 1972 to teach all school subjects in the country's native tongue also has reduced the employability of Somalis in private concerns, whose businesses require the knowledge of foreign languages.

Impact of Policy Reform on Agricultural and Livestock Prices

During the period of Scientific Socialism, the GSDR controlled prices of major agriculture products. The industrial sector development orientation of the Soviets required that agricultural prices remain at levels that were affordable by the urban consumers who worked in the new industrial developments. In 1981 the government began a process of policy reform that eventually raised prices to a market level for most products.

Livestock Prices

Livestock prices were controlled far less than crop prices. The continual movement of herders made it difficult to develop any effective price policy for the domestic market. However, the government did intervene in the livestock export market to a certain extent. An autonomous government agency, the LDA, was created to regulate export livestock marketing. One of its functions was to set minimum export prices. The LDA was to adjust this floor price to stimulate exports. In reality, the LDA exercised very little control over prices and export prices continued to rise while the LDA was in existence.

In 1981, the GSDR policy shift from public sector to private sector marketing included abolishing the LDA. Since that time, livestock trading has been in the hands of the private sector. Most recently, private sector livestock exporting companies were formed to improve the ability of livestock traders, 90 percent of whom are in debt, to exploit market opportunities. These companies are made up of producers and traders who are working to present a unified front in dealings with overseas importers. One of the functions of the consortium of the 50 export marketing companies is to set floor prices for livestock exports. In this case, it is the producer and trader who make the pricing decisions rather than the government.

Crop Prices

In the following discussions, we refer primarily to the ceiling prices imposed by the ADC. We were unable to locate a set of producer free-market prices, which in Somalia would be determined principally by the two harvest seasons, the grain stocks in the country, and the flow of grain imports.

In the crop sector, price controls and monopolistic marketing of sorghum and maize by the ADC had a much greater impact on crop marketing than the LDA had on livestock marketing. Prices for sorghum and maize paid to producers by the ADC were considered low by farmers, to the point of being below the cost of production. Furthermore, farmers were allowed to store only a one-year supply and were obliged to sell the remaining production to the ADC.

In the 1970s, grain prices set by the ADC fell in real terms as the country suffered from serious inflation. (Real prices can be utilized as an indicator of farmer welfare; increases in real prices mean that the farmer can command more goods and vice versa.) Not only were producer prices low, but the farmers' buying power was declining rapidly. As a consequence, parallel markets developed; prices were four to six times higher than the official price of sorghum and maize paid by the ADC. Scarce resources were used up in evading official controls.

Table 4. Sorghum and Maize: ADC Producer Prices
(SS/metric ton)

	Nominal price		Real		
Year	Sorghum	Maize	Sorghum	Maize	CPI
1977	750	750	750	750	100.0
1978	750	750	680	680	110.2
1979	750	750	550	550	135.3
1980	1,000	1,000	461	461	216.7
1981	1,500	1,800	479	574	313.4
1982	1,500	1,800	390	469	384.2
1983	2,650	3,250	506	620	524.0
1984	2,720	3,250	270	322	1,007.7
1985	13,000	15,000	929	1,071	1,400.0

To a certain extent, ADC prices can serve as a proxy for free market prices, since the commencement of the reform program in 1981. ADC real prices for sorghum and maize have tended upward, reflecting developments on the free market. By 1985, price were 100 percent

higher in real terms than in 1980; the comparable increase for maize was 130 percent. Within the period, backsliding on the part of ADC occurred in 1984 when inflation neared triple-digit levels. In that year, real prices fell to unprecedentedly low levels.

Welfare Impacts of the Price Decontrol Policy

Who appears to benefit most from the increases in grain prices resulting from the SAP? The growers? The retailers? The middlemen? Consumers?

Since the beginning of the SAP in 1981, retail prices have gone up in real terms, more than doubling for maize and nearly doubling for sorghum. However, in the absence of free-market farm-gate price series (producer prices), we cannot allocate gains among producers, middlemen, and retailers. Anecdotal and impressionistic evidence indicates that all three groups have made significant real gains from the cereals trade since liberalization began. While consumers are paying more in real terms for grains, the increases in production have greatly eased access to these grains. In the past, price-induced shortages had limited such access, especially for urban consumers.

Table 5. Maize and Sorghum Retail Prices
(SS/metric ton)

	Maize		Sorghum	
Year	Nominal	Real	Nominal	Real
1977	1,240	1,240	1,240	1,240
1978	1,250	1,134	1,840	1,670
1979	2,390	1,753	2,210	1,621
1980	7,220	3,332	8,770	4,047
1981	4,110	1,311	6,200	1,978
1982	5,280	1,374	5,610	1,460
1983	8,670	1,655	6,800	1,313
1984	34,400	3,415	27,000	2,680
1985	45,000	3,214	40,000	2,857

Bananas

Banana prices, which are market-determined, have gone up almost 130 percent in real terms since 1980. That, combined with the depreciation of the currency, has produced powerful incentives for banana growers to produce more. These pricing developments have also played a key role in promoting the rush for banana land.

Private Sector Growth and Institutional Reform

From 1969 until the early 1980s the most important institutions in Somalia belonged to the Government. The scientific socialism of the regime called for state control of production, marketing, and distribution of all goods vital to the well-being of the nation. This included nearly all manufactures, most foodstuffs, nearly all imports and, to the extent possible, exports. These institutions included government agencies (ministries, offices, the Central Bank) and parastatal organizations like the ADC, ONAT, the pasta factory, and Somaltex. Through the early 1970s the system worked, using large inputs of Soviet aid.

Under such protection, the fundamental inefficiencies and disequilibria in the Somali institutional matrix remained hidden. However, when Somalia suffered the simultaneous shocks of drought, the Ogaden war, and the Soviet departure, the shaky equilibrium fell apart. The state and parastatal institutions, which had strangled the national private sector, had to pull the nation through a major crisis of inflation, famine, public debt, and diminished financial resources.

Unfortunately, the institutions called on to save the nation's economy were more in need of reform themselves than able to carry out the structural adjustment program Somalia undertook beginning in the early 1980s. As Somalia began its recovery from years of mismanagement, it had no viable institutions with which to implement the reforms needed. When, in 1981 and 1982, the GSDR finally abandoned costly and fruitless attempts to control livestock exports and cereals marketing, they in effect authorized a third set of institutional actors to take the stage: the private sector.

In theory, public institutions carry on activities of benefit to the society as a whole, which are either inherently unprofitable or of such importance to equity and welfare that they cannot be entrusted to private interests. These activities usually include the creation of infrastructure, national defence, other vital public services, and the

establishment of rules and regulations to govern the operations of society. Parastatal institutions are usually created to promote sectors into which private investors hesitate to enter or to ensure equity in sectors where private interests might work against general popular welfare.

In Somalia, parastatals have acted as obstacles to economic development and equity. The private sector in the early 1980s was in no condition to take a major role in reviving the economy without significant assistance and a change in the policy climate, which for years had discouraged entrepreneurial activity.

For this reason, when the major Western donors began providing significant assistance to Somalia, they included in their policy programs major institutional reforms in the public and para-public sectors. They also called for the creation of a deregulated economic nexus in which the private sector could flourish.

The GSDR has adopted a series of measures intended to rationalize the national economy and promote both growth and popular welfare. Several of these have helped reform existing institutions; others have led to the creation of new ones; and some have eliminated obstacles to efficient economic performance. Principal among these reforms are:

- The elimination of certain state monopolies
- The privatization of state and parastatal activities
- Improved management of the public sector
- Improved regulatory and procedural climate for private enterprise

Needless to say, these reforms have proceeded at different speeds and with varying degrees of success. There is no room in this short paper for the detailed analysis of the impact of the reform program on each institution it touches, although this might prove a useful exercise in the future. Instead, this section can only present a few examples of the impacts of these reforms.

The elimination of para-public marketing monopolies has led to very dynamic small-scale private sector participation in national cereals marketing and livestock exporting. This, in turn, has contributed to significant increases in

crop production and has fueled a resurgence in livestock exports since 1983, in spite of the apparently permanent loss of the Saudi cattle market due to politics in the country.

However, the trend toward privatization has slowed recently as the GSDR has procrastinated on the restructuring of the Hides and Skins Agency, authorizing private banking, and liberalizing fuel imports among others.

Although private investment rose as a percentage of GDP after liberalization --

1979-80 average	1980-84 average
5.5%	8.8%

-- most of the results of the encouragement of the private sector are difficult to quantify. Observers of the Somali scene are unanimous in commenting on the striking growth of small businesses, shops, trades, light manufacturers, both in Mogadishu and in the interior -- even in small villages.

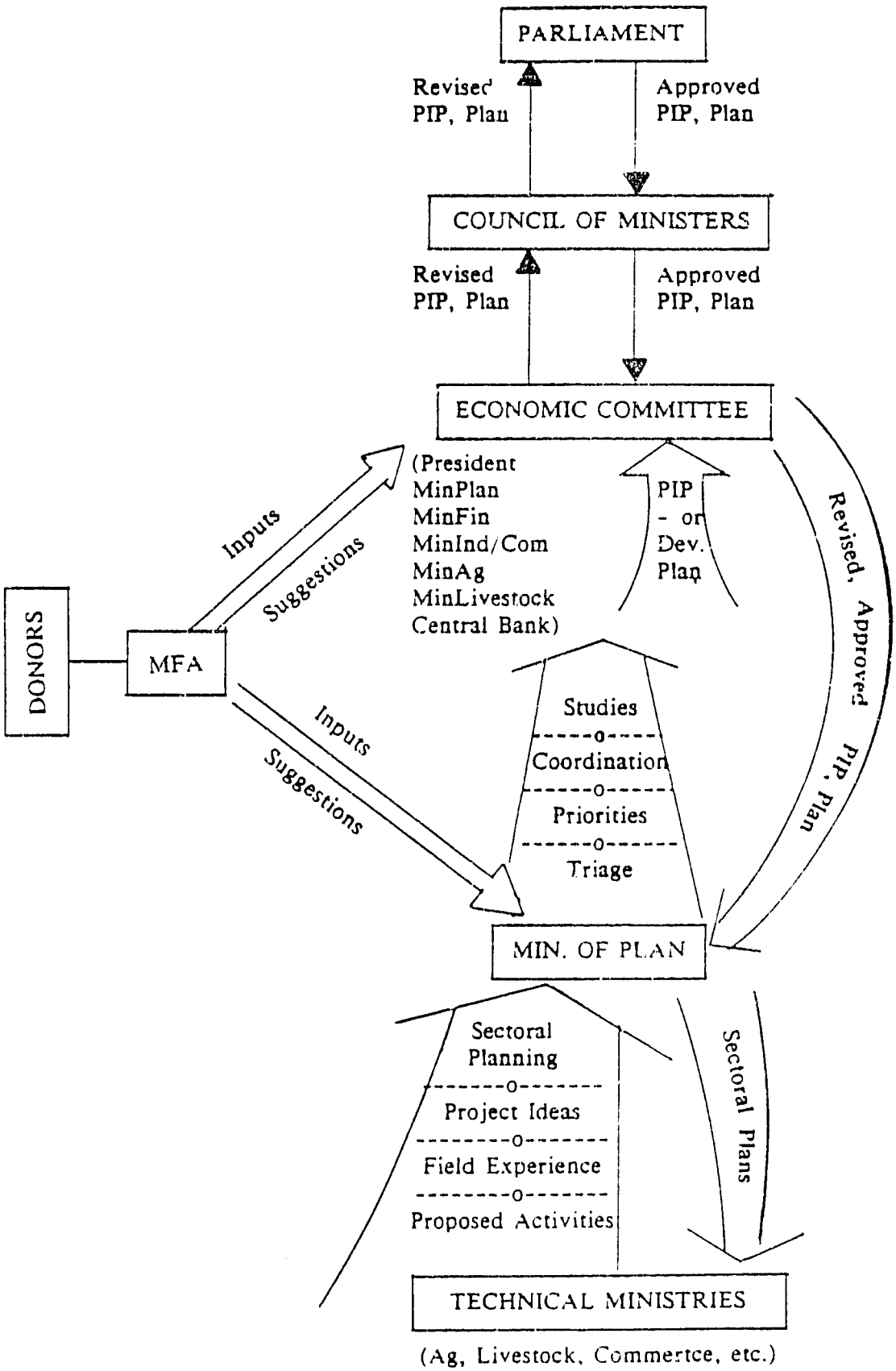
However flourishing the small and medium scale enterprise sector may be, Somalia has not yet enacted a coherent, useful set of procedures and regulations for foreign or national investors that would encourage them to enter the national economy in force. This, in turn, has meant that development of the private sector has turned far more toward services and trade than toward production activities. The Ministry of Industry and Commerce has prepared a draft law on foreign investments (20 November 1986), but this law has not yet been approved by the GSDR and is not in force.

The failure to enact and publicize useful codes and procedures points out the failure of the reform program to date to produce institutions capable of implementing reforms. A look at the procedures for decision-making of the GSDR points this up very nicely. In theory, policy options are adopted as in Figure I. Reality is quite different, as shown in Figure II.

A disconcerting array of influential personalities and agencies participate in making decisions about development policies, programs, and projects, including ministers, businessmen, donors, and other groups or individuals. They intervene directly at the highest levels, arrange lobbying efforts, and succeed, more often than not, in getting their pet projects adopted by the GSDR and a funding agency. No Ministry, including Plan and Finance, has the ability and the power to control this interference with the planning and coordination process. All are thus powerless to coordinate

FIGURE 1

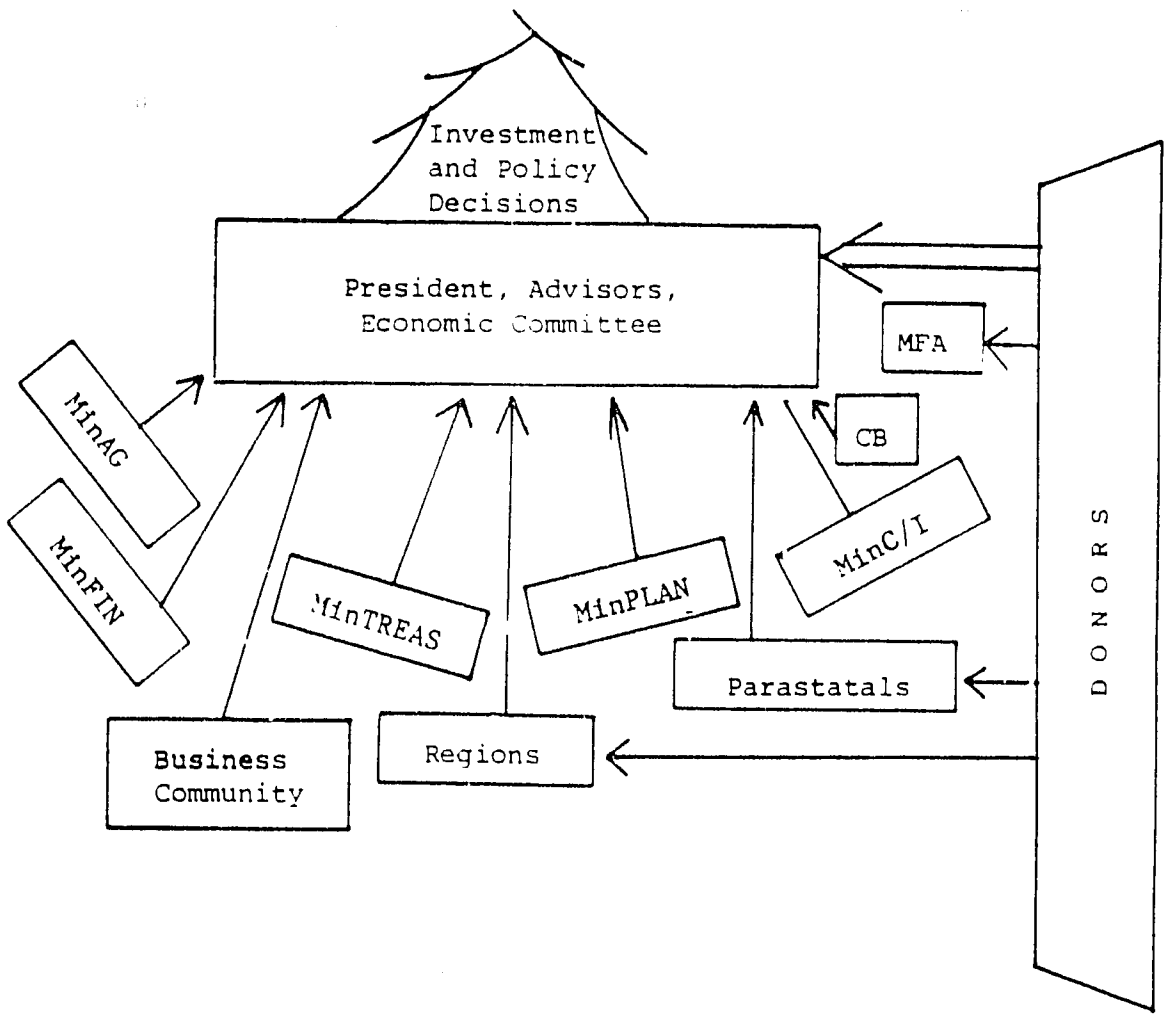
GSDR PLANNING PROCESS



IMPLEMENTATION

FIGURE 2

GSDR PLANNING PROCESS
(alternate)



and regulate the structural reform process. This is one of the most serious weaknesses in the national reform program.

Donor efforts to insist on the reform and restructuring of the Civil Service led to the "Somali Civil Service Study" of September 1984. Funded by USAID, this work presented a series of recommendations for improving the efficiency of the GSDR ministries. The study treated a wide range of urgent issues: organizational restructuring, management performance, personnel administration, pay scales, training, and donor roles. The report has been accepted but not fully implemented by the Government.

According to the study, the Somali administration must justify its existence by facilitating national development in creating wealth rather than consuming the national budget futilely. Since potential resources for supporting the civil service are meager, the GSDR must limit personnel and enterprises to what it can afford. Although some ministries have been combined (e.g., Commerce and Industry were joined in 1985) and some bureaucrats have been retired or sent to other sectors (about 1,000 to 2,000 per year since 1985), observers note very little improvement in civil service performance since the GSDR accepted the report's conclusions. At the current pace and if the decision to hire no new civil servants is maintained, the recommended target of 36,000 personnel might be reached in about 1995.

The reform program as a whole seems to have led to significant improvement in civil service welfare, but not because of the pay raises recommended by the 1984 study (200-500 percent) or by the Poulin Study of December 1986 (600 percent across the board). The resurgence of the informal private sector has enabled many officials to start small businesses and to supplement their salaries effectively by taking time off from work to run them.

The Poulin Study brought to the fore another aspect of the GSDR reform program. In order to diminish the current expenditure budget relative to GDP, the GSDR has adopted a policy of turning recurrent government activities into projects and funding them out of the donor-generated counterpart funds (CPF) of the Domestic Development Budget (DDB) of the Treasury Ministry.

Although this does relieve some of the pressure on the current expenditure budget, which has declined as a proportion of GDP since 1983, it represents a very short-term solution to the provision of services such as road maintenance and agricultural extension, which are almost entirely

paid for by donor-generated CPF in the DDB. Although tax collections rose as a percentage of GDP from 3.9 to 4.6 between 1985 and 1986, the GSDR is not close to generating the revenue it needs to maintain basic services.

To complete the institutional reforms still needed in Somalia, the donors must first help create institutions capable of implementing reforms, internally and externally. This means:

- Continuing to press for the reforms proposed by the 1984 Civil Service Study and the Poulin report
- Continuing the movement to rationalize productive activities now carried out by parastatals
- Encouraging the GSDR to adopt and establish codes, regulations, and procedures to encourage productive private investment
- Strengthening the capacity of the GSDR agencies (e.g., the Ministry of Plan) to effect a triage between sustainable and non-sustainable projects and the power of those agencies to convince the GSDR and donors to accept their decisions
- Defining carefully the role of state and parastatal agencies in the future of Somalia and the means to pay for these services

On the whole, the impacts of the institutional reforms in Somalia have been positive:

- Government revenues are up.
- The small and medium scale enterprise sector has boomed.
- Agricultural production and services have risen dramatically.

- Livestock exporters are opening up new markets and recapturing their predominant position on the national economic scene.

But much remains to be done. The lack of donor coordination, along with Somalia's failure to develop institutions capable of implementing the reforms the GSDR has approved, will make the task a long and difficult one.

Commodity Assistance Programs

Donor commodity assistance to the Somali Government (GSDR) takes three basic forms: food aid, commodity import programs, and cash sales programs. USAID and the IBRD use these approaches in a conditional manner in order to influence the GSDR's policy choices. The economic policy conditions attached to commodity assistance programs have promoted economic reforms that have encouraged agricultural production increases and fostered increased income and welfare among small farmers and herders in Somalia. At the same time, commodities brought in under these programs could have disincentive effects on prices for domestic cereals.

A cursory examination indicates that we do not have enough information to determine precisely whether imported commodities have had a negative impact on domestic cereals production. On balance, while the large amounts of cereals imported in the early 1980s may have had a negative impact on domestic production, at the present levels and composition of food aid, the impact is probably negligible, except in specific circumstances.

In 1985 and 1986, the U.S. was the only donor offering food to the GSDR in significant quantities. The European Economic Community (EEC), which had previously occupied second place among food donors, has unofficially suspended food aid since 1985. The IBRD and the IMF do not provide food; the World Food Program (WFP), United Nations High Commission for Refugees (UNHDR), and other bilateral donors only contribute to feeding refugees. The WFP also contributes food for work rations to a National Range Agency (NRA) Range and Forestry Project and to two nutrition intervention projects for vulnerable groups.

The United States Government (USG) commodity exports consist of wheat, wheat flour, oil, and rice. The GSDR uses up to 55 percent of these imports to feed official institutions -- the army, hospitals, prisons, schools, etc. The other 45 percent is sold at public auction to the private sector.

A number of factors suggest that food aid has not had significant negative impact on domestic production. A parastatal agency, the ENC, exists to receive, store, and resell food aid donated to the GSDR. The ENC can sell this food to the private

sector, but only after the public institutional demand is satisfied. In most circumstances the ENC sells very little to the private sector. In 1985, ENC sold the following quantities of imported, donated commodities:

Wheat flour	30,853 metric tons
Rice	20,306
Edible oil	8,754
Total (cereals)	51,159 metric tons[1]

Table 6. 1985 Domestic Cereals Production

(Metric tons)

Commodity	UNDP/USAID	FAO	IBRD
Maize	382,000	273,000	280,000
Sorghum	226,000	295,000	260,000
Rice	10,000	10,600	N/A
Total	618,000	578,600	540,000

Although the scale of the discrepancies among these estimates is disconcerting, even the most conservative shows ENC and thus donated imparts at less than 9.5 percent of domestic production.

The 45 percent of USG commodities sold at auction to the private sector have brought prices near or slightly above import parity prices for those items. There is only limited substitutability between the imported cereals -- rice and wheat products -- and domestic ones -- maize and sorghum. This severely limits the impact of the imported donated grain on the market for domestically produced cereals.

On the other hand, there is a reason to be concerned that imports may affect domestic production adversely under specific circumstances. Food requirements (in kilograms per year) for the non-refugee populations of the SDR are as follows:

1. Source: Meeting with ENC, 15 January 1987.

Table 7. Food Requirements
(Kg per year)

Group	Ministry of Agriculture estimate	GSDR/IBRD estimate
Nomads	40	40
Rural	120	180
Urban	160	200

Total food requirements for the non-refugee population are estimated at 513,200 metric tons per year by the Ministry of Agriculture and 664,200 metric tons per year by GSDR/IBRD. When these data are compared to the production data noted previously, Somalia may already be self-sufficient in cereals in good years. Other estimates put the deficit at up to 20 percent. Following the banner years of 1984 and 1985, a surplus may even exist, particularly if one includes ADC cereal stocks and those imputed to dry-land sorghum growers. This surplus might substitute for imported cereals to the extent the coarse grains can replace fine in the Somali market.

If quantities of food aid were to increase abruptly to a greater but unknown proportion of national consumption without a corresponding prior decrease in domestic production, local production would surely suffer from lower prices. This may have occurred in the late 1970s and early 1980s.

If imports of sorghum and maize were to resume, competing directly with domestic production, adverse effects might occur. This also may have happened prior to 1984.

The 55 percent of USG commodity assistance that is distributed through the ENC is provided to institutions at subsidized prices determined by the GSDR. If these commodities were not available through imports, the institutions would have to procure the commodities on the domestic market. These purchases would tend to drive prices higher and encourage domestic production. If the quantities involved are greater, as they were in the late 1970s and early 1980s, this factor would weigh very heavily in the balance.

In the past, the arrival of commodities at or near harvest time depressed the markets for locally produced cereals. The factor is still a danger, as the Somali market is relatively volatile and subject to short-term fluctuations at the drop of a rumor.

Leakages of food from refugee programs are the least known but potentially the most dangerous of the effects that food imports may have on local cereals markets and production. Informal estimates of this leakage range from 10 to 60 percent of all rations delivered to refugees. The effect on production, particularly near refugee camps, is likely to be marked.

In summary, although the effect of food aid on domestic cereal prices and production is not entirely clear, it seems that the effect of the current quantities and composition of food aid on domestic cereal prices is minimal. Factors such as domestic production levels, storage efficiency and capacity, stocks on hand, and local food preferences may play a larger role than food aid in determining prices for maize and sorghum. In any case, the decision of several European donors to purchase between 15,000 and 30,000 tons of domestic cereals from the ADC to feed refugees in 1987 will help avoid the danger of depressing the local market.

Commodity Import Programs (CIPs) and Cash Sales Programs (CSPs) affect growth and equity in the Somali economy, including the agricultural sector, by channeling imports into priority categories that promote specific economic or social goals. While the influence of these highly conditional programs on bringing specific, badly needed reforms to the attention of the GSDR is very clear, the team could not estimate the extent to which the programs had succeeded in channeling imports into priority sectors. This matter merits further study.

V. CONCLUSIONS

Donor pressure, exerted primarily by USAID, the IMF and the IBRD, has played an instrumental role in initiating and implementing a series of liberalizing reforms undertaken since 1981 by the GSDR.

GSDR acceptance of the reform program has been generally good. Resistance to specific reforms has been unsystematic and particularistic, based on traditional loyalty groups within Somali society. Members of these groups often have interests in the perpetuation of specific elements of the state-controlled monopoly/monopsony or parastatal production/distribution systems inherited from the days of Scientific Socialism.

The reform program has had a direct and powerful impact on the crop agriculture sector, leading to increased production and increased real income for small-holding cereal producers, as well as a return of farmers to the land.

It has had an equally direct and powerful impact on the small and medium private enterprise sector in both services and manufacturing. It has led to a proliferation of enterprises and a significant rise in employment and real wages in the capital as well as in secondary towns and many villages.

The reform program's impact on the livestock sector has been less direct, since this sector was less subject to state control in the past. Preliminary indications show that producer prices have <u>at least</u> kept up with inflation and probably undergone real increases since the reforms began. The new, private export companies and associations, working with a newly privatized Chamber of Commerce, may be able to spur the sector to new growth through quality control and the opening of new markets.

The reform program's impact on macroeconomic indicators has also been generally positive; although external, uncontrollable factors, including the Saudi ban on cattle imports, international oil price fluctuations, and conflict with Ethiopia, have compromised certain positive trends.

Food aid, at present levels and composition, seems to have only a minimal effect on farm-gate prices for domestically produced cereals. However, the timing of shipments and the leakage of refugee aid into the market present serious dangers.

Civil service reforms have begun, but their effect seems minimal to date. There has been little or no effort to decentralize real governing powers, including revenue generation and use, outside of Mogadishu.

The lack of data on all sectors of the Somali economy and of institutions capable of gathering data pose serious questions about the cost of further attempts to analyze the effects of the policy reform program on growth and equity in the Somali economy. However, a number of studies and data collection efforts would be extremely useful to determine the precise results of one of the most striking examples in Africa of the influence of liberalization on a previously state-controlled economy.

APPENDIX A. BIBLIOGRAPHY

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APPENDIX B. LIST OF CONTACTS

LIST OF CONTACTS

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NA Shirwa and Sons Import and Export Commissioners

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Noor A. Shirwa, President

APPENDIX C. POLICY INVENTORY MATRIX

APPENDIX C POLICY INVENTORY MATRIX

Policy Category: Fiscal

Policy Intervention	Implementing Institution	Impact Assessment	Reforms Undertaken
Recurrent Spending	Ministry of Finance, although constrained by promises made to the Politburo.	Production - Imports - Domestic Consumption - Exports - Inflation - Government Revenues	The GOS is seeking to cut recurrent spending and hike taxes to reduce budget deficits. In recent years, deficits hade been excessive, ranging as high as 11 percent of GDP. To reduce recurrent spending, the GOS. - abolished the practice of automatic employment for all high school graduates in 1983. - has representatives in all spending ministries and agencies to review all expenditures requests before authorization in order to limit expenditures within budget allotments and to disallow low priority purchases. - reduced civil servant employment two (2) percent in 1985. Over 2,500 civil servants were retired between January and October 1985 and an additional 1,600 were awaiting President's approval for retirement. Also, 1,300 were dismissed and given the opportunity to work in agriculture or fisheries. Since October 1985, retired employees are not being replaced. - was adjusting expenditure ceilings for the remainder of 1986. Those ministries who exceeded budgetary allocations in the first half of 1986 were reduced by the same amount in the second half. In addition, there was an across-the-board reduction of five (5) percent in all ministries and no new allocations. Total savings equivalent to 12 percent of non-interest ordinary outlays were projected.

Policy Intervention	Implementing Institution	Impact Assessment	Reforms Undertaken
Taxation	Ministry of Revenue	Production - Imports Domestic - Consumption Exports + Government Revenues - Inflation	While tax revenues as a share of GDP had fallen from 8.6 to 3.9 percent over 1982-85, they were expected to approach 4.6 percent in 1986. Tax collections were up 175 percent in the second quarter of 1986 over the second quarter in 1985 and 72 percent over the first quarter of 1986. The GOS: - is altering specific tax rates to ad valorem basis; - is broadening the coverage of excise duties already in place; - is basing the calculation of import duties on a more realistic exchange rate; - is enhancing revenue collection through extensive staffing and administrative improvements; -- Mogadishu has been divided into 13 revenue collection districts. -- A concerted effort is underway to deny exemptions and require full payment of all levies. -- A survey of all commercial establishments and property is being undertaken. -- Additional collection posts are to be opened up. -- Training programs have been instituted in various tax sectors. - is implementing new taxes, consisting of (a) an excise tax effective 7/85 at ad valorem rates between 5 and 100 percent on 30 commodities, (b) a 5 percent cascade sales tax, and (c) introduction of a 20 percent surcharge applicable to non-government imports to replace a 50 percent surcharge on imports transacted through external accounts.

Policy Intervention	Implementing Institution	Impact Assessment	Reforms Undertaken

Parastatal Enterprise	Ministry of Commerce and Industry and other sectoral ministries.	Production
		Imports
		Domestic Consumption
		Exports
		Government Revenues
		Inflation
		
		Little immediate impact on any of the above variables.
			Forty nine parastatal enterprises have been established. The performance of the enterprises has been poor in recent years. Most enterprises operate well below capacity and many are facing financial difficulties. As a consequence, devolution of parastatal enterprise is taking place.
			
			- In 1982, an Inter-Ministerial Commission was set up. It is:
			  - conducting financial audits of all enterprises;
			  - recommending measures to improve enterprises' operations;
			  - seeking to reduce the number of enterprises; and
			  - standardizing accounting procedures.
			
			- In 1984, employees of industrial public enterprises were brought under the labor code that applies to the private sector.
			  - Compensation is now determined by bargaining.
			  - The GOS can offer production incentives to individual enterprises.
			  - Parastatal are free to hire and fire.
			
			- In 1984, a number of enterprises were transferred to workers' cooperatives.
			- Board of Directors are being established for each enterprise to enable them to operate more autonomously.
			- Foreign rehabilitation of some enterprises, e.g. a cement factory, has taken place.
			- Some entities that were operating uneconomically, consisting of e.g. a gypsum plant, have been shut down where rehabilitation was not feasible.
			- IBRD has agreed to finance feasibility studies for rehabilitation and divestiture of public enterprises.
			- Parastatals no longer receive preferential treatment when acquiring credit.

Policy Category: Foreign Exchange

Policy Intervention	Implementing Institution	Impact Assessment	Reforms Undertaken
Exchange Controls	Central Bank	Production: + Imports: + Domestic Consumption: Exports: + Government Revenues: Inflation:	Exchange controls are being liberalized. Exchange controls, which limited access to requisite foreign exchange, had constituted a major impediment to economic growth in Somalia. - External account facilities were opened on July 15, 1981. All Somali Nationals owning foreign exchange abroad were allowed to open external accounts in the form of either time or demand deposits. - On January 1, 1985, the opening of export promoting and import accounts denominated in foreign currencies by Somali nationals or foreigners was allowed. - While surrender requirements for the proceeds from exports of goods were hiked from 35 to 50 percent during 1986, they are still considerably lower than the 100 percent level existing prior to 1985. Although the franco valuta system under which Somali nationals could finance imports with foreign exchange abroad was abolished in 1985, the introduction of the system of import and external accounts, nonetheless, means that imports financed with foreign exchange held abroad continue, in effect, to be permitted freely.
Exchange Rate	Central Bank	Production: + Imports: - Domestic Consumption: - Exports: + Government Revenues: - Inflation: +	Since 1982, the GOS has adopted a flexible exchange rate policy; in the previous eight (8) years the currency had been pegged to the U.S. dollar at a fixed rate, thereby becoming significantly overvalued. The official exchange rate was depreciated 140 percent in 1982, 15 percent in 1983, 48 percent in 1984, and 63 percent in 1985. Under the 1985 IMF financial program a freely floating system was established for most private transactions. Also, although it was recently suspended by the GOS, an auction to be held monthly was started in September 1986, proceeds from commodity import arrangements are placed in the auction.

Policy Category: External Trade

Policy Intervention	Implementing Institution	Impact Assessment	Reforms Undertaken
Import Controls	Ministry of Commerce and Industry.	Production Imports + Domestic Consumption + Exports Government Revenues + Inflation	The GOS is easing import controls. With the exception of a relatively few items prohibited for reasons of public safety and social policy, all items can be imported without restriction; licensing requirements virtually have been abolished.

Policy Category: Prices

Price Controls	Ministry of Commerce and Industry	Production + Imports Domestic Consumption Exports Government Revenues Inflation +	Price controls have been relaxed in recent years. A de facto elimination of all price controls took place at the beginning of 1985. Prices of all products except petroleum products, cigarettes, and sugar are now set freely. As for petroleum products, in March 1986 the price of gasoline exceeded import parity and the price of diesel reached import parity in June 1986.

Policy Category: Monetary

Policy Intervention	Implementing Institution	Impact Assessment	Reforms Undertaken
Interest Rates	Central Bank	+ Production Imports Domestic - Consumption - Exports Government Revenues Inflation	The GOS is moving toward an interest rate structure designed to provide for a positive real rate of return to savers and full cost recovery on lending operations. Although interest rates remain negative in real terms, they are being hiked. The most recent instance was four percent in September, 1986.
Money Stock	Central Bank Ministry of Finance	Production - Imports Domestic - Consumption + Exports Government Revenues - Inflation	Inflation, although down considerably from the nearly triple digit levels of several years ago, remains high. Monetization of government budget deficits has been a primary causal factor. In order to control inflation, the GOS, thus, is striving to reduce the growth of the monetary stock; the expansion in net domestic credit is being reduced to eight percent. Also, the use of commodity import program (CIP) funds will be limited to $5 6,600 million with any receipts in excess of the amount to be deposited to a blocked account at the central bank rather than at the commercial bank; in limiting the loanable funds of the commercial bank, this will dampen demand pressures and inflation.

Policy Category: Private Sector

Policy Intervention	Implementing Institution	Impact Assessment	Reforms Undertaken
Private Sector Activity	Various institutions including the Ministries of Planning and Agriculture	+ Production Imports Domestic Consumption Exports Government Revenues Inflation	The GOS is seeking to stimulate private sector activity, especially in manufacturing which contributes but 5 percent of GDP. - In order to guarantee a minimum level of credit to the private sector, limits have been placed on Agriculture Development Corporation (ADC) credit extensions. - A quasi-private Chamber of Commerce has been established; the private sector also may form trade associations. - The operation of private schools and private practice by physicians are now allowed. - A revised private and foreign investment law has been approved at the technician level and was expected to be put to the Council of Ministers before the end of 1987. The la will reduce regulations and give incentives to private firm - A law allowing the formation of private commercial banks an insurance institutions has been prepared and was awaiting the President's signature. - Private importation of all goods is allowed and all livestock and bananas are exported privately.

Policy Category: Agriculture Sector

Policy Intervention	Implementing Institution	Impact Assessment	Reforms Undertaken
Marketing	Ministry of Commerce and Industry Ministry of Agriculture	+ Production - Imports Domestic Consumption + Exports Government Revenues Inflation	Significant market liberalization is taking place. In the past, most agriculture marketing was undertaken by the GOS and this constituted a drag on agriculture performance. - The Livestock Development Agency (LDA) was abolished in April 1981; livestock trade is now conducted primarily by private traders. - After 1981, the GOS discontinued the requirement that fishermen sell their catch directly to the government agency SOMALFISH at set prices, resulting in closure of the agency. Fishermen can now sell their catch at prevailing market prices. - The National Trading Agency (ENC) had held monopoly import rights for rice, wheat, flour, edible oil, pasta, sugar, tea, and most other consumer goods. They operated an extensive distribution system, supplying both public institutions and private shopkeepers with imported foodstuffs. While continuing to receive donor-funded wheat, wheat flour, oil and rice and selling them at below market prices, the Agency since 1981 no longer imports other goods, purchases no goods outside Somalia and only sells to the private sector when public sector institutional demand is satisfied. - The requirement that farmers sell their main staple products for domestic consumption to the ADC has been waived since 1982. The ADC, which had held a monopoly over the domestic grain trade, is confined to purchasing local production at prevailing market rates and selling to institutions such as hospitals, schools, and the military. Therefore, the organization is now a marginal factor in the marketing of locally produced maize and sorghum with purchases declining from 30 percent to a very small fraction of domestic production in 1985.

Policy Intervention	Implementing Institution	Impact Assessment	Reforms Undertaken
Pricing	Ministry of Agriculture	Production: + Imports: – Domestic Consumption: Exports: + Government Revenues: + Inflation: +	Prices of major agriculture products are increasingly set by market forces; support prices are revised periodically. Artificially low prices had affected production negatively. For example: - In 1981, producer prices for most agriculture products were increased 30 to 50 percent; for bananas the hike was 100 percent. - At the beginning of 1985, producer prices of bananas were doubled, amounting to a real increase of 38 percent. They were increased again by almost 45 percent at the beginning of 1986. - Minimum export prices for livestock now move in line with current market conditions.
Input Supply	Ministry of Agriculture, Ministry of Commerce and Industry, Ministry of Health	Production Imports Domestic Consumption Exports Government Revenues Inflation Little Impact in near term on the above variables.	The GOS is encouraging private sector distribution of agriculture inputs which consist primarily of tractors, oil, fertilizers, veterinary drugs and pumps. - The GOS is to permit any private individual, group of individuals, or company to obtain licenses to import diesel fuel and lubricants and distribute them through private channels without additional charges. - ONAT, the state tractor service company, has been subsidizing tractor rentals, discouraging private sector distribution. Under the IBRD Agricultural Sector Structural Adjustment Program (ASSAP), ONAT will be required to achieve full cost recovery for tractor rentals. - The GOS is increasing the number of non-prescriptive veterinary drugs classified as safe for private imports.

Policy Intervention	Implementing Institution	Impact Assessment	Reforms Undertaken
Parastatal Enterprises	Ministry of Agriculture	Production Imports Domestic Consumption Exports Government Revenues Inflation Little impact in the near term on the above variables.	Some devolution of parastatal enterprise is taking place. With few exceptions, none of the public sector enterprises processing agricultural products or providing agricultural services had been able to cover costs and most were making substantial losses. In addition to closing the LDA and SOMALFISH and restricting the operations of the ADC and ZNC, the GOS transformed the National Banana Board on August 1, 1983 into a joint venture company, SOMALFRUIT. The Board is now owned 60 percent by DeNadai -- a multinational headquartered in Italy -- and 40 percent by the GOS. With the help of external assistance, the GOS has rehabilitated the Mogadishu Dairy and the Juba Sugar Plant and milk and edible oil factories have been shut down. The GOS also may rationalize the operations of the Hide and Skins Agency (HASA). A study is underway and agreement must be reached between the GOS and the World Bank on the disposition of HASA prior to release of the second tranche of the ASSAP.

APPENDIX D. MATRIX OF DONORS AND POLICY ISSUES

APPENDIX D

MATRIX OF DONORS AND POLICY ISSUES

The following table attempts to present a superficial image of donor stances on a wide range of policy issues that affect the agricultural sector in Somalia. We had first intended to put simple yes/no codes in each box that would represent the attitude of a particular donor to a particular policy option. However, the response from the donor representatives were too varied to permit such a black/white interpretation.

The donor opinions reproduced in the table are drawn largely from interviews with representatives in Somalia. Exceptions are the World Bank, whose Somalia Desk Officer in Washington was kind enough to receive us and which has written policy option documents; and the IMF and USAID, which also have written policy option papers that the team has read. While the IMF, ~~and~~ the IBRD and USAID have active stances on all of the policies mentioned in the table, the other donors usually do not. The French, German, and UN agencies do not attach any conditionality to their aid and thus only engage indirectly in policy dialogue. They say they are here to help the GSDR or to act for humanitarian and/or political reasons. The Italians are the most important bilateral donor in Somalia, but their program is coordinated very little, if at all, with those of the other donors. Most of their assistance is outside the PSIP and is conceived in reaction to the pressures of GSDR requests and Italian commercial interests.

Donors	Exchange rate unification	Exchange rate freedom	Civil service reform	Privatization of parastatal	Recurrent costs	Interest rates	Liberalized marketing	Liberalized input supply	Bank privatization	Surrender requirement	End price control	Food aid
USAID	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Low as possible	Yes	Yes
IBRD	Yes	Yes	Yes	Only when appropriate	Yes	Yes, but might accept subsidies for some sectors	Yes	Yes	Yes	Ok as tax at these rates	Floors, ceilings	No
IMF	Yes	Not necessary	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Necessary	Floors, ceilings	No
Germany	Yes, support IMF	Not necessary but nice	Yes	Yes	No	Yes, weakly	Yes	Yes	Yes	--	Floors, ceilings	No, UNHCR only
Italy	Yes, Weakly	Yes, weakly	Yes, weakly	Ambiguous	Italy will pay them	Yes, weakly	Yes	Yes, weakly	No hope	--	Slow, gradual	No
France	Favor but don't expect it	Yes	Yes, strongly but no action	Yes, lead to investment	Not much	Yes	Yes	Yes	Yes, but not French bankers	Eliminate if possible, useful as tax	Yes	No
UN Agencies	Not interviewed	Not interviewed	Yes, but only pushing	Where appropriate	Yes, but not pushing	Not interviewed	Yes	Yes	Not interviewed	Not interviewed	Floors, ceilings	Yes (WFP)

APPENDIX E. RECOMMENDATIONS FOR PHASE II RESEARCH

APPENDIX E
RECOMMENDATIONS FOR PHASE II RESEARCH

Time limitations have kept Phase I of the Agricultural Sector Policy impact assessment to a cursory examination of the origins and results of Somalia's Structural Adjustment Program. Phase II is to carry out an in-depth evaluation of the effectiveness and distributional impact of the GSDR policy reform program.

The need for additional studies and data is enormous in Somalia. Even more important, existing data are unreliable and often contradictory. The only exception is the banana industry where SOMALFRUIT appears to be doing a creditable job producing the requisite information. Somalia's deficiencies in data and studies can only be solved over the medium and long term through a program of institution building and strengthening.

Mounting an extensive data collection effort and undertaking a series of studies over the near term will be costly enterprises in both money and human resources. If they are not carried out in the context of an institution-building process, the reliability and usefulness of their products may be questionable.

As with any development project, the costs and benefits of any new data collection and studies effort must be assessed. The gains which spring from the program, as well as the sustainability of those gains, should be clear before the program is undertaken.

A number of studies would further our knowledge of the Somalia economy and help us in assessing the impact of economic policy reforms.

Internal Labor Markets in Somalia

A study of internal labor markets should be undertaken, including the analyses of formal sector employment, wages, recruitment, and career posts; urban/informal sector labor markets; and rural wage market. Connections between wage labor and the income strategies pursued by rural-based extended families should be probed. At present, there is no systematic collection of unemployment and wage data by the GSDR.

Microstudy of Household Income Strategies

An effort must be mounted to address the income-generating strategies of extended families. The primary objective would be to understand and predict responses to changing incentives. For example, the degree to which subsistence and marketing inputs are readily shiftable, whether incentives to produce grain will withdraw resources from animal production within household economies, or what the impact of import incentives will be on migration to the Gulf can only be analyzed when household strategies are understood. We also need to know on what households spend their income. Over the longer run, such information should be collected periodically through ongoing research studies on a panel of households in order to provide information that is comparable over time.

Regional Income Strategies

A clearer picture is required of the strategies by which households and extended families in the various regions in the country -- dryland, irrigated, and pastoral -- obtain income, avoid risks due to uncertain rainfall, save and invest. For instance, what factors determine the quantity of grain stocks held by farmers in the Bay Region and how do these stocks affect prices and output?

Commodities Market Study

A study of agricultural markets is needed urgently. The study would clarify the response of livestock offtake rates and exports to price changes; the supply response of grains and other commodities; the effect of current import release prices; the production costs and farmgate prices of the various agriculture commodities; the price levels and costs of production at which farmers switch from (a) cereals to sesame, fruits, vegetable, (b) maize to rice, and (c) food to fodder; and the costs for potential ADC stabilization efforts. Since crucial assumptions about the functioning of these markets are presently being made on the basis of little systematic information, a significant improvement can be made by collecting and analyzing data available from municipal records and other sources, including selected interviews. For example, producer price series for maize and sorghum do not exist; only ADC official prices for the commodities are available. The producer price

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series, together with data already available on retail prices, would provide valuable information on the share of benefits accruing to producers and retailers.

A Study of Pastoralism

One of the major deficiencies in our study is the lack of knowledge about the impact of structural adjustment on livestock herding. We feel that, on balance, herders have benefited from the reform program. Yet, the data are simply unavailable. The impact of the adjustment program on livestock traders also requires clarification. We require domestic arrival prices, herd gate, and retail prices. The Mission-funded livestock marketing study may help sort out these questions.

Institutional Analysis Inventory

Additional details are required on what institutions, including GSDR, parastatal, private, and PVO, work in crops, livestock, fruits, extension, etc. The inventory would discuss their goals and plans, relationships among each other, and resources.

In addition to the studies above, there are a number of specific data needs.

- Data on the distribution and uses of land holdings for dryland farming and irrigated agriculture are needed. Time series data on who plants what, where, how much, and why should be collected.

- To assess more fully the impact of moving toward more realistic exchange rates, more accurate and more timely data on the composition of imports is required.

- Analysis of the impact of food aid on domestic production requires further analysis of (a) the substitutability of domestically produced sorghum and maize for imported cereals -- rice and wheat products -- and (b)

the leakages of food from refugee feeding programs.

- We need to know who is getting agricultural credit and for what purposes. Information also is required on the informal (nonbank) credit system.

- Whether sorghum can be used economically for fodder also is of interest.

APPENDIX F. BANANAS: THE FORGOTTEN EXPORT

APPENDIX F. BANANAS: THE FORGOTTEN EXPORT

Somalia exports two agricultural products, livestock and bananas. Banana exports, which had fallen to 34,300T in 1981 from 81,800T in 1975, advanced more than 75 percent over 1984-86, reaching 62,400T at the end of the period. While banana exports had fallen back in 1984-85, they were still almost 30 percent higher by the end of 1986 than they had been in 1981. Yet no banana projects are listed in the 1986-1988 Public Sector Investment Program of the GSDR. While millions pour into irrigated maize, rice, and sugar projects and further millions into dry-land sorghum and range management projects, bananas stand alone, ignored by the major donors and by the GSDR.

Somalia's agricultural investors do not seem to neglect the sector in the same way. By all reports, a land rush has begun in the banana planting areas between the Shebelle and Juba Rivers. Small farmers are beginning to plant more of their land to this crop and important politicians and Mogadishu merchants are purchasing or leasing banana plantations. In 1981, 3,600 hectares were planted to bananas in Somalia. By 1985, there were 5,700 hectares. In 1986, planters under contract to SOMALFRUIT planted 6,150 hectares. Banana production has risen more slowly than hectarage planted because the newer farmers are not as adept at exploiting their resources as are the veterans, but there is significant potential for expansion of this crop, which furnishes important sums of desperately needed foreign exchange to the SDR and remunerative employment to thousands of Somali workers.

The FAO reports that the average banana crop in Somalia between 1981 and 1985 was 77,000mT. From 1976 to 1980, the average was only 52,000mt/year (FAO, October, 1986, p.9). General opinion in Somalia avers that about 2/3 of the crop is exported each year, or about 50,000T, which correlates exactly with the IBRD estimate of 52,000T of bananas exported in 1985 (IBRD, January 1986, p.16). These 1985 exports represented SS 533,200,000, a not inconsiderable sum (FAO, op. cit., p.18).

What has happened to revitalize banana agriculture in Somalia? During the 1970s banana production declined regularly, planters replaced bananas with other crops, investment dried up and secondary industries based on bananas failed. By 1979, the Ente Banana (Parastatal Banana Board), the GSDR agency which held the monopoly on banana purchasing and exports, called in two Italian experts to see what could be done.

Mr. Silvano Fantoni is an agronomist who had been a banana planter in Somalia until 1970. He left just after the state took control of the banana sector. Mr. Luciano Guidotti came to Somalia just after Mr. Fantoni left. He was part of a group of Italians who took a 49 percent share in a factory in Kismayo that was to manufacture crates for the export of bananas. The GSDR owned the majority of shares in the factory. They estimated that with normal development of the banana plantations, they would soon manufacture 10 to 15 million crates per year.

They began construction and the factory was ready in 1973, but by then the banana sector had already begun to fail. The economic results of the factory were mediocre at best and the 150 or so small planters, of whom about 100 were Italians, began abandoning bananas for other crops, or else left agriculture entirely.

By 1979, Mr. Guidotti had become the owner of the entire minority share (49 percent) of the crate factory. He felt that to save his stake, he needed to do something to increase banana production. He thus called upon the Ente Banana to invite Mr. Fantoni to Somalia to advise them. They accepted and Fantoni undertook a study on rehabilitating banana production in Somalia. This invitation may represent the first timid step toward liberalization of the Somali economy after the multiple debacles of the years 1977-1979.

Between 1980 and 1983, Mr. Fantoni and Mr. Guidotti worked for the Ente Banana in the increasingly market-oriented atmosphere of the SDR. They first looked for technical ways to increase banana production. They worked with the same group of small farmers who had stuck with bananas throughout the period of Scientific Socialism and got some decent results, working on:

- Fertilization,
- Soil preparation,
- Plant maintenance,
- Chemical applications,
- Banana preservation for shipment/export, and
- Mechanization

They exerted themselves particularly to obtain badly needed foreign currency for imports of machinery, spare parts, and agricultural chemicals. The lack of these inputs had constituted one of the major reasons for the decline in the sector before 1979. The tighter foreign exchange became, the more farmers switched to other crops and the more farms that were abandoned. Fantoni invested a great deal of time and energy in convincing the farmers that the foreign exchange would be available when needed.

But when Fantoni and Guidotti thought about the process of banana production for export, they realized they could not do the job themselves. They could carry out the arduous and complicated task of planting, caring for and harvesting bananas. They could master the technically rigorous processes of treating, cleaning, packing, storing and shipping the bananas to a seaport. But they also needed someone who could transport the bananas to profitable markets and find buyers for them. They needed a central point of coordination for the whole banana exporting business.

The Ente Banana had proven itself incompetent at this task. In spite of its official government-given monopoly on all marketing and exporting of bananas, it had failed to coordinate the different operations so necessary to successful banana exporting. They did no marketing work at all. They had no idea of what the international banana market required: types of fruit, quality, shape, size, packing, quantities, etc. In addition the GSDR simply did not have the money to invest in the banana sector in the way that Fantoni and Guidotti felt was necessary to make it profitable.

Thus in 1983, they began looking for outside help. Fantoni contacted the De Nadai Group, an Italian conglomerate that had sufficient capital, owned its own sea transport and had much experience in the international fruit trade, especially in bananas. The Group agreed to ask the Ente Banana to sell them a 60 percent share in the agency for $3,277,000. Since then the Group has invested over $20 million in the new company, SOMALFRUIT. They have purchased three large farms in the irrigated area and now produce 35 percent of the export crop themselves. The rest comes from 114 farmers, including 14 Italians. Most plant between 10 and 100 hectares. In addition to the establishment of the three farms, their investment went for machinery, equipment, inputs, etc.

The Group's only activity in Somalia is the export of fruit. After three years, they have recovered about half their investment. The GSDR has conceded them the right to reinvest all their export earnings until the industry is on its feet. But all has not gone smoothly, in spite of recent increases in banana production and exports. Most of SOMALFRUIT's major problems arise from the confusion and irregularities of the Somali rules, codes, and regulations dealing with foreign investment, customs, creed, foreign exchange, and banks. The 1985 MF ruling that all Somali import/export transactions had to pass through the CSBS was an administrative disaster, slowing all aspects of the process dramatically.

But in spite of its problems, SOMALFRUIT is working quite well. Its management feels that it is the agricultural activity in the country that pays its own way. They have had about $5 million in support from Italy, where they buy all their equipment and other inputs but have received no other external support. At the 1986 level of exports of 57,000T, they are far from saturating their potential market, which could probably absorb up to 120-150,000mT. Their production goes entirely to Italy and the Arabian peninsula. In 1985, Italy took 51 percent of the crop. In 1986, it took 62 percent. All fruit is sold at international market prices. They do not have a sweetheart deal with Italy, guaranteeing a market at an above-market, subsidized price. SOMALFRUIT will probably not be able to enter other markets in a major way because Italy and Somalia do not have the international political clout needed for such penetration. France, for example, buys most of its bananas from its former colonies in Africa, the U.S. from its allies in Central America.

SOMALFRUIT runs its own agricultural credit operation for its contract farmers. The company provides all necessary inputs and the farmers pay from 0 to 50 percent down. SOMALFRUIT collects the rest from the price they pay for the bananas at harvest. Although they do not have an official monopoly on banana exports, no one else in Somalia can hope to sell overseas. Thus far they have had no problems at all with recovering their money.

The company employs approximately 400 people full-time. This includes 102 who work permanently in 10 packing centers and another 300 or so in offices and farms between Mogadishu and Kismayo. In addition, it provides part-time employment for nearly 50,000 people as pickers, porters, packers and the like. SOMALFRUIT management estimates that this employment is the equivalent of 15,000 full-time jobs. For the most part, these part-time workers are farmers living around the banana area, who are not looking for full-time jobs.

SOMALFRUIT has looked into the possibility of exporting other Somali fruit to Europe or Arabia. Without major investments, this does not seem possible. The Arabs do not eat much grapefruit and Italy imports its supplies from Israel where the production is large, uniform, attractive and relatively inexpensive. Production of mangos and papayas is too irregular and the fruit is not uniform enough for packing or marketing. They have sold small quantities of watermelons as off-season crops in both Italy and Arabia, but both countries grow their own and the potential for market expansion is very limited.

SOMALFRUIT claims that the Somali banana is very hard to grow. Soil and climate conditions make it difficult and expensive to produce. For this reason, it is one of the best tasting, most nutritious bananas around, they say. They feel that it will earn its share of the world banana market and maintain a profitable, private banana industry in the SDR.

Banana Production and Sales 1984-86

1984			
	MIDDLE EAST	33,000t	$9,366,000
	ITALY	14,772t	$4,890,000
1985			
	MIDDLE EAST	16,130t	$4,545,000
	ITALY	29,190t	$8,461,000
1986			
	MIDDLE EAST	22,035t	$6,135,000
	ITALY	35,907t	$10,439,000

APPENDIX G. REMAINING REFORMS

APPENDIX G: REMAINING REFORMS

While the number of reforms that the GSDR has already implemented is impressive, the reform effort remains incomplete. Much work must still be done.

Public finances need to be strengthened further; budget deficits remain far too large. Civil servant rolls must be pared back more quickly and salaries which have remained unchanged through seven years of inflation require a significant adjustment upward. Taxes, in spite of omprovements in collection, remain quite low by international standards. Any further alterations in the tax system should be as growth-enhancing as possible.

The Public Sector Investment Program (PSIP) requires further rationalization. Still projects are not prioritized; recurrent costs are not taken into consideration; and economically non-viable projects are pursued.

Parastatal enterprise must be restructured. Forty-nine parastatal enterprises exist today in spite of GSDR promises to discard or privatize many of them. The performance of nearly all the enterprises is poor. Their failure creates obstacles to normal growth in many sectors of the economy.

While the foreign exchange auction was proceeding well until its recent suspension by the GSDR and a freely floating rate has been established for most private transactions, the official rate remains significantly overvalued. The GSDR must implement a foreign exchange system that produces a realistic rate.

Although interest rates have been hiked on a number of occasions in recent years, they remain negative in real terms. The GSDR needs to adopt an interest rate structure that will provide for a positive real rate of return for savers and full cost recovery on lending operations.

GSDR intrusion in the process of financial intermediation may be excessive; all financial intermediaries continue to be GSDR-owned. Although a law allowing the formation of private commercial banks and insurance institutions has been prepared, it is still awaiting the President's signature. Certain foreign banks have been approached about joint ventures with Somali groups, but interest has been limited. In any case, appropriate regulations do not exist yet.

In agriculture, while a number of policy impediments remain, the most significant relate to land tenure and parastatal enterprise. The GSDR does not have a land tenure policy; only a very rough cadastral survey has been undertaken. While state

lands are being allocated to private farmers, the tenure arrangements are uncertain. Parastatal monopsonies in hides and skins (HASA) and frankincense and myrrh, both of which provide the private supplier with insufficient inducements for production, should be eliminated. Also, the ENC should cease selling grains received from abroad at below market prices.

The GSDR must establish an economic atmosphere conducive to development and growth of the private sector. It must approve draft regulations and procedures for foreign and national investors. The Chamber of Commerce must become a true voice of the Somali private sector. Somalia must establish policies which will enable the nation to prosper using its own resources.

APPENDIX H. METHODOLOGY

Office and the Agriculture Office were ready with time, advice, documents and opinions as required. The Director's Office also provided an atmosphere of encouragement and interest in our work. Officials of the GSDR were generally helpful, but lacked access to detailed and specific information about the impacts of policy on the agricultural sector. Representatives of other donors were also very forthcoming and provided us with what data they had. All were ready to discuss agricultural and macroeconomic policies and to speculate on their impacts.

APPENDIX H. METHODOLOGY

To carry out this study, USAID contracted with Development Alternatives, Inc. and Robert R. Nathan Associates (RRNA) under the Macro-Economic Analysis IQC (No. PDC-0000-I-00-6135-00) to provide a multidisciplinary team in collaboration with the Africa Bureau Development Policy Division. A three person team, composed of an institutional analyst/team leader, an agricultural economist and a macro-economist, carried out the assignment.

The team met in Washington with the staff of AFR/DP and with teams going to Mali and Zambia from December 17 through December 19. We discussed the purpose of the assignment and began collecting background materials. After leaving the U.S. on January 4, 1987, the team suffered a three-day delay in Rome, thanks to a broken Somali Airlines airplane. We used this time to read through the literature on Somalia and to plan strategy for our arrival in country.

We finally arrived in Mogadishu during the night of 8/9 January and began work immediately. We remained in Mogadishu through 16 January, meeting with officials from USAID, other donors, the private sector, and the GSDR. On January 16 and 17 we travelled to Baidoa, via the Shebelle River Valley, to visit irrigated and dry-land agricultural areas, as well as a pastoral rangeland zone. The staff of the Bay Area Rural Development project were extremely helpful and hospitable to us during this visit.

We remained in Mogadishu during the remainder of our stay except for a one day trip to Merca, Correoli and the lower Shebelle Valley on 24 January. We continued meeting with representatives of the GSDR, the private sector, USAID and other donors while we prepared a draft report, which was submitted to the Mission on 22 January. On 25 January, the Mission held a debriefing session and offered us their comments on our draft.

After our return to the U.S., the team presented the draft report to AFR/DP on 28 January and attended debriefing seminars on 29 January and 5 February. Final drafts incorporating suggested revisions were submitted to AID on February 20.

During our stay in Somalia, the team noted the dramatic scarcity of reliable quantitative data on economic and social trends in the country. For this reason, our assessment was based largely on impressionistic and anecdotal evidence. When statistics appeared, they were often contradictory and ill-defined. To use them we chose the worst-case sets and applied them to our hypotheses. Our conclusions are thus tentative, but we have a great deal of confidence that thorough research would verify them.

The USAID Mission in Somalia was extremely helpful, both logistically and substantively during our stay. The Program

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APPENDIX I. AGRICULTURE CREDIT

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The level of demand for agriculture credit can serve as an indicator of the vigor of economic activity in the agriculture sector. Historically, agriculture credit in Somalia has gone for marketing, rather than productive, purposes.

Lending Institutions

The two institutions that provide agriculture credit are the Commercial and Savings Bank of Somalia (CSBS) and the Somali Development Bank (SDB). Agriculture credit, which totaled over SS 1 billion over 1975-85, is divided about equally between the CSBS which lends short-term (10-12 months) and the SDB which lends medium-term. Virtually no long-term (7-20 years) lending takes place. Most credit went for livestock marketing where repayment rates seem to have been low.

A small farmer credit program was begun in 1983 in CSBS with the help of the UNDP. Under the program, seasonal production credit is provided; operational expenses incurred during planting are funded and repayments are made at the time of harvest. The small-scale farmer, since he cannot put up collateral, furnishes a promissory note; the chief of the farmer's clan, in turn, takes up the responsibility for ensuring repayment. This pilot program is the first of its kind in Somalia. UNDP and FAO, which implement the project, found that demand for credit was low originally. However, rising producer prices, effective extension, and the availability of inputs, including seeds and fertilizer for non-traditional crops, has led to steadily increasing demand. The program is considered an outstanding success; pay back rates range as high as 95 percent.

As for the SDB, agriculture credit ranks first among sector priorities. SDB agriculture credit funds clearing of

agriculture lands, tractor services and other inputs, and irrigation. The CSBS and the SDB have many shortcomings, related mainly to their limited capacity to evaluate loan proposals adequately, monitor use of funds, and recover repayments. IDA has provided assistance to the SDB to strengthen the work of the institution. The results, however, fell short of expectations.

Interest Rates

In spite of increase in agriculture interest rates -- most recently in January 1985 -- rates remain sharply negative in real terms. Recently, however, there have been indications that interest rates are becoming less negative in real terms.

Table I-1. Interest Rates

	CSBS rates	SDB rates	Inflation
1981	10	10	44.6
1982	12[a]	10	22.6
1983	12	10	36.4
1984	12	10	92.2
1985	15[b]	14[b]	37.9
1986	15	14	33.8

a. Altered June 30.
b. Changed January 1.

According to these data,[1] agricultural interest rates increased in real terms with the start-up of the SAP in 1981, fell with the backsliding on the reform effort over 1983/84, and are now again rising in real terms.

1. Deposit rates also have been sharply negative in real terms; ranging from 6 to 9 percent in 1981, they now vary between 16 and 26 percent.

Experience in many countries has shown that negative real interest rates in agriculture have generally not had long-run beneficial effects on production and income and have mainly benefitted the large farmers, who normally have better access to the limited pool of subsidized credit. Under negative real interest rates, the interest rate no longer serves as the allocating mechanism for credit; that role is delegated to creditworthiness and politics. Since larger farmers tend to be more creditworthy and better connected, small farmers are denied credit.

Moreover, rates for small farmers are subsidized by the CSBS and SDB relative to rates for other entities. Differential lending rates for CSBS were essentially introduced on January 1, 1985. While the rate for small-scale farmers was set at 15 percent, rates for public and private enterprise were fixed at 19 percent and rates for foreign-owned enterprises at 20 percent. Since 1981, SDB rates for agriculture have been subsidized vis-a-vis rates for other subsectors, although the relative subsidy has been going down marginally in recent years. Since rates for farmers are subsidized by CSBS and SDB relative to rates for other entities, lending to agriculture has been discouraged relative to other subsectors.

Generally speaking, no significant production credit has been available to farmers seasonally, except through the UNDP program, and no credit links were forged in the input delivery or crop marketing system.

There has been a lack of agreement among donors on the issue of subsidized agriculture credit. Some seem willing to accept subsidized rates in priority sectors such as agriculture.

Impact of SAP

The SAP produced significant increases in agriculture credit extensions over 1981-82. In sharp contrast, over 1978-80 the portfolio of agriculture loans outstanding at the CSBS fell drastically, declining by 45 percent in real terms. Total agriculture credit was up SS 198 million in both 1981 and 1982. In real terms, credit flows to agriculture in 1981 were four times what they were in 1980, while the comparable increase in 1982 over 1980 was three fold. By the end of 1982, CSBS agriculture credit added up to almost 25 percent of total credit outstanding compared to 18 percent two years earlier. Clearly, the elimination of parastatal monopsony, including the move toward more liberal

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pricing policies, the increases in real interest rates, and the good weather, contributed to the robust credit demand over 1981-82.

Another very encouraging development that has taken place since commencement of the SAP is the increasing share of agriculture credit going to the private sector. In 1981, the private sector accounted for 35 percent of total CSBS agriculture credit extensions; by 1984 the proportion was 83 percent.

Retrenchment in agriculture credit extensions, however, was in evidence over 1983-85. In the beginning of the period, excessive government borrowing "crowded out" the private sector, including agriculture. At the end of the period, the GSDR moved to tighten monetary policies as mandated by the stand-by arrangement with the IMF. Credit flows to agriculture actually declined in nominal terms in both 1983 and 1985. By the end of 1985, agriculture's share in total CSBS credit had declined to 10 percent.

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APPENDIX J. LAND USE AND TENURE

APPENDIX J. LAND USE AND TENURE

Land tenure in Somalia presents a serious potential constraint on development. Traditional and modern systems of access to land exist side by side, occasionally in harmony, sometimes in conflict, but with a general effect of generating a feeling of insecurity in a domain where long-term investments in secure holdings are necessary for continued progress and development.

Tenure conditions vary among the three major categories of land use in Somalia today: pasture, irrigated agriculture, and dryland agriculture. But the traditional principle of Somali access to resources holds for all three. Historically, Somali herders and farmers had rights to use but not sell land, according to their membership in clans. The longer a piece of ground had benefitted a particular family or clan, the stronger their claims to continued use became.

Before the coup of October 1969, little attention seems to have been paid to land tenure questions. Farming has always occupied a low status in the hierarchy of traditional Somali values and farmers were seen as hard working, low-income drudges, dependent for protection and support on nomadic herder groups.

However, after the coup, attitudes both toward traditional ways of doing things and toward land changed dramatically. One of the primary policies of the early years of scientific socialism in Somalia was the proscription of reference to traditional Somali clans for any purpose whatsoever.

The Somali government, under Soviet tutelage, clearly considered land an important capital resource which the state should control. Beginning in 1975, when the GSDR enacted Law Number 73 declaring the state owner of all land

in the country, the government has moved to substitute itself for the traditional Somali clans as the ultimate repository of land, granting usufruct to members of the corporate group -- in this case the entire nation.

This policy had a number of consequences:

- Combined with low producer prices in agriculture, it severely restricted farmers' willingness to invest in land which they or their families had not occupied for significant periods of time.

- Significant quantities of good quality agricultural land were expropriated for the use of state farms, settlements of former nomads and state-owned agricultural enterprises.

The land tenure situation, combined with (1) the inefficiency of state-run production enterprises and purchasing monopsonies and (b) the failure of parastatal import monopolies to provide desired producer inputs and consumer goods at affordable prices, led to stagnation, if not decline, in the crop sector of the economy during the years of Scientific Socialism. Livestock production, measured in terms of exports, rose during the same period. The main difference between the crop and livestock sectors was that the government was unable to intervene effectively to take public control of marketing, production, or access to land from private herders or merchants.

After the series of misfortunes which afflicted Somalia during the late 1970s, including droughts, wars, inflation, depletion of foreign exchange reserves and abandonment by their major international supporter, the GSDR turned in the early 1980s to a reform program orienting the economy as a whole to the free market. Unfortunately, the series of reforms which have taken place have dramatically influenced land values without establishing a consistent, comprehensive and comprehensible system of land tenure laws and land use priorities for the nation.

The value of crop land has risen as returns to crop agriculture have soared following the liberalization of trade in cereals and other crops in 1981-82. In particular, the supply of irrigated land is very limited.

- Somalia's two rivers supply limited quantities of water.

- Much irrigated land has suffered from poor drainage and thus from waterlogging and salt build-up.

- Inefficient state farms, settlements, and enterprises occupy much choice land.

- GSDR officials and rich urban merchants have begun occupying land for commercial plantations as returns to land increase.

The GSDR, at donor urging, has undertaken certain measures to palliate the land tenure problem. They have:

- Broken up a number of state farms formerly run by the Ministry of Agriculture

- Broken up some of the settlements and distributed the land to occupants

- Deemphasized the policy of forcing nomads (transhumant herders) to give up their traditional life style and settle in agricultural communities

- Continued the policy of non-interference with lands devoted to export crops, i.e. bananas

The series of laws about land tenure promulgated under Scientific Socialism call for the leasing of all crop and pasture land for long periods of time (usually 50 years, although the team also heard of 10, 20 and 30 year leases) and at low taxation rates based on areas leased and the probable use of the land. However, leasing calls for a good deal of time and expense to follow administrative procedures through their convoluted paths, pay for accurate surveying of lands, and to settle all potential disputes to particular holdings.

The team was unable to find out more about the actual application of the leasing laws, but we had the impression that:

- Although leasing activities have increased dramatically in recent years, most of it has been by new arrivals on the crop-agriculture scene -- functionnaires who have received access to land in lieu of severance pay from the GSDR; politicians and merchants who are investing in crop agriculture; the new class of transhumant farmers who will leave the cities to farm as long as conditions (weather, prices, etc.) are propitious, but return to the cities when they are not -- not by the traditional users of the land.

- There is little confidence in the permanence of current land allocations under the existing laws. This seems to be limiting investments to a certain extent, especially among those who feel most vulnerable to changes in tenure priorities or rules -- the newly arrived farmers.

- There is serious potential for conflict among those who propose to use land for pasture and those who prefer to crop it, especially if they are not members of the same or allied traditional clan groups.

The issues of land tenure and land use have yet to receive the attention they deserve in the policy reform process in Somalia. Land reform, or at least systematization of the rules and regulations as well as of their application, should rank high among the policy priorities of the coming year.

Specific points of attack might include:

- The establishment of a simple, fast, inexpensive way to survey, mark, and register lands

- Recognition of the difference in tenure criteria of irrigated, rainfed, and pasture land

- Recognition of the difference between securely held land that has been exploited for generations by one family and less securely held land that has recently been occupied under modern rules

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- Establishment of special rules for the occupation of crop land by refugees

- The assurance of real title security to those who do register their land

- The preparation of a national land use plan, establishing priorities and locations for pasture, crop, urban, public, private and reserved land, particularly for construction, rehabilitation, and maintenance of infrastructure which enhances the value of land

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