# Liberian Lessons:
## Enhancing Somalia's Debt Relief Process

Briefing Paper

Supported By

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# Acronyms

| | |
|---|---|
| ADF: | African Development Fund |
| AfDB: | African Development Bank |
| AMISOM: | African Union Mission in Somalia |
| AU: | African Union |
| CGD: | Centre for Global Development |
| EU: | European Union |
| FCAS: | Fragile and Conflict-affected Situation |
| FDI: | Foreign Direct Investment |
| FGS: | Federal Government of Somalia |
| FMS: | Federal Member States |
| G7: | Group of Seven |
| GEMAP: | Governance and Economic Management Assistance Programme |
| HIPC: | Heavily Indebted Poor Country Initiative |
| IFIs: | International Financial Institutions |
| IMF: | International Monetary Fund |
| LDCs: | Least Developed Countries |
| MDRI: | Multilateral Debt Relief Initiative |
| NDP: | National Development Plan |
| NTGL: | National Transitional Government of Liberia |
| PFM: | Public Financial Management |
| PIP: | Public Investments Program |
| SMP: | Staff Monitored Programme |
| SRBC: | State and Resilience Building Contract |
| TSF: | Transitional Support Facility |
| UCT: | Upper Credit Tranche |
| UK: | United Kingdom |
| UN: | United Nations |
| UNMIL: | United Nations Mission in Liberia |
| US: | United States |
| VNSAs: | Violent non-state armed actors |

# 1. Introduction

Liberia and Somalia both experienced a protracted civil conflict from the late 1990s to the early 2000s, with sporadic episodes of violence still continuing in Somalia. The prolonged absence of a functioning government made both countries fall behind on their external debt payments throughout the conflict period. In an effort to end years of conflict, the international community re-engaged both countries and sought to address their external indebtedness through the Heavily Indebted Poor Country (HIPC) Initiative.

Liberia was able to complete the HIPC Initiative in a four-year period, while Somalia is yet to qualify for the initiative (i.e., reach its Decision Point[1]), six years since it initiated its engagement in the debt relief process. At the time of their respective re-engagements with the international community, the two countries shared economic and political challenges, as both countries were classified as fragile and conflict-affected situation (FCAS), least developed countries (LDCs) with sizeable and protracted arrears to external creditors. There are many Liberian lessons for Somalia.

This briefing paper[2] aims to examine similarities and differences between Somalia and Liberia in their engagement in the debt relief process, allowing Somalia and its development partners to draw useful insights and lessons learned (see Section 5) that if applied in Somalia could accelerate its debt relief process. It presents four key success factors - progress towards a durable cessation of violence and socio-political stability, human and institutional capacity, political leadership and the support of a champion - that facilitated the acceleration of Liberia's debt relief process and compares how Somalia fares in those factors. The paper finds that, with respect to the key success factors, Liberia and Somalia's experience were comparable, with the exception of one factor, which can partly explain Somalia's sluggish debt relief process in comparison to Liberia. Similar to the Liberian experience, since 2012, Somalia is making progress toward reaching a durable political settlement and in achieving peace and security and continues to strengthen its institutional and human resource capacities. Somalia's executive leadership has shown its willingness to provide strong and sustained political leadership to steer the country's engagement in the debt relief process – although much can be learned from Liberia's experiences. Despite these similarities, Liberia has had no recurrence of violence since the internationally-brokered peace agreement of August 2003, while Somalia

1 The Decision Point is the point in which the Board of Executive Directors of IFIs qualify a country for debt relief (see Somalia NGO Consortium 2018. Debt Cancellation for Somalia: The Road to Peace, Poverty Alleviation and Development for more details).

2 As part of the research for this paper, interviews conducted with individuals who had served in government positions and advisory roles that had been deeply involved in Liberia's engagement in the HIPC Initiative and related debt relief processes were used to draw information included in sections of this paper.

continues to try to reach a durable political settlement and faces violent challenges from violent non-state armed actors (VSNAs). Another salient difference between the two countries is that Somalia lacks an influential creditor country that can champion the country's debt relief aspirations. This finding suggests that, if Somalia is to have an expedited debt relief process that restores access to additional grant and concessional resources and private investment inflows, an influential country should assume the role of a champion.

The paper also briefly examines Liberia's economic performance and its current external debt situation post-HIPC (see Section 3.1) to draw lessons (presented in Section 5) that could help Somalia avoid some pitfalls Liberia experienced during its post-Completion Point[3] period.

The paper comprises the following sections:

- Country contexts - Liberia and Somalia;
- Evolution of Liberia and Somalia's external debt and their experience in the debt relief process;
- Key success factors for an expedited debt relief process and country performances; and
- Conclusion and lessons learned.

3 The Completion Point or Floating Completion Point is the point at which external creditors provide irrevocable debt relief and requires the completion of additional IFI conditionalities (see Somalia NGO Consortium 2018. Debt Cancellation for Somalia: The Road to Peace, Poverty Alleviation and Development for more details).

# 2. Country contexts – Liberia and Somalia

Libera and Somalia show significant parallels in terms of the events that had occurred in their modern histories. Both countries saw the toppling of the civilian governments through a military coup d'état that brought to power autocratic military commanders in chiefs, Sergeant Samuel Doe for Liberia and Major General Siad Barre for Somalia.[4] The Barre and Doe regimes were heavily supported by the United States (US) during the Cold War era.[5] Years of bad policies, weak governance, deteriorating terms of trade and socio-economic conditions brought about widespread dissatisfaction with the Doe and Barre regimes. With the fall of the Soviet Union, the US discontinued support to autocratic regimes in low-income countries such as Liberia and Somalia, diminishing its financial assistance packages to both countries. A combination of global, domestic political and country-specific factors contributed to the downfall of the Doe and Barre regimes, precipitating the ensuing protracted conflict that categorised both countries as "failed states" that were largely neglected by the international community during the 1990s. Throughout the conflict period, both countries continued to fall behind on debt payments to their external creditors.

A combination of strategic, security, economic, political and humanitarian considerations, led the international community to intervene in Liberia and Somalia, with the objective being to bring about peace and stability to both countries. On the security front, peacekeeping troops were deployed to both countries. However, Liberia has had no recurrence of violence since the internationally brokered peace agreement and deployment of peacekeeping troops, while Somalia continues to make efforts to achieve a durable political settlement and suffers from sporadic violent attacks from violent non-state armed actors (VNSAs). On the political front, the emphasis was and continues to be on establishing and strengthening electoral democracy. In the social sector, the international community has provided a substantial amount of humanitarian and development assistance. On the economic front, Liberia and Somalia shared the same experience in that they are high commodity-export dependent countries plagued by chronic underdevelopment and poverty, low and at times negative rates of economic growth, which were further compounded by the protracted conflict. In regard to the public sector, both countries were similar in that they were re-establishing

4 Samuel Doe came to power in April 1980 through the violent removal of the then president, William Tolbert. Mohamed Siad Barre's ascendance to power was quite different, as the 1969 military coup d'état was regarded by many to be "bloodless".

5 On the first anniversary of the military coup d'état of 1969, the Barre administration adopted "scientific socialism" as its political ideology and hence received substantial military and development assistance from the Soviet Union from 1970-77, with Somalia-Soviet Union ties ending after Soviet support to Ethiopia during the Ogaden War. From 1978 onwards, the Barre administration had successfully pivoted to the other Cold War power, the US, as a means of obtaining crucial US loans and grants to support the government's security, political, economic and social objectives.

state institutions from scratch, thus leaving the state to face considerable human and institutional capacity constraints.

At the time the two countries began their engagement in the debt relief process, Liberia and Somalia had, in absolute terms, similar amounts of external debt. However, relative to population, GDP, exports and domestic revenue, Liberia had a heavier external debt burden than Somalia. The considerable difference in debt-to-GDP and debt-to-exports between the two countries can be explained by Liberia's small economy and export earnings relative to Somalia. The table below provides demographic, economic, financial and external debt data at the time of engagement in the debt relief process.

**Table: Demographic, Economic. Financial and External Indebtedness Indicators**

| Indicators | Liberia (End-June 2007) | Somalia (End-2018) |
|---|---|---|
| Total Population (millions) | 3.51 | 14.74 |
| Nominal GDP (US$ millions) | 610 | 4,700 |
| Revenue (three-year backward average, US$ millions) | 78 | 146 |
| Exports of Goods and Services (three-year backward average, US$ millions) | 200 | 1,100 |
| Nominal External Debt Stock (US$ millions) | 4,400 | 4,700 |
| External Debt in Arrears (% of total external debt) | 96[a] | 96 |
| Per Capita Indebtedness (US$) | 1,250 | 320 |
| Debt-to-GDP (%) | 720 | 100 |
| Debt-to-exports (%) | 2200 | 430 |
| Debt-to-revenue (%) | 5,600 | 3,200 |

*Sources:* IMF Country Report No. 08/106; IMF Country Report No. 10/192; IMF Country Report No. 19/256.

Notes:
a. Per cent of external debt in arrears was obtained from Liberia's Decision Point Document (IMF Country Report No.08/106), while all other indicators were obtained from Liberia's Completion Point Document (IMF Country Report No. 10/192).

# 3. Evolution of Liberia and Somalia's external debt and their experience in the debt relief process

This section describes the evolution of Liberia and Somalia's external debt, and how, with the support of the international community, both countries made efforts to normalise relations with their external creditors. They both sought to normalise their relations with external creditors and ultimately to address their external indebtedness by engaging in the HIPC Initiative, a performance-based framework[6] and joint initiative of the IMF, World Bank, regional development banks[7], and other multilateral, bilateral and commercial creditors.

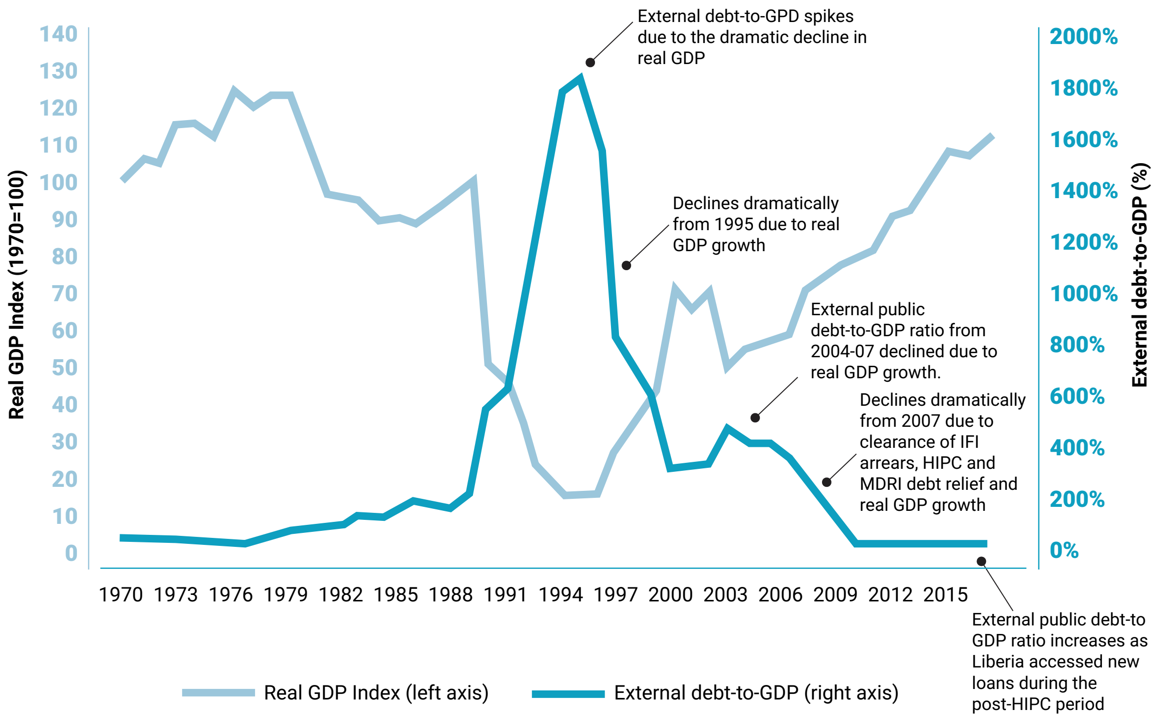
## 3.1. Liberia's external debt, the path to debt relief and post-HIPC outcomes

During much of the 1960s and during the early to mid-1970s, Liberia enjoyed reasonable GDP growth at an annual average of ~4%[8] and steady increases in export earnings thanks to favourable primary commodity prices. Increased government revenues, fed by export earnings, allowed high government spending, which was further boosted by external borrowing for public investment projects throughout that period.[9] However, during the late 1970s and much of the 1980s[10] commodity prices fell sharply, reducing the growth of GDP and exports. In response, the Liberian government opted to stimulate the economy through large-scale public investments that, in the end, proved to be unproductive.[11] Due to increased borrowings, Liberia's external debt started to increase significantly, with its debt-to-GDP ratio rising from ~43% in 1977 to ~184% in 1986 (see Figure 1). By the mid-1980s, during the Doe administration, Liberia started falling behind on its external debt payments when it got into arrears with the IMF in December 1984 and with the World Bank in 1985.[12] By the end of the Doe regime in 1989, Liberia's public debt-to-GDP ratio reached ~240% and increased to ¬540% in 1990 as a result of real GDP declining to 49% of its 1970 and 1989 level.

Throughout the Doe administration until the end of the first Sirleaf administration, Liberia

6 The HIPC Initiative is premised around the implementation of reforms that seek to improve macroeconomic, structural and social policies and programs with a view to spurring economic growth and development and alleviating poverty.
7 Regional development banks refer to the: Asian Development Bank, African Development Bank, European Bank for Reconstruction and Development and Inter-American Development Bank.
8 From 1960-74 as per the World Bank 2019 database.
9 It should be noted that Liberia experienced a foreign investment boom between 1959 and 1963. As a result, the Liberian government borrowed heavily to finance its public investment programme throughout much of the 1960s in anticipation of future revenue flows derived from the exploitation of iron ore resources. Unfortunately, these future revenue flows did not materialize, leaving the government to face a debt servicing problem that had been resolved through a rescheduling agreement on debts falling due between 1963-68 with its external creditors facilitated by the IMF. For more detail, see Dalton (1965), Maynard (1970) and Honda and Schumacher (2006).
10 As can be seen in Figure 1, Liberia experienced slow growth in the 1970s and negative growth during the 1980s.
11 See IMF Staff Country Report No. 00/50.
12 On World Bank arrears, though Liberia began to fall behind on its debt service payments in 1985, the World Bank suspended its disbursements to Liberia in December 1986 and placed Liberia in non-accrual status (i.e., fails to repay arrears for more than six months) in June 1987. For more details, see IMF Country Report No. 04/84 and Gifford (1993, pp. 34).

**Figure 1: Liberia Debt-to-GDP Ratio and Real GDP Growth (1970-2017)**




*Sources:* Author's own elaboration based on data from Penn World Table 9.1 and the World Bank 2019 Database. Data on real GDP are from Penn World Table 9.1. Data on external debt-to-GDP are from the World Bank 2019 Database (Washington, D.C.: 2019).

did not service its external debt. With interest in arrears and the accompanying penalty interest charges, Liberia's external debt kept increasing. The external debt-to-GDP ratio peaked at around 1800 per cent in 1995 (see Figure 1) mostly due to the dramatic decline in real GDP[13] (real GDP declines to about ~14% of its 1970 level as seen in Figure 1) brought on by the wide-scale destruction that occurred during the First Liberian Civil War[14] (IMF, 2004). Since the downfall of the Doe regime in 1989, the growth of Liberia's external debt stock was due to the accumulation of external debt arrears (i.e., non-payment of interest and late/penalty interest) not by new borrowing for public investment. Following the end of the conflict in 2003, Liberia recorded four years of economic growth (2004-07) before qualifying for the HIPC Initiative in early 2008. Steady GDP growth, initial debt relief under HIPC, and a commercial debt buy-back made possible by HIPC led to a sharp decline in the debt-to-GDP ratio during 2008-10 (Figure 1).[15]

The signing of the peace agreement, the establishment of the National Transitional Government of Liberia (NTGL) and the deployment of peacekeeping troops in 2003 brought about an enabling environment that allowed Liberia to re-engage with key development partners and international financial institutions (IFIs). While the immediate priorities of the NTGL after the end of the Second Liberian Civil War was to tackle the country's urgent humanitarian and reconstruction needs, there were initial

13 According to IMF Country Report No. 00/50, real GDP declined to about 10 per cent of the pre-war level, which is very close to the decline in the real GDP index shown in Figure 1 (~14 per cent decline of the 1970 level).
14 Liberia was plagued by two civil wars in its recent history. The First Liberian Civil war lasted from 1989-97, while the Second Liberian Civil War lasted from 2000-03.
15 The debt relief operations that occurred during this span of time (2008-10) include: (i) the clearance of arrears owed to the international financial institutions (IFIs) in late 2007 (World Bank and AfDB) and early 2008 (IMF); (ii) the execution of a commercial debt buyback operation in April 2009 that accounted for~97% of commercial debt holders and the completion of a similar operation to buyback the remaining debts from the last two commercial creditors in November 2010, with both operations being financed through the World Bank's Debt Reduction Facility; and (iii) the granting of HIPC, MDRI and MDRI-like debt relief in July 2010 and beyond-HIPC debt relief (mainly by the Paris Club)

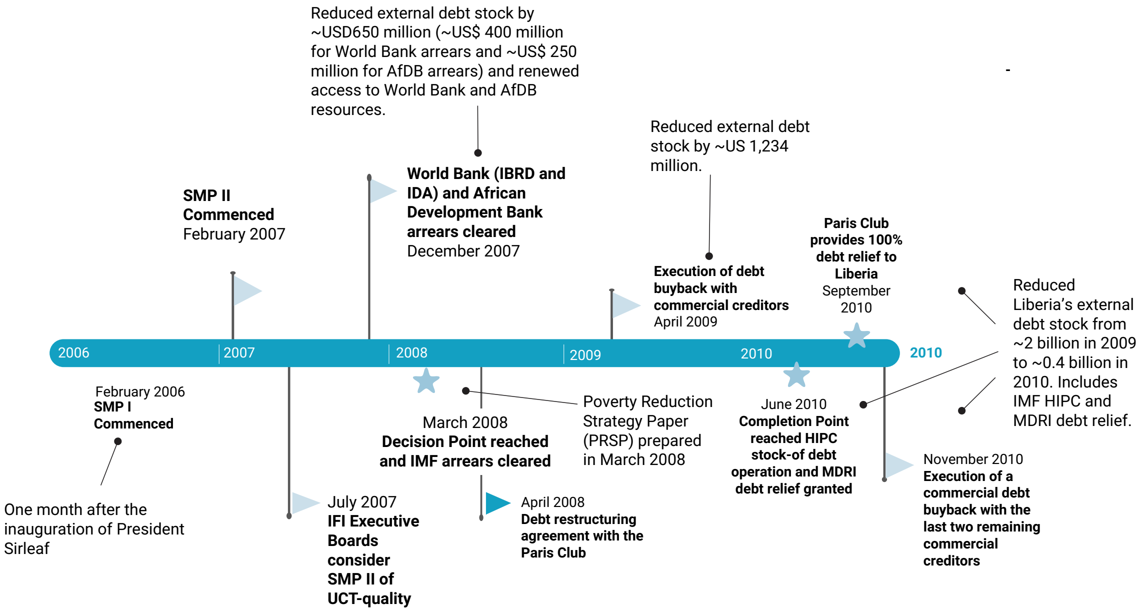
discussions between the government and IFIs, namely the IMF, on how Liberia could resolve its external indebtedness.[16] Discussions around the prospects of Liberia securing debt relief failed to gain traction in creditor circles, as there was no credible commitment by the NTGL toward economic governance reform because of the high level of corruption in the public sector and the NTGL's mismanagement of resources.[17]

It was only under the leadership of Ellen Johnson Sirleaf, elected in November 2005 that Liberia was able to make headway in its bid for debt relief. Liberia was able to qualify for the HIPC Initiative within 26 months since it began its first SMP and graduated from the Initiative and received Multilateral Debt Relief Initiative (MDRI) debt relief after just over two years since qualifying. Based on the framework of the HIPC Initiative, Liberia obtained relief of 97% of its commercial debt, 94% of its external bilateral debt[18], and 90% of its multilateral debt once it reached its Completion Point in June of 2010. Figure 2 depicts key milestones in Liberia's debt relief process.

Liberia's experience with the debt relief process has earned the country the reputation of being a trailblazer of the HIPC debt relief process for other conflict-affected countries with sizeable and protracted arrears, making it a good comparator for Somalia (see Box 1 for a brief overview).

The normalisation of relations with external creditors in March of 2008 and the provision of debt relief in mid-2010 has had a relatively positive effect on the Liberian economy as there was a steady inflow of foreign direct investment (FDI) and increasing domestic revenues (Figure 3).[19] It is quite evident that Liberia's experience with the debt relief process had allowed the government to showcase their reform commitment, thereby allowing them to secure the stamp of approval of the IFIs that has led to renewed access

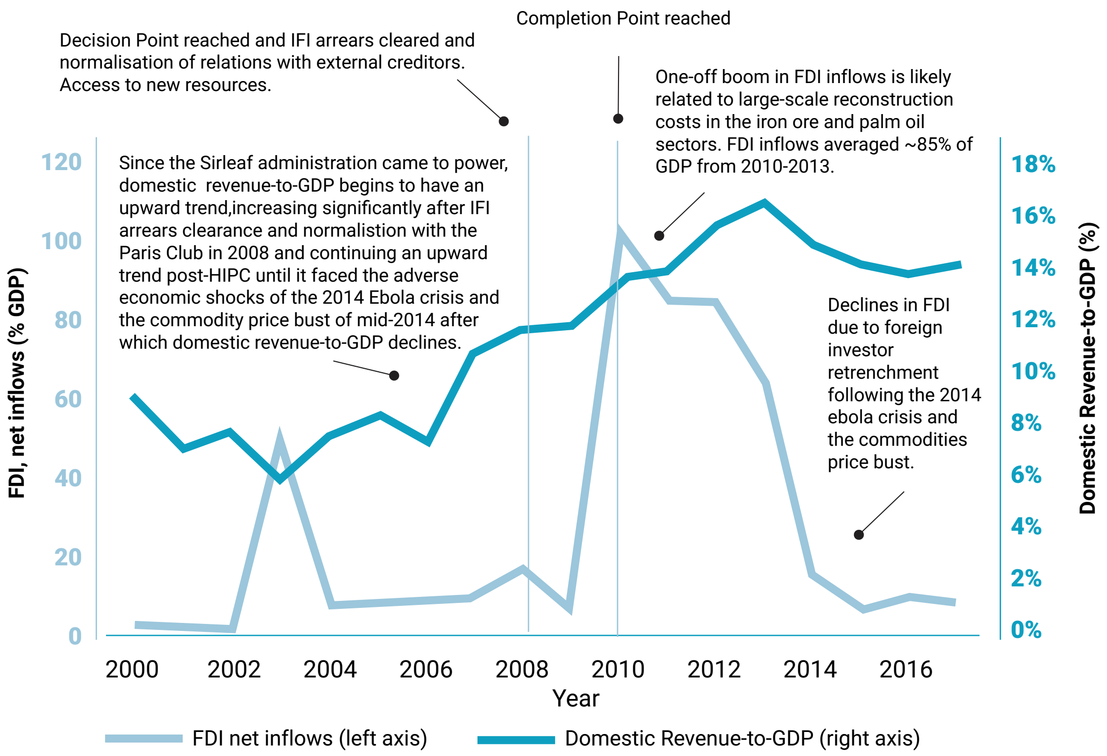
## Figure 2: Liberia's Debt Relief Process Timeline




*Source:* Author's own elaboration.

16 See IMF Country Report No. 04/84.
17 Under the NTGL, after a series of corruption scandals and gross mismanagement by the authorities, including the misappropriation of development aid, Liberia's development partners negotiated with the NTGL an economic and financial governance program – the Governance and Economic Management System (GEMAP) - that posted non-national consultants with co-signatory powers in key government ministries and state-owned enterprises – a move that some Liberians viewed as highly invasive of Liberia's sovereignty. For more information on the GEMAP programme, see Alao (2010).
18 Paris Club creditors cancelled 100% of their claims on Liberia.
19 The increase in government revenue was mainly driven by increasing extractive sector rents. 6 See IMF Country Report No. 04/84.

**Figure 3: Liberia: FDI Inflows and Domestic Revenue-to-GDP (2000-17)**




*Sources:* Author's own elaboration based on data from World Bank 2019 Database (Washington, D.C.: 2019) and IMF, World Economic Outlook, April 2019. Data on FDI net inflows (as % GDP) are from World Bank 2019 Data on domestic revenue are from IMF Staff Reports.

to concessional resources. In addition, the provision of debt relief in 2010 likely signalled to foreign investors that Liberia was "open for business" and facilitated a massive inflow of FDI between 2010-13 related to large rehabilitation investments in the iron ore and palm oil sectors.[20] FDI inflows significantly diminished thereafter due to the retrenchment of foreign investors following the Ebola crisis of 2014 and the commodity price bust that had occurred after mid-2014. On balance, renewed access to concessional resources and steady inflows of FDI and the accompanying increase in domestic revenues has put Liberia in a better footing to transition from post-conflict reconstruction to inclusive economic growth, development and poverty alleviation.

While Liberia's economic situation is on a better footing since receiving debt relief in 2010, the country continues to struggle to translate higher government revenues (driven mainly by economic rents obtained from its extractive industries) and new concessional and grant financing (made possible by HIPC) to broad-based and inclusive economic growth, development and poverty alleviation. This struggle has been further exacerbated by the recent adverse economic shocks of the Ebola crisis and the commodity price bust of mid-2014. These adverse economic shocks had exposed the government's over reliance on rents from extractive industries, with Liberia's domestic revenue declining rapidly resulting in higher fiscal deficits. The shrinking revenue envelope, growing fiscal deficits (financed out of Liberia's international reserves) and accumulating debt[21] has put great pressures on Liberia's future repayment capacity, with the IMF and World Bank classifying the country as being

20 FDI inflows spiked to ~103 per cent of GDP in 2010 and averaged ~85 per cent of GDP from 2010-2013 (see Figure 3)
21 External debt in Liberia has increased since 2010 due to new borrowings related to infrastructure projects and the government's fiscal response to economic shocks (see IMF Report No. 18/172).

in moderate risk of debt distress[22] less than a decade after receiving debt relief. The sizeable accumulation of new debt is made even more concerning given inefficiencies in public investment, owing to Liberia's poor public investment management framework[23], possibly further weakening the government's debt repayment capacity and hindering the country's long-term growth and development prospects. In addition, the Liberian government has in recent years contracted new non-concessional loans further straining the country's weakened capacity to meet debt obligations.

**Box 1: Liberia – Debt Relief Trailblazer for Conflict-Affected Countries with Sizeable and Protracted Arrears to External Creditors**

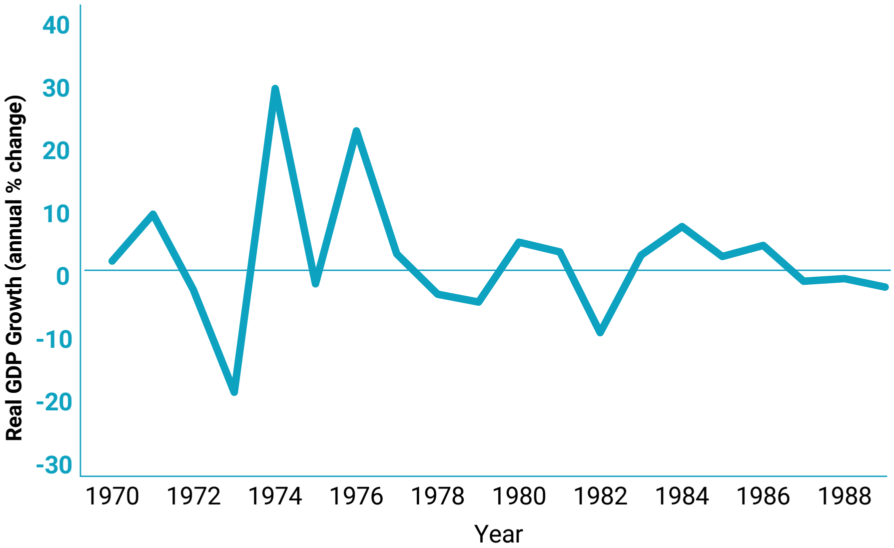
Liberia's engagement in the debt relief process presented unique challenges to the IFIs (the administrators of the HIPC Initiative), as it was the first conflict-affected country with protracted arrears to the IFIs that lacked HIPC and MDRI Trust Fund resources to support debt relief operations, including the clearance of IFI arrears. Prior to Liberia, the vast majority of countries that had graduated or were engaged in the HIPC Initiative were peacetime countries where state institutions were intact for relatively long periods of time. Liberia, Somalia and Sudan[24], being the last three countries requiring large-scale IFI arrears clearance operations and not being engaged in the HIPC Initiative at the time, were left out of the original financing framework of the HIPC and Multilateral Debt Relief Initiatives.[25] This essentially meant that resources were not earmarked for debt relief operations, including the clearance of IFI arrears. Thus, the resolution of Liberia's protracted IFI arrears problem required IFIs along with the country's external creditors to apply innovative solutions that addressed this particularly unique context. Notable precedents set in Liberia's debt relief process include:

- **Precedent:** World Bank mobilizes financial resources during the IDA15 replenishment to clear arrears for Liberia and to cater for a similar arrear's clearance operations for other prospective countries with protracted arrears to the World Bank.
- **Precedent:** IMF arrears clearance operation and Decision Point occurred almost in unison.
- **Precedent:** IMF and World Bank Executive Boards utilised their discretion in determining that Liberia's SMP II satisfied the upper credit tranche (UCT) conditionality required to reach Decision Point. The decision by the Board was the first instance in which an SMP was qualified as meeting the conditionality standards of a UCT program arrangement.
- **Precedent:** The debt relief financing package required for the IMF's participation in Liberia's debt relief process, covering both HIPC Initiative and MDRI-like relief, were mobilised by contributions from 102 IMF member countries.
- **Precedent:** The IMF Executive Board approved an 'MDRI-like' debt relief operation to extinguish the remaining post-HIPC debts of Liberia once the country reached its Completion Point. This precedent was established to allow Liberia to receive MDRI-like or beyond-HIPC relief as the country was ineligible for MDRI given that the 2008 arrears clearance operation put Liberia's IMF debts well past the IMF's MDRI cut-off date of end-2004.

For the remaining conflict-affected countries with sizeable and protracted IFI arrears (Somalia and Sudan), there is a growing consensus amongst both IFIs and the Paris Club that precedents set in Liberia's debt relief experience could serve as a model to follow.

22 See latest IMF-WB Debt Sustainability Analysis (IMF Country Report No. 19/169).
23 See IMF Country Report No. 16/352.
24 While Eritrea, like Somalia and Sudan, is a HIPC-eligible country, it was not included in this discussion as its IFI arrears situation isn't clear. There is no publicly available information that indicates whether Eritrea owes sizeable and protracted arrears to the IFIs.
25 See IMF. Update on the Financing of the Fund's Concessional Assistance and Debt Relief to Low-Income Member Countries. September 16, 2008. Available at: https://www.imf.org/external/np/pp/eng/2008/091608.pdf

**Figure 4: Somalia: Real GDP Growth (1970-89)**




*Source:* World Bank 2019 Database (Washington, D.C.: 2019)

## 3.2. Evolution of Somalia's external debt and its march toward debt relief

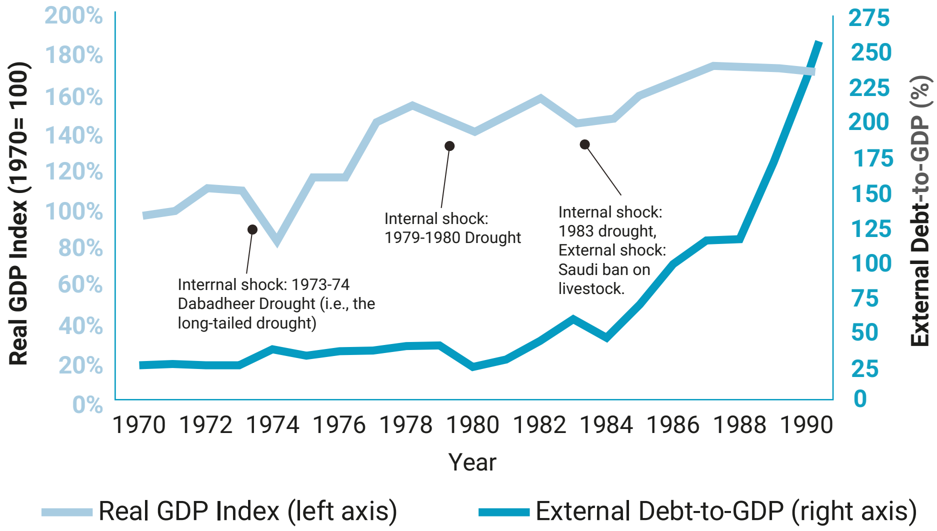
The evolution of Somalia's external debt has followed a similar trajectory to the Liberian one. During the 1970s and the 1980s, the Barre regime borrowed significantly to finance its Public Investment Program (PIP), a series of planned public investment projects that sought to spur economic growth.[26] The vast majority of the PIP investment projects were managed inefficiently, proving to be unproductive and having little effect on Somalia's economic growth.[27] As a result, high and stable rates of economic growth remained elusive from the 1970s to the 1980s (see Figure 4).

Throughout this period, economic conditions in the country, including the external debt situation, continued to deteriorate. The government continued to finance new investment projects and provided funding for the operations of previous projects, causing the government to resort to foreign borrowing. Furthermore, the imports of capital goods (i.e., equipment, machinery, vehicles etc.), inputs and fuel required for the execution of the PIP investment projects rose more swiftly than exports (namely live animal exports), worsening Somalia's trade balance. As the projects did not generate many exports or import substitutes, over time the debt service caused balance of payments deficits which were financed by resorting to balance of payment support loans, thus increasing Somalia's external debt. In addition to unproductive projects, Somalia's external borrowing was also used for military expenditures.

With the deteriorating macroeconomic environment, Somalia faced difficulties in meeting its external debt obligations. In the mid-1980s, the government concluded two rescheduling agreements with the Paris Club. Moreover, external debt payment difficulties were evident when the country fell into arrears with the IMF in July 1987 (Oeking and Sumlinksi, 2016). With the government engaging in inflationary finance (averaging ~4% of GDP from 1984-1989), the ensuing high inflation (over 60

26 Many of these investment projects were implemented by state-owned enterprises (see Mubarak, 1996, pp.95).
27 See Mubarak (1996, pp. 95-114) for more detail on the PIP and its (non)-effect on Somalia's economic growth.

**Figure 5: Somalia's Debt-to-GDP Ratio and Real GDP Growth (1970-90)**



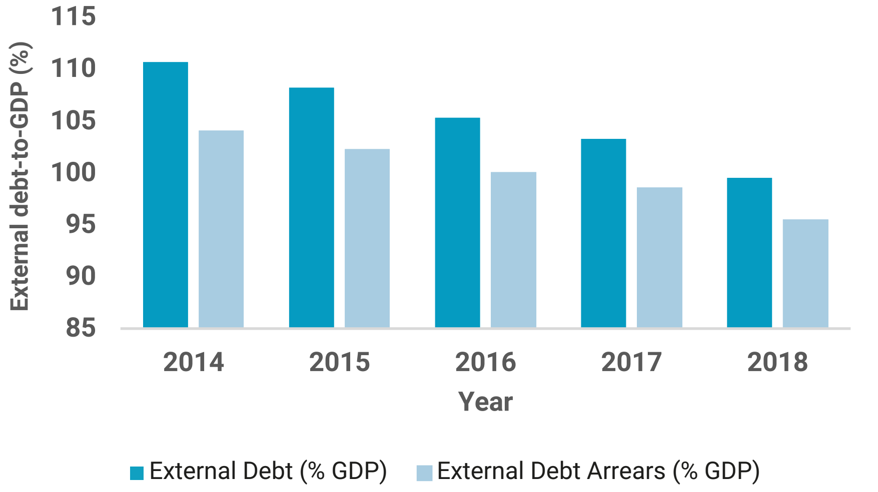

*Sources:* Data on external debt-to-GDP data are from World Bank, World Tables, 1995. Data on real GDP are from World Bank 2019 Database (Washington, D.C.: 2019).

per cent from 1980-90[28]) led to currency depreciation and a further deterioration in the macroeconomic environment and socio-economic conditions.[29] This, in turn, contributed to the socio-political unrest that led to the large-scale violent conflict that broke out in the late 1980s and early 1990s. Somalia's public debt-to-GDP ratio increased from ~47% in 1984 to ~260% in 1990, just before the collapse of the state in January 1991. Figure 5 provides a depiction of the evolution of Somalia's external debt-to-GDP and real GDP (as an index, with 1970=100) from 1970-90.It is important to note that it was difficult to provide a comprehensive picture of external debt-to-GDP and real GDP from 1970-2018 given a lack of available data during the conflict and transitional years 1991-2013.

Without a functioning government in place and without resources, Somalia fell into arrears with all its external creditors and fell into non-accrual status with the World Bank in 1991.[30] Since 1991, Somalia's external debt steadily accumulated due to non-payment of interest due and penalty interest charges, much like in Liberia, growing from 62% of GDP in 1983 to 260% of GDP in 1991 and reaching US$ 4.7 billion (~100% of GDP) by 2018 (see Figure 6).

28 See http://somalia.opendataforafrica.org/lhqzaxg/somalia-inflation-and-emlpoyment. Accessed on 10 August 2019.
29 High levels of inflation in 1980 were caused by supply-side induced inflation caused by the 1979-80 drought and increased domestic prices of imported inputs due to the parallel market exchange rate being more than double the official exchange rate. Inflation declined in mid-1981 due to a devaluation in the Somali Shilling. In 1983, inflation began to rise sharply due to supply-side shocks such as adverse weather conditions and a shortage of foreign exchange due to Saudi Arabia's ban on Somali livestock (Mubarak, 1996, pp. 26; Zulu and Nsouli, 1985, pp. 17). High Inflation rate continued to plague Somalia from 1984-90 and was made worse towards the latter half of the 1980s as the Somalia Commercial and Saving Bank, a publicly-owned financial institution providing commercial and retail banking services, expanded the money supply through irresponsible credit expansion and supply of circular cheques, i.e., quasi-money (Carrier and Lochery, 2013, pp. 347).
30 Somalia was in non-accrual status with the World Bank since 1991 (see World Bank Report No. 124734-SO).

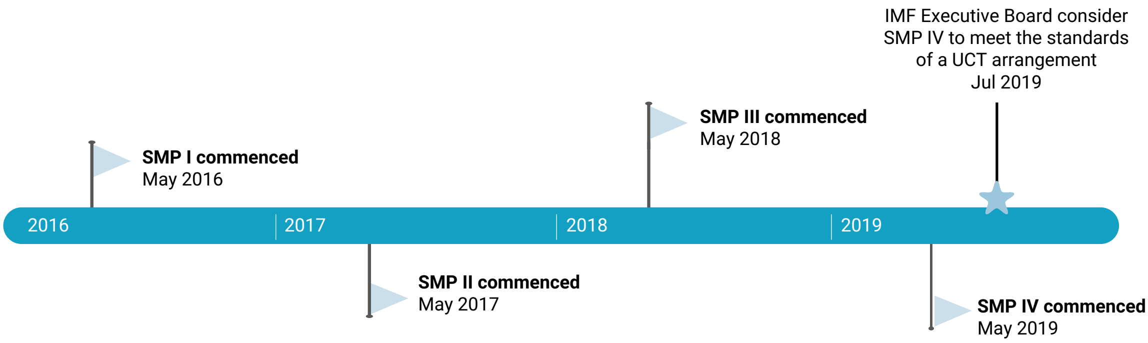
## Figure 6: Somalia's External Debt and External Debt Arrears (2014-18)




*Source:* Data on external debt and external debt arrears data obtained from the IMF Somalia Mission Team.

Somalia's move in the HIPC Initiative has been a slow-moving process. Starting in May 2016—nearly four years after the new FGS was instituted in 2012 and three years after the London Somalia Conference 2013 which galvanized international support for Somalia, it has been implementing a series of IMF SMPs (SMP I-IV) without yet qualifying for the HIPC Initiative, i.e., reaching Decision Point (Figure 7). However, in the latest IMF staff report issued in August 2019, the IMF staff were of the view that the policies contained in Somalia's new SMP (SMP IV) meets upper credit tranche (UCT) conditionality standards[31], with the Fund's Executive Board agreeing with the staff's appraisal.[32] The IMF's classification of SMP IV as meeting the conditionality standards of an UCT arrangement takes Somalia a step closer to qualifying for the HIPC Initiative.

## Figure 7: Somalia's Debt Relief Process Timeline




*Source:* Author's own elaboration.

31 An IMF supported program of UCT quality are the Extended Credit Facility (ECF) and the Standby Credit Facility (SCF). In addition, on a case-by-case and exceptional basis, the IMF's Executive Board has the discretion to qualify a country for the HIPC Initiative in programs other than the ECF and SCF. These programs include the Rapid Financing Instrument, Rapid Credit Facility, Rights Accumulation Program and the SMP (IMF, 2017).
32 See IMF Country Report No. 19/256.

Although the country has moved closer to qualifying for the HIPC Initiative, Somalia still requires international efforts to coordinate the requisite technical and financial assistance needed to overcome obstacles to its debt relief process. These obstacles include the need to: (i) mobilize adequate and competent human resources required for the implementation of a UCT-quality SMP; (ii) raise resources required for the debt relief operations of IFIs; and (iii) secure commitments or financing assurances for the participation of most of its external bilateral and multilateral creditors in the debt relief process[33]. The annex provides details about the financial resource needs required for IFI arrears clearance and the participation of IFIs in the debt relief process, i.e., the HIPC Initiative and MDRI.

When looking at Somalia's economic conditions since its re-engagement with the international community, it can be observed that the country has seen steady improvement in its macroeconomic and fiscal situation.  Since 2012, the country has seen low-to-moderate economic real GDP growth rates, averaging ~2% between 2012-17[34]. Total domestic tax revenue has increased from US$ 70 million in 2013 to US$ 183 million in 2018, with the IMF projecting it to reach approximately US$ 196 million by the end of this year. In recent years, the country has experienced very low levels of inflation, averaging ~2% from 2013-18[35], with inflation peaking at 6.1 per cent[36] in 2017 due to the drought. While Somalia's macroeconomic environment is steadily improving, at this point in time, it is premature to make an assessment on Somalia's economic performance, as the country has not received debt relief and the corresponding increase in net resource transfer post-HIPC seen in the case of Liberia. However, Section 5 does provide lessons learned from Liberia's experience during the post-HIPC decade (2010-19) that if applied in Somalia in a forward-looking manner will put the country in a good position to avoid many of the potential pitfalls.[37]

33 Under framework of the HIPC Initiative, Somalia needs to secure financing assurances amounting to at least 70% of HIPC-eligible debts from its external creditors to qualify for the HIPC Initiative.
34 IMF, World Economic Outlook, April 2019.
35 Ibid.
36 IMF Country Report No. 19/256.
37 The pitfalls experienced by Liberia during its post-debt relief period are discussed in the latter part of Section 3.1.

# 4. Key success factors for an expedited debt relief process and country performances

Liberia's success in having an expedited debt relief process and securing deep debt relief, suggests several key success factors that have facilitated the country's swift progression through the debt relief process. These key success factors—at the country and international levels--seem relevant in other FCAS countries and are discussed below for both Liberia and Somalia. In addition to what appear to be general success factors,[38] there are country- or context-specific success factors , applicable in Liberia's engagement in the debt relief process that may not apply to Somalia and vice-versa.

## 4.1. Country level

Low-income HIPCs emerging from conflict with sizeable external payment arrears feel a particular sense of urgency and have an economic incentive in wanting to achieve two goals in the least costly manner and within the shortest possible time horizon. First, normalise its financial relations with external creditors (i.e., the resolution of external debt arrears) to regain access to new grant and concessional resources needed to kick-start reconstruction. Second, secure the maximum amount of debt relief as fast as possible to bring external debt to a sustainable level, relative to the country's payment capacity and reconstruction needs.

A country's normalization of financial relations with its external creditors and qualification for the HIPC Decision Point is premised on whether a country is able to meet HIPC requirements (e.g., capacity for implementing sound economic policies and having the requisite debt management capacity), with normalisation of relations with IFIs serving to signal to other creditors that the country has qualified for debt relief. Yet there are other factors that play a role in determining the speed of the HIPC process, as the Liberian experience has shown. Three factors are of particular relevance to Somalia: progress towards a durable cessation of violence and resulting socio-political stability; human and institutional capacity; and political leadership. The following sections describe how these factors have worked in Liberia and Somalia.

### 4.1.1. Progress towards a durable cessation of violence and socio-political stability

Progress towards a durable cessation of violence and socio-political stability is a key success factor for an expedited debt relief process, as a country that is able to avoid crises and demonstrate good efforts to bring about peace would facilitate its bid for debt relief. Oeking and Sumlinski (2016) also make the same assertion when it comes to a country vying to resolve its protracted arrears situation, with the authors stating: "… once the country finds itself accumulating arrears it should recognize the importance

38 Owing to the different historical, economic, political, geographic, social and temporal contexts between the two country cases.

of a peaceful political environment to their clearance. The better it can protect itself from fragility the shorter its predicted time laboring towards arrears clearance." The same holds true for a country vying to secure debt relief.

When the new Sirleaf administration came to power in Liberia in 2006, the cessation of violence and socio-political stability had been met. In 2003, the international community brokered a political settlement (the Accra Comprehensive Peace Agreement), which brought about: (i) the removal of the then-president, Charles Taylor[39], from office; (ii) the inclusion of rebel factions, opposition parties and other civil society into the Government; and (iii) the cessation of hostilities between rival Liberian actors. Shortly after the signing of the peace agreement, the United Nations (UN) Security Council established a UN peacekeeping operation in the country – the UN Mission in Liberia (UNMIL) - to ensure compliance with the peace agreement. The Accra Comprehensive Peace Agreement and UN peacekeeping troops created the enabling environment in which Liberia conducted its first truly free and fair parliamentary and presidential elections in November 2005, leading to the election of Ellen Johnson Sirleaf, Africa's first female president. The two terms of the Sirleaf administration brought greater peace and stability to Liberia.

Turning to Somalia's peace and security situation, the security environment has been gradually improving in recent years. Between 2000-12, the country was mired in political instability and conflict between transitional governments and VNSAs. In early 2007, the increasing threat posed by VNSAs led the African Union (AU) and the UN to establish an African peacekeeping force in the country– the African Union Mission in Somalia (AMISOM).[40] In contrast to UNMIL, AMISOM, alongside the Somali National Army, has had to combat VNSAs – often focused on destabilizing the Somali government. Joint operations by AMISOM and the Somali National Army over the years since 2007, has liberated numerous towns in south-central Somalia, forcing VNSAs to retreat to rural areas.[41]

In the political context, due to the security situation prevalent in the country, Somalia was unable to conduct free and fair elections based on universal suffrage (as in the case of Liberia). However, the country has in 2017, successfully made its electoral process more inclusive and democratic compared to the 2012 electoral process.[42] For instance, the profile of Somalia's federal parliament has broadened from one dominated by senior men to include greater women and youth representation. Women representation in the Lower House of the Federal Parliament increased from ~14 per cent in 2012 to 24 per cent in 2017.[43] Moreover, Somalia's parliament has gotten much younger, with 60 per cent of members of the Lower House and 50 per cent of members of the Upper House being between the ages of 25-50.[44] The greater degree of legitimacy in the 2017 parliamentary and presidential elections has contributed to improving political stability at the national level. Additionally, Somalia has moved to a new federal governance system, with the country now having five Federal Member States (FMS).[45] The country's new federal dispensation has the

39 Charles Taylor was the warlord-turned-president who ruled Liberia as its president from 1997-2003 after which he was exiled to Nigeria.
40 The AU's Peace and Security Commission approved the deployment of 8,000 AU peacekeeping troops on 19 January 2007. On 20 February 2007, the UN Security Council endorsed the establishment and deployment of peacekeeping troops to Somalia in UN Security Council Resolution 1744 (Williams, 2018).
41 For more information on AMISOM and SNA operations in Somalia see Williams (2018).
42 In 2017, 275 electoral colleges (each comprised of 51 clan elders, 14,025 in total) elected 275 lower house federal parliamentarians compared to the 135 traditional elders that selected the parliamentarians in 2012.
43 See Abdi Latif Dahir, "The fate of fragile Somalia is now in the hands of a remarkably young, diverse, parliament," Quartz Africa, March 2, 2017. Available at: https://qz.com/africa/922449/the-fate-of-fragile-somalia-is-now-in-the-hands-of-a-remarkably-young-diverse-parliament/. Accessed on 17 July 2019.
44 Ibid.
45 Somalia's five Federal Member States are Puntland, Jubaland, Southwest, HirShabelle and Galmudug.

potential to contribute to improving political stability, governance and public service delivery. Currently, the Federal Government of Somalia (FGS) and FMS are working on putting in place a suitable federal governance system for the country, although significant challenges remain in operationalising federalism in Somalia.

To summarize, Somalia is making progress in ending the violence and in establishing a stable and durable political settlement – albeit not comparable to the peace and political stability enjoyed by Liberia during the Sirleaf era. While that may be the case, experience with FCAS countries (e.g., Afghanistan) highlight that while the cessation of violence and socio-political stability is the ultimate outcome desired from debtor country publics and the international community, the non-attainment of this goal during a country's engagement in the debt relief process is not a barrier. Rather it is a complete lack of progress to bring about durable peace and socio-political stability that stymies a country's progression through the debt relief process. In this respect, Somalia's continual improvement in its security and political situation is a critical impetus for debt relief, so as to access new external funding for the reconstruction of the country, which will likely further consolidate peace, poverty alleviation and development.[46]

### 4.1.2. Human and institutional capacity

Having the requisite human resource and institutional capacity is without question the most fundamental critical success factor, as the granting of debt relief is premised on a country's ability to implement sound policies and improve its economic governance. As such, the implementation of the conditionality requirements of the debt relief process requires effective institutions staffed with competent staff and having sound institutional arrangements and processes required for good economic policymaking and implementation.

Since the start of the HIPC Initiative, multilateral and bilateral (in particular Paris Club) creditors have placed emphasis on the adoption of economically sound policies (e.g., macroeconomic stability, transparent fiscal policies, poverty reduction strategies) and improvements in economic governance and quality of institutions when deciding on granting debt relief to a HIPC country. The importance placed on these considerations represents a major policy shift in the granting of debt relief from the previous traditional considerations that put more emphasis on political, strategic, military and commercial ties with debtor countries. This shift in the debt relief decision-making process was in response to a growing consensus in IFIs, policymaking and academic circles on the critical importance that sound policies and good and effective institutions play in economic development. Within this context, HIPC-eligible countries wanting to engage in the debt relief process in a serious and meaningful manner must be willing to exert extensive and intensive efforts to improve economic governance, strengthen its human and institutional capacity and formulate and implement sound policies.

While there may be a willingness on the part of the country to undertake reform measures to improve economic governance and policymaking, authorities in low-income HIPC countries often struggle to establish sound governance structures, efficient and effective bureaucracies and have issues in attracting and retaining skilled individuals in the public sector. In the case of Liberia and Somalia, these challenges are even made more acute due to the legacy of conflict that has left the countries bereft of much human and institutional capacity, as years of conflict result in the destruction of state institutions and the loss of highly skilled bureaucrats and technocrats. Also, protracted absence

46 See Somalia NGO Consortium 2018. *Debt Cancellation for Somalia: The Road to Peace, Poverty Alleviation and Development.*

of an effective and functioning government significantly reduce investment in human capital, hindering the development of a skilled workforce.

Cognisant of the capacity challenges facing FCAS countries like Liberia and Somalia, IFIs provide technical assistance and capacity-building support to strengthen the organizational, policymaking and human capacities of state institutions. The IMF, particularly, through its Staff-Monitored Programs (SMPs), supports fiscal, monetary, statistical and economic planning institutions to strengthen the institutional, organizational, policy-making and human capacities to prepare a country to implement a more rigorous IMF-supported program of UCT-quality required for debt relief. The implementation of such a rigorous program serves as a signal, informing external creditors, stakeholders and potential investors on progress made in improving governance and institutional quality and policymaking. For countries like Liberia and Somalia, the implementation of an IMF-supported program would serve to showcase the country's reformist credentials. In addition to IMF support, its sister institution, the World Bank, also provides support to help strengthen state capacity in FCAS countries by providing technical assistance and capacity-building support in a number of public financial management (PFM) areas that include: public expenditure management, revenue collection and management (including natural resource management), civil service reform and decentralization.[47] Unlike the IMF that only provides technical assistance and capacity-building support to the central governments of its member countries, the World Bank is able to provide similar support to subnational administrations.[48] Like the Bretton Woods Institutions[49], the African Development Bank's (AfDB) also supports capacity-building, policy and institutional support projects around PFM and economic governance issues that are tailored to country circumstances and needs.[50]

At the beginning of Liberia's post-conflict period, it was quite evident that the country was suffering from a severe human resource problem, with one official remarking: "the capable were not available, so the available became the capable" (Blum *et al.*, 2019). To address its human resource deficiencies, the Liberian government recruited from its diaspora, with a number of programmes being set up after the election of Ellen Johnson Sirleaf. These include the donor-funded Senior Executive Service Program, the Transfer of Knowledge Through Expatriate Nationals programme and the Liberian Emergency Capacity Building Support programme, all of which provided salary top-ups to increase the appeal for the diaspora to return to Liberia, amongst other incentives. In addition to tapping into the talents of the Liberian diaspora, the Sirleaf administration also extensively engaged non-national consultants and advisors through donor-funded programs. The infusion of skills and expertise from qualified nationals, diaspora returnees and

47 See Independent Evaluation Group (IEG) (2014).

48 In the case of Somalia, in addition to the FGS, the World Bank provided technical assistance and capacity-building support in a number of areas to Somaliland, Puntland and the Benadir Regional Administration, and as part of its new Country Partnership Framework, intends to expand to other FMS between 2019-22 (see World Bank Report No. 124734-SO). Although Liberia is a unitary state, the World Bank had been leading on decentralization-related reforms (IMF Country Report No. 07/356).

49 The IMF and World Bank are at times collectively referred to as the Bretton Woods Institutions, owing to the fact that both of these sister institutions were established at the Bretton Woods Conference (more formally referred to as the United Nations Monetary and Financial Crisis) held in Bretton Woods, New Hampshire during World War II from 1-22 July 1944.

50 It is important to note in supporting technical assistance and capacity-building interventions targeting countries with protracted arrears, both the IMF and World Bank do not utilize institutional resources and instead rely on donor trust funds. On an exceptional basis, the World Bank does allow HIPC countries in non-accrual status that are re-emerging from conflict and are close to reaching Decision Point to access IDA funds through pre-arrears clearance grants (see IDA's Further Elaboration of a Systematic Approach to Arrears Clearance, June 2007, IDA15). Similarly, the AfDB also provides support through a donor trust fund, namely the Transitional Support Facility (TSF) and also allows access to fifty (50) per cent of a country's ADF performance-based allocation (see African Development Bank Somalia Country Brief 2017-2019).

expatriates helped to reinforce the national vision of putting in place a reform-minded and developmental administration. It also helped in quickly and smoothly rolling out reforms that would put in PFM systems, policies and IFI conditionalities required for the HIPC Initiative, including the development of a poverty reduction strategy paper (PRSP).

Liberia not only needed an injection of human capital to make progress on its reform agenda but also had to rebuild its institutional and policymaking capacity to implement an IMF-supported program. Development partners and IFIs came in to provide support in this area through donor programs, including the IMF SMP. Efforts to strengthen Liberian institutions, human resources and policymaking capacity was critical in supporting the implementation of a rigorous six-month SMP program[51] in mid-2007 that allowed Liberia to finally qualify for debt relief in March 2008.

For Somalia, at the start of the country's re-engagement process in 2013, the human capacity challenges facing the country were as big as those of Liberia in 2006. The poor quality and quantity of human resources in the civil service was apparent in the fact that many of the FGS's ministries, departments and agencies were understaffed and that the government struggled to identify its staffing needs and competitively recruit and retain quality staff.[52] Much like Liberia's response to human resource constraints, Somalia mobilized skills and expertise from qualified Somalis within the country, diaspora returnees and non-national consultants and advisors through donor-funded programs. On the institutional strengthening front, like Liberia, Somalia has benefited from several donor-funded programs, aiming to strengthen state institutions[53], with the country benefiting from more than 115 technical assistance and training missions[54] from the IMF in its areas of expertise[55] during 2013-2019. Of late, the IMF and the World Bank have jointly planned to provide technical assistance to support the FGS's formulation of the country's ninth National Development Plan (NDP) that is aimed to serve as an interim PRSP.[56] Efforts in building institutional, organizational, human resource and policymaking capacities have been instrumental, allowing the country to implement three IMF SMPs thus far successfully.

In sum, re-emerging from conflict, Liberia and Somalia have faced difficult circumstances, with human, institutional and policymaking capacity shortages impacting the two countries engagement in the debt relief process. To address this issue, with the support of the international community, both countries quickly mobilized human resources, launched institution-building interventions and benefited from policymaking support. Clearly, for Somalia, the successful completion of three IMF SMPs during mid-2016—mid-2019 is a testament to the progress the country has made in improving economic governance, building institutions and strengthening its capacities to develop and implement sound policies. However, going forward, as SMP IV has been qualified as a "full" IMF-supported program (implementation of which would count toward HIPC Decision Point), the government's continued efforts to improve the quality of governance, institutions and policymaking will be of chief importance and will have significant implications on how

51 This was the SMP that met the standards of an IMF UCT program approved by the IMF Board of Executive Directors on July 2007.
52 Human resource challenges facing subnational administrations, especially those of the emerging states (Jubaland, Galmudug, Hirshabelle, and Southwest), may be even more daunting.
53 These include projects and programs funded by the World Bank-administered Multi-Partner Fund, the African Development Bank, the UN Development Programme-administered Multi-Partner Trust Fund and from the forthcoming EU State and Resilience Building Contract, among other donor-supported programmes and projects.
54 See IMF Country Report No. 19/256
55 That is, macroeconomic policy, monetary policy, exchange systems, macroeconomic and financial statistics, financial sector reforms and tax policy and administration reforms.
56 See IMF Country Report No. 19/67.

soon the country could qualify for the HIPC Initiative.

### 4.1.3. Political leadership

While the capacity for sound economic policymaking and quality of institutions (and related IFI conditionalities) are the main determinants in the HIPC debt relief decision-making process, political engagement by the government and certain development partners is a key success factor that also plays a crucial role. Thus, a country vying to secure debt relief would need to become engaged politically to: (i) secure support for expedited and deep debt relief from its external creditors and development partners; and (ii) minimise political opposition and maximise political support for the debt relief-related economic reforms on the domestic front.

From the Liberian experience, it is clear that the country's engagement in the HIPC Initiative was leadership-driven. The executive leadership, President Sirleaf, her cabinet (particularly the Minister of Finance) and the Central Bank Governor, initiated, drove and steered the country's debt relief process until the country secured deep debt relief and graduated from the HIPC Initiative. According to one former Liberian government official, "Debt relief for Liberia would not have been possible without strong leadership from President Sirleaf who took ownership of the debt relief process and worked to avoid any derailment."[57] Throughout the debt relief process, President Sirleaf provided the overall guidance and strategic direction based on her knowledge of: (i) bureaucratic, political and business actors with vested interests against reforms (particularly the anti-corruption drive);and (ii) political windows of opportunity to advance Liberia's debt relief agenda at the global level. In the domestic political arena, Sirleaf's experience as a Liberian civil servant and decades-long foray into Liberian politics[58] gave her the skills and experience to navigate Liberia's complex and challenging political economy to push needed reforms. In the international arena, Sirleaf's extensive international experience[59] and the vast network of international politicians, bureaucrats and influential people acquired from her long experience in international policymaking circles, contributed to pushing the Liberia debt relief envelope further and in obtaining debt relief faster.

At the start of her first term in office, Sirleaf made it clear to stakeholders that securing debt relief for her country would be a top national priority of her administration. This was not just political rhetoric, as President Sirleaf took ownership of the reform program. Her full and unwavering support to the debt relief agenda assured senior government officials, including the Minister of Finance, Central Bank Governor and other key ministers, the political backing they needed to implement bold reforms, and compelled bureaucrats that may have resisted reform to toe the President's line. Moreover, Sirleaf's leadership in her government's reform agenda also signalled to the IFIs, external creditors, development partners and the broader international community that the country would play an active and central role in the debt relief process.

In terms of garnering political support from the international community for Liberia's bid for expeditious debt relief, President

57 Interview with former government official.

58 Sirleaf's political experience includes serving as an Assistant Minister of Finance (1972-73 and 1977-79) and Minister of Finance in the Tolbert administration (1979-80) and President of the Liberian Bank for Development and Investment (1980). Sirleaf also was also elected as a senator in the 1985 general election but had been incarcerated as a political prisoner shortly thereafter (see Scully, 2016).

59 Sirleaf's international experience includes working as a Senior Loan Officer at the World Bank, Vice President of the Africa Regional Office of Citibank (1981-85), Vice President and Executive Board Member of Equator Bank (1986-92), Assistant Administrator and Director of UNDP's Regional Bureau for Africa (1992-97) and was the Chairperson of the Open Society Initiative for West Africa (OSIWA) from 2001.

Sirleaf proactively leveraged her credibility and good standing, tapping into her broad support network, including from politicians, former senior bureaucrats and influential individuals in creditor countries. For instance, she reached out to Steve Radelet a former US Deputy Assistant Secretary of the Treasury for Africa who was working for the Centre for Global Development (CGD), a US-based think tank, to seek his technical and advisory support (Cooper, 2017). Radelet had earned a reputation as being a savvy international bureaucrat who knew the ins and outs of the international financial system, including the HIPC debt relief process. CGD, however, was not particularly accustomed to having its staff provide technical and advisory support to countries and had lacked the financial resources to have staff available to provide such service[60], viewing such a task as being more in the purview of the IFIs. George Soros, the billionaire philanthropist and founder of the Open Society Institute, a long-time friend of President Sirleaf who believed in her leadership, moved in to fund Radelet's support to Liberia after hearing about Sirleaf's need for support (Cooper, 2017).

In order to fill the human resource gap needed to manage the debt relief process and its associated reforms, President Sirleaf not only sought assistance from foreigners but also tapped into the potential of the Liberian diaspora, filling her cabinet, senior civil service and advisory posts with diaspora returnees (Blum et al., 2019). She was well aware that the HIPC Initiative was a rigorous process that would require a Minister of Finance with experience as an international technocrat to manage the HIPC process, and therefore, appointed Antoinette Sayeh, a former World Bank staffer, as Liberia's Minister of Finance to lead on Liberia's engagement in the IFI-administered HIPC process. As Minister of Finance, Sayeh was responsible for the implementation of economic reforms associated with the debt relief process. Moreover, regular meetings and engagements with IFIs, external creditors and debt relief advisors had allowed Sayeh to provide President Sirleaf with crucial information and insights, which were utilized by Sirleaf during her high-level missions abroad. Hence, "close and regular coordination between the Presidency and the Ministry of Finance was critical to furthering Liberia's debt relief aims."[61]

In seeking to expedite the debt relief process, the Sirleaf administration had employed strategies that created, sustained and elevated the sense of urgency on the need for expedited and deep debt relief required to kick-start the country's urgent reconstruction and poverty alleviation needs amongst the international community. In their meetings with dignitaries and counterparts and in international foras in Washington D.C. and other locations, both Sirleaf and Sayeh called for swift and deep debt relief. This sense of urgency helped shape a favourable international environment that facilitated expedited and deep debt relief.

The Sirleaf administration also took political leadership in engaging its supporters in creditor circles and in international networks to resolve and draw media attention to bottlenecks in the country's debt relief process. For instance, with the support of these actors, the Sirleaf administration helped influence the IFIs to mobilize resources for Liberia's debt relief. The country faced the challenge of mobilizing resources for the clearance of IFI arrears and for the participation of IFIs in the HIPC Initiative and MDRI, as the country was not included in the original financing framework of the HIPC Initiative.[62] As Liberia came closer to reaching its Decision Point, IFIs had to scramble to raise resources required for arrears clearance and their participation

60 See Supporting Liberia's Reconstruction and Development. Available at: https://www.cgdev.org/topics/supporting-liberias-reconstruction-development. Accessed on 9 May 2019.
61 Interview with former advisor of the Ministry of Finance.
62 The HIPC and MDRI Trust Funds were established to finance IFI participation in the HIPC Initiative and MDRI

in the HIPC Initiative. By December 2007, while the World Bank and AfDB both cleared Liberia's arrears, the IMF was slow in mobilizing the needed finances to clear arrears and to cover their HIPC and MDRI costs. The IMF had to mobilize funds from a multitude of their member countries, requesting them to contribute small portions of balances collected in their First Special Contingent Account that would be transferred to a designated account – the Administered Account for Liberia.[63] This account was established to fund the delivery of IMF debt relief for Liberia.

As the IMF fundraising process became difficult, the Sirleaf administration and its international partners, namely the US, actively courted other IMF member states to contribute to the Administered Account for Liberia. In addition, Sirleaf sought the help of world-renown musician, activist and influencer Bono to shine a light on Liberia's external debt problem. In an interview with the Financial Times[64], two days before the start of the 2007 IMF-World Bank Annual Meetings, Bono had challenged the IMF to do more to help the impoverished country (Cooper, 2017). The combined efforts mentioned above helped to secure financial contributions from 102 IMF member countries to meet the IMF financing gaps for debt relief.[65] The political leadership shown in forming alliances and mobilising support for an expedited debt relief process by Sirleaf and her team was arguably key in influencing the IMF to move quicker on the issue than they may have otherwise.

In dealing with the issue of vulture funds who often prey on HIPC countries, President Sirleaf again demonstrated leadership and political savvy.[66] Early on, her team had identified a US-based law firm that specializes in sovereign debt restructuring to take these vulture funds on in court. To prevent the seizure of sovereign assets, she had instructed her team to transfer assets to two banks[67] that shelter sovereign assets from creditor seizures.[68] Though 97.5 per cent of the holders of Liberia's commercial debt participated in a World Bank-financed debt buyback operation in April 2009, two vulture funds holding the remaining 2.5 per cent chose not to participate and instead sought legal action (Wong, 2012). In November 2009, a court in the United Kingdom (UK) ruled in favour of the two vulture funds, awarding them US$ 20 million[69], "seriously jeopardizing Liberia's recovery from civil war" (Arnone and Presbitero, 2011). To avoid making costly payments to these two unrelenting vulture funds, Sirleaf enlisted the help of an investigative journalist who released an exposé on the individual behind one of the vulture funds, effectively ending the fund's pursuit of claims against Liberia (Cooper, 2017). In addition, Sirleaf also endorsed the efforts of advocates, including Jubilee UK, that were instrumental in the UK parliament's passage of the Debt Relief (Developing Countries) Act 2010 that restricts vulture funds from making excessive profits from low-incoming developing countries. The passage of the law saved Liberia approximately US$ 40 million in court-ordered debt/claims payments[70],

63 The First Special Contingent Account was established to mitigate against the risk posed to the Fund's financial health by overdue financial obligations. The balances accrued to each shareholder are refunded in the event that there are no overdue financial obligations in that year.
64 See Eoin Callan, "Bono takes IMF to task on Liberia," *Financial Times*, October 19, 2007. Available at: https://www.ft.com/content/02c04b08-7d9d-11dc-9f47-0000779fd2ac. Accessed April 19, 2019.
65 The contributions from 102 IMF member countries were used to finance the IMF's arrears clearance operation and HIPC and MDRI-like debt relief operations for Liberia's IMF debts. For more detail see Box 3.10 Liberia's Debt Relief in IMF. 2014. IMF Financial Operations 2014. Accessed on 27 April 2019. Available at: https://www.imf.org/external/pubs/ft/finop/2014/pdf/finop2014.pdf.
66 Vulture funds are essentially investment pools similar to venture funds, with the only difference being that venture funds seek out investments in up-and-coming firms while vulture funds invest in securities of distressed companies or countries.
67 The New York Federal Reserve or the Bank of International Settlements
68 See Scott (2007).
69 See BBC, "Liberia ordered to pay 'vulture funds' over 1978 debt. *BBC*, November 26, 2009. Available at: http://news.bbc.co.uk/2/hi/africa/8380117.stm. Accessed 18 August 2019.
70 See *BBC,* "Liberia agrees deal with 'vulture funds'. *BBC*, November 23, 2010. Available at: https://www.bbc.com/news/world-africa-11819276. Accessed 19 August 2019.

and creates a favourable precedent for other low-income countries being targeted by unscrupulous vulture funds.

To enhance external creditor confidence in the quality of Liberian institutions, Sirleaf knew that it was critical to remove the perception of corruption in the Liberian public sector. However, doing so meant that she would need to resist pressures from the political and business elites in the domestic arena that had profited under Liberia's war economy and decades of mismanagement and corruption. Despite this, she demonstrated strong political leadership in tackling corruption. In her inaugural address in 2006, Sirleaf doubled down on her election campaign promise to end corruption. During her first term in office, Sirleaf backed up the political rhetoric by rolling out several measures to tackle corruption. These measures include, among others, the: introduction of a biometric identification system for the civil service that resulted in the removal of 4,700 ghost workers from the government payroll[71]; the introduction of a Civil Service Code of Conduct; the establishment of an Anti-Corruption Commission in 2009; and issuance of Executive Order No. 2 on "Protection of Whistleblower" that provides legal protection to those who report on corrupt practices in the public and private sectors. The Sirleaf administration's efforts to tackle corruption had successfully altered the international community's long-held perception of Liberia as a country prone to high levels of corruption and mismanagement.

Similar to Liberia, Somalia's leadership have made it clear that securing debt relief is a key priority for the country. However, due to frequent changes of government (four changes of the cabinet from 2012 to present), Somalia compared to Liberia was put at a disadvantage, as different governments had to navigate the steep debt relief learning curve. As in Liberia, in an effort to enhance the human resource capacities to support the debt relief process, Somalia's leadership appointed diaspora returnees as ministers and senior civil servants. A number of these diaspora returnees had previously worked for international institutions, injecting skills and expertise to Somalia's re-emerging public sector. When it comes to the implementation of economic reforms - the fundamental driving force of the debt relief process - Somalia experience is comparable to Liberia's. According to the IMF, the FGS is making credible efforts towards implementing reforms under the SMP as indicated in the most recent IMF Staff Report: "Despite these headwinds, staff is encouraged by the authorities' determination to meet their commitments under successive SMPs. The authorities' consistent implementation of difficult reforms has helped maintain macroeconomic stability and build capacity in key institutions covering all economic and financial sectors."[72]

Measures to tackle corruption in Somalia are also comparable to the ones in Liberia. For instance, from 2012-19, the FGS was able to: achieve the launch of a revised payroll system and biometric identification system for the civil service in 2014; establish a Somalia Financial Management Information System that records expenditures, controls spending and provides timely and accurate financial reports; passage into law of the Public Procurement, Concessions and Disposal Act in 2015; the passage of the Anti-Corruption Bill by both the upper and lower houses of parliament; and the adoption of a PFM Bill by cabinet in 2017. Over the past year, the Somali government has also taken a progressively tougher stance on corruption, as indicated by the recent arrests and prosecution of public officials alleged to have been involved in corrupt practices.

To sum up, the political instability of the past and the debt relief learning curve have limited Somalia's leadership in becoming

71 See Yearbook of the United Nations, 2006 Vol. 60
72 See IMF Country Report No. 19/256.

strategically engaged in the country's debt relief process in contrast to Liberia. Somalia's government is cognisant that the country's reconstruction and development hinge on it being able to quickly normalize relations with external creditors to gain access to new grant and concessional resources, and hence willing to demonstrate the ability to steer the country's engagement in the debt relief process. However, it should be noted that Somalia's leadership has yet to solidify some of the key strategies, tactics, and alliances that were instrumental in the context of Liberia's experience with the debt relief process.

### 4.2. International level: the support of a champion

At the international level, we examine one standout success factor that helped advance Liberia's debt relief process; that is, the support of an influential creditor government or "champion."

Securing a champion can help accelerate a country's progression through the debt relief process. The champion can leverage its influence within IFI Boards, creditor circles and plurilateral bodies such as the Group of Seven (G7) to push for an acceleration of the debt relief process. A creditor country can decide to become a champion for reasons that may stem from security, political, economic and humanitarian motivations or a combination of these. Countries lacking the support of a champion may experience a longer debt relief process. While a country should look to secure broad-based support among as many creditor governments as it can, having a champion helps a country seeking debt relief secure a more positive reception from its other external creditors who may have otherwise been indifferent to the country's bid. An ideal champion would be a country that has sizeable shares within the IFIs and influence within the Paris Club, making countries from the G7 generally the best suited to take up the role.

In the case of Liberia, the US support was critical in generating the political and policy momentum for an expedited debt relief process for the country. At a donors' conference in 2007, US Secretary of State, Condoleeza Rice stated that the US would cancel all of its claims on Liberia as part of the HIPC framework, exemplifying the US's role as a champion for Liberia.[73] With that statement, the US became the first creditor to openly commit to cancelling Liberia's debts more than a year before the country reached its Decision Point. The US played a significant role in the IFI arrears clearance process, providing two bridge loans to clear IMF and World Bank arrears[74] and financial contributions to the AfDB's arrears clearance operation.[75] It also played an instrumental role in helping secure resources that would enable the IMF to deliver its share of debt relief under the HIPC Initiative. In assisting Liberia in securing resources to be channelled to the IMF's Administered Account for Liberia, the US Department of Treasury sent letters to IMF member countries urging that they contribute a certain portion of the balances remaining in the First Special Contingent Account.[76] The support and contributions provided by the US facilitated the normalization of Liberia's financial relations with the IFIs, which was followed by that with bilateral,

73 See Sue Pleming, and Lesley Wroughton, "U.S. plans to cancel $391 million in Liberia debt," Reuters, February 13 2007. Available at: https://www.reuters.com/article/us-liberia-usa-debt/u-s-plans-to-cancel-391-million-in-liberia-debt-idUSWAT00695320070213. Accessed on 1 May 2019.
74 See IMF Survey: IMF to Back Liberia With Debt Relief, New Financing. 18 March 2008. Available at: https://www.imf.org/en/News/Articles/2015/09/28/04/53/sonew031808a. Accessed on 5 May 2019.
75 Financing for the clearance of AfDB arrears was provided by a consortium of countries that include the United States, EU, Nigeria, Germany, the United Kingdom, Canada, Norway, South Africa, Sweden, Switzerland, Finland and Denmark (see AfDB. 2007. Liberia: Proposal for Arrears Clearance Under the Arrears Clearance Programme and Post-Conflict Country Facility. Available at: https://www.afdb.org/fileadmin/uploads/afdb/Documents/Financial-Information/00157381-EN-LIBERIA.PDF. Accessed on 1 May 2019.
76 Interview with former advisor of the Ministry of Finance.

other multilateral and commercial creditors. The US also helped the country engage its commercial creditors: in 2008, the New York Federal Reserve hosted the first meeting between the country and this creditor group, with the Federal Reserve signalling to commercial creditors that it would be in their best interests to cooperate with Liberia in the debt relief process (Cooper, 2017).

The US had a number of motives that may explain why it engaged in helping to broker a peace settlement in Liberia and championed Liberia's bid for debt relief. First, one apparent reason was the long-standing and unique relationship between the United States and Liberia, as the country was founded by freed American slaves. Second, in the face of intense domestic and international criticism for its intervention in Iraq, the US administration took a greater leadership role in brokering a peace settlement and in engaging in Liberia's post-conflict reconstruction to rebut its critics who had argued that the US's unwillingness to intervene during the Second Liberian Civil War "undermined its human-rights justification for the Iraq war" (Kabia, 2009). Third, some international actors such as the United Kingdom (UK), France, the AU, and the UN Secretary-General urged the US to play a more active role in Liberia (Kabia, 2009).[77] Fourth, there were clear humanitarian motives by the US administration toward Liberia as the country was recovering from conflict and was still in humanitarian distress. Fifth, there may have been interests to re-establish long-held commercial relations with the country, as many US companies in the extractive sector were operating in the country prior to the breakout of conflict in 1989.[78] Sixth, and arguably most important, an accelerated debt relief process, leading to the normalisation of relations with external creditors, would spread the burden of financing Liberia's reconstruction amongst several countries and multilateral institutions (relieving the US of the full burden), as creditor practices restricted them from providing new loans to countries with protracted arrears.

Somalia's experience in securing a champion differs significantly from Liberia's. To date, an influential creditor government has yet to take on the role of a champion for Somalia, although the European Union (EU) Commission has called for the acceleration of the debt relief process. Among the aims of the EU's recent budget support to Somalia was to provide a political signal to the IFIs and external creditors to speed up Somalia's re-engagement process with the international financial community.[79] While the EU's support, is a positive contribution to the acceleration of Somalia's debt relief process, the EU is limited in its capacity to serve as a champion for Somalia as it is a multilateral institution and not a creditor.

In comparing Liberia and Somalia's experience in this key success factor, it is important to highlight the international development cooperation landscape during the years since Liberia's engagement in the debt relief process in 2005-08 has changed. One notable and acute difference is that influential countries, namely the US and the UK, have become increasingly concerned over domestic political issues of late (e.g., Brexit), leaving little bandwidth for development-related issues affecting LDCs. Despite this challenge, there still may be windows of opportunity for Somalia to exploit to secure the support of an influential creditor government that can advocate for

77 France and the UK's insistence that the US play a more active role in the conflict stemmed from their concerns that continued conflict in Liberia had regional spillover effects that led to conflicts in neighboring Côte d'Ivoire and Sierra Leone, with both countries having a stake in ensuring peace and stability in their former colonies (Kabia, 2009).
78 According to Adebajo (2002), prior to the First Liberian Civil War, a number of US companies were operating in the country. These companies included: Firestone, Goodrich and Uniroyal that had established and operated rubber plantations; Bethlehem Steel that had established and operated an iron ore mine; and a number of financial institutions such as Citibank, Chase Manhattan and Chemical Bank that had all operated local branches in the country (Adebajo, 2002).
79 See European Commission. 2018. Action Document for the Implementation of the Horn of Africa Window (T05-EUTF-HoA-SO-59 – Somalia State and Resilience Building Contract.

swift and deep debt relief, especially among key G7 countries, namely the US and the UK.

Both the US and the UK have been playing pivotal roles bilaterally and in international institutions in supporting humanitarian, political, security and economic developments in Somalia and are among the country's external creditors, with the US being the largest, making them well suited to take on a champion role. Since the outbreak of conflict, the US and the UK have provided significant humanitarian contributions to UN agencies and other humanitarian organisations. On the security front, the two countries have funded peace and security operations, including the deployment of military personnel that provides security assistance to the Somali National Army. On the political front, the US and UK have assisted in Somalia's state-building process and in laying the foundations for federalism and democracy. On the economic front, there have been indications that the US and the UK are willing to cooperate and support the long-term development of the country, including in the exploitation of its natural resources.

In summary, at the international level and in contrast to Liberia, Somalia is yet to secure a champion to help push its debt relief agenda within the IFIs and in creditor circles, with the risk that this might prolong the duration of the process. As in the case of Liberia, Somalia could greatly benefit from the support of an influential creditor government that steps in as a champion for a speedy and deep debt relief process for the country. In view of the US and UK's long-standing relationship with the country and their keen interest in having a stable, resilient and self-sustaining Somalia, there are good prospects for Somalia to have one of these two countries champion the country's debt relief cause. Key to securing a champion will be for Somalia to tap the potential motives of influential creditor governments such as the US and the UK that could step into the role.

# 5. Conclusion and lessons learned

There are striking historical parallels between Liberia and Somalia from the authoritarian and conflict period to the period of re-engagement with the international community. The similarities include: long periods of authoritarian and undemocratic rule with both countries having a former military man at the helm; gross mismanagement of the economy that led to economic troubles, including the inability to service external debt; the breakout of conflict, its subsequent protraction and the continual accumulation of external debt arrears throughout the conflict period; and a sustained period of re-engagement with the international community that includes both countries foray into the debt relief process. However, despite these historical parallels and similar starting points at the start of their re-engagement process, a marked difference is in the duration of the debt relief process. In a little over two years from the start of its first SMP, Liberia was able to have its arrears cleared and qualify for HIPC debt relief and in a little over two additional years, it obtained debt cancellation for almost 100% of its Paris Club debt, 97% of its commercial debt and 90% of its multilateral debt. In contrast, Somalia is making slow progress, as the country has not qualified for debt relief six years on from when it began its re-engagement process.

While the IMF and World Bank claim that the debt relief decision-making process is premised on issues around economic governance, institutional quality and in the implementation of sound policies, Liberia and Somalia's experience suggests that other factors play a role in expediting the debt relief process. In addition to making progress in securing the peace and having political stability in place, other critical factors include having the support of a "champion" country. In the case of Liberia, it is clear that the Sirleaf factor and the influence and resources that the United States brought into the debt relief process was instrumental in accelerating the process. In the case of Somalia, the country has not had the benefit of securing a "champion" to date and as a result, has gone through a rather sluggish debt relief process in comparison to Liberia.

The disparities in these two cases highlight that Somalia needs a political champion that can mobilize a coalition of creditors that are supportive of the country's debt relief efforts, including through contributions of financial resources to help finance IFI arrears clearance, HIPC and MDRI debt relief. In addition to Liberia, other FCAS countries such as Sierra Leone (UK) and Côte d'Ivoire (France) have benefited from the support of a champion. However, the question remains: which of Somalia's bilateral external creditors will fill this role? Only time will tell if Somalia will secure a champion. However, Somalia is not in a position to wait on a champion to provide support when that country so chooses, as low economic growth and weak institutions, both currently afflicting Somalia, are two factors that cause conflict to break out in Sub-Saharan Africa (Yartey, 2004). If a champion does not swiftly step in to help Somalia resolve its external debt problem, Somalia and the international community face the risk of undoing the immense security, political, social and economic gains made since 2012 as the country would sink deeper into a vicious poverty-conflict trap. Such an eventuality would be unfavourable to both Somalia and the international community.

Somalia will only be able to break free from the quicksand of the vicious poverty-conflict trap if the country can spur rapid economic recovery in the short-to-medium term and sustainable and inclusive economic growth in the long-term. The Somali government is making credible efforts to enhance its human resource and institutional capacity, improve economic governance and institutional quality and formulate, and implement sound policies to achieve such an objective.

Somalia's external creditors share responsibility in the country's external indebtedness given questionable lending practices of the past premised on strategic, security, economic and political considerations as opposed to ones around debt sustainability and economic governance. It is, therefore, high time that the country's external creditors and a champion country took meaningful steps to assist Somalia to swiftly resolve its external debt problem.

Overall, Somalia can learn many lessons from Liberia's experience in the debt relief process so that it may have a shorter and smoother debt relief process during the pre- and post-Decision Point periods and better face challenges in the post-Completion Point period

Salient lessons for Somalia and its development partners that can be drawn from Liberia's experience in both the pre- and post Decision Point and post-Completion Point periods are in the succeeding parts of this section.

### Lessons from Liberia's pre- and post-Decision Point periods

Section 4 detailed the four key success factors that facilitated an expedited debt relief process for Liberia and compared it to Somalia's experience. Several lessons can be drawn from the section. However, a few critical lessons to be learned from Liberia's experience are summarized below:

- **Consolidate gains in peace and security:** As evident in the Liberian case, the cessation of violence and socio-political stability created the enabling environment that facilitated a speedy debt relief process. To make a stronger case for debt relief, Somalia will need to continue to make progress in its peacebuilding, security, and stabilisation efforts.

- **Sustain improvements in economic governance, institutions and policymaking:** Primacy should be placed on improving the governance and quality of institutions and policymaking to allow Somalia to be able to successfully implement the current UCT-quality SMP IV that would qualify the country for the HIPC Initiative. Following Liberia's example, Somalia and its development partners will need to inject human resource capacities and best practice systems to supplement existing capacities.

- **Enhance political engagement in the debt relief process:** In Liberia's experience, strong and proactive leadership from the executive helped to drive the debt relief process forward both domestically and internationally. Somali should enhance their engagement and coordination in the debt relief process to push through reforms and secure broad-based support from creditor governments, development partners, and allies.

- **Mobilize resources for IFI debt relief operations (arrears clearance, HIPC and MDRI-like Debt Relief):** Somalia, a potential champion country and other development partners will need to mobilize resources for debt relief operations, as the country had not been included in the original financing framework of the HIPC Initiative (see annex for details on IFI resource needs for their participation in Somalia's debt relief process).

- **Develop strategies and forge alliances to generate political momentum and consensus for expedited and deep debt relief:** Following the Liberian example, Somalia's political leadership should also seek to develop strategies and forge alliances that could generate the political and policy momentum and consensus around expedited and deep debt relief for Somalia. Somalia can create a favourable international environment conducive for its debt relief objectives by making a sustained effort to create and elevate the sense of urgency for debt relief. Moreover, they should make the case that recent gains in the country remain fragile, and without much needed financial support required to kick-start reconstruction and advance poverty alleviation efforts, Somalia risks falling into a vicious poverty-conflict trap. In addition, the political leadership should undertake efforts to garner international support for a more flexible debt relief process as was given to Liberia to expedite the process and secure maximum debt relief.

- **Cultivate stronger relationships with influential creditor governments to secure a champion:** Somalia's political leadership will have to make a sustained effort to cultivate stronger relationships with the US, the UK and its other external creditors to secure a champion. Somalia and its allies will need to be strategic in leveraging the motivations (historical relationship, (geo)political, security, economic, humanitarian etc.) of influential creditor governments to have them take on the role of a champion.

## Lessons from Liberia's post-Completion Point period:

The latter part of Section 3.1 describes some of the pitfalls experienced by Liberia during its post-debt relief period. Given that there are high prospects for Somalia's qualification for debt relief under the HIPC Initiative in early 2020, one can reasonably expect Somalia will secure irrevocable debt relief in the medium-term period. Thus, Somalia and its development partners should engage in a broader discussion about what the future post-debt relief Somalia should look like going forward. Liberia's post-debt relief period provides some acute lessons that can help Somalia avoid costly mistakes made in Liberia that have jeopardized debt sustainability, hampered economic growth and development prospects and efforts to alleviate poverty. The lessons are as follows:

- **Continue efforts to establish and implement sound public debt management framework, strengthen institutional debt management capacity and ensure debt sustainability:** Somalia will need to establish a robust legal and institutional framework for public debt management[80]. In future, Somalia will also need to develop and implement a medium-term debt management strategy that articulates the government's debt management objectives and informs their external borrowing. In the case of

80 In the case of Somalia, the legal and institutional framework would be articulated in primary and secondary legislation that would most likely contain provisions on: (i) the legal authority to borrow and issue debt; (ii) transparency and accountability measures; (iii) the institutional structure and arrangements for debt management; (iv) institutional framework for coordination of debt management with fiscal and monetary policy and between the debt management entity and the budget, cash management and development planning units; and (v) prohibitions/limits on subnational borrowing; among other provisions.

Liberia, the country has contracted non-concessional loans of late[81], increasing its debt burden and raising its risk of debt distress (if funds from these loans are disbursed). Somalia should learn from Liberia's mistake and limit external financing to concessional loans and grants during the country's post-debt relief era.

- **Develop a robust public investment pipeline under NDP 9 and ensure that borrowing is used for productive purposes:** During Liberia's post-debt relief period, the Liberian government did not have an adequately detailed, appraised and costed pipeline of externally-financed priority public investment projects in its NDP – Agenda for Transformation. An IMF assessment of Liberia's public investment management capacity states: "concessional loans and grant funding are often driven by the priorities of donors rather than the GoL [Government of Liberia]. In extreme cases, concessional loan agreements have been concluded without the project details being finalized, appraised, or adequately costed...externally-financed projects are planned through separate processes."[82] Not having a robust pipeline of detailed, appraised and costed donor/creditor-financed public investment projects in the country's NDP hindered the efficiency of public investment in Liberia. Looking forward, Somalia and its development partners should work to ensure that NDP 9 has a fully detailed, appraised and costed pipeline of public investment projects that promote pro-poor growth, with development partners committing to financing specific projects.

- **Continue efforts to improve the overall business climate to sustain FDI inflows:** Following the granting of debt relief for Liberia in mid-2010, Liberia received massive inflows of FDI between 2010-13. These FDI inflows were channelled mainly to rehabilitating critical infrastructure (e.g., transport networks and private facilities) in the mining (iron ore) and palm oil sectors, as there was a serious deterioration in vital physical infrastructure, owing to destruction and maintenance neglect associated with the conflict. However, it appears that the surge in FDI inflows was driven mainly by favourable commodity prices, as evident in the steep drop in FDI inflows following the mid-2014 commodity price bust and the 2014 Ebola crisis. In a forward-looking post-debt relief Somalia, one could expect massive FDI inflows (most probably targeting the extractive sector) à la Liberia. The rents from extractive industries (if used prudently) can significantly contribute to economic growth, development and poverty alleviation. However, as evident in the Liberian experience, over-reliance on rents and FDI inflows from extractive industries comes at a cost during periods of unfavourable commodity prices. Hence, going forward, Somalia should utilize a two-pronged approach that aims to attract FDI in the extractive sector and to other sectors (e.g., manufacturing, services, tourism etc.) by creating an enabling business environment. Creating the enabling environment would entail the implementation of reforms that would remove legal, macroeconomic, political, financial, security, and infrastructural disincentives for foreign investment. If Somalia establishes an enabling environment for FDI, the country would have improved prospects for sustained FDI inflows (if inflows are well-monitored and competition is encouraged), with local businesses and the labour market benefiting from the accompanying innovation, technology, economies of scale and scope, skills and managerial expertise provided by foreign firms.

81 See IMF Country Report No. 19/256.
82 See IMF Country Report No. 16/352.

# Annex

# Resources needs and mobilisation required for IFI debt relief operations

Somalia owes US$322 million[83], US$ 346 million[84], and US$ 110 million[85] to the IMF, the World Bank, and the African Development Bank, respectively. These are sizeable amounts, and hence, there will be a need to secure US$ 778 million to clear arrears to the IFIs.[86] A brief description of the available resources and possible modalities for arrears clearance is provided below.

**African Development Bank:** Arrears owed to the AfDB are cleared through a tripartite burden-sharing approach between the country, the AfDB and a donor country (or multiple). The Bank's contribution is provided through Pillar II resources of the TSF[87], with the vast majority of those resources coming from the Bank's concessional financing window – the African Development Fund (AFD). As per Bank policy, Pillar II resources for arrears clearance are allocated on a first-come, first-served basis. In addition, AfDB policy strictly prohibits the use of Bank resources in what may be construed as refinancing operations. As such, for Somalia, the use of Pillar II resources can only be applied to clear arrears to AfDB[88] and Nigerian Trust Fund arrears (~25% of the total arrears or ~US$ 28 million), as ADF resources cannot be used to clear ADF arrears given that the TSF Pillar II consist mainly of ADF resources.[89] For Somalia, the vast majority of its external debt arrears is ADF arrears that comprise 75% of total arrears (~82 million) owed to the Bank. Hence, the remaining 75% would need to be financed through donor contributions, owing to the government's limited payment capacity. In addition, resources from donor partners will also be required to allow the Bank to provide MDRI debt relief to Somalia.

**IMF:** In the case of the IMF, in a fashion similar to Liberia, the Fund will need to mobilize resources to clear Somalia's IMF arrears (~US$ 322 million). In the case of Liberia, a number of IMF member countries were approached and were kindly requested to contribute small portions of balances collected in their First Special Contingent Account to an Administered Account for Liberia that would be used to cater for an arrears clearance operation and for the Fund's participation in the HIPC Initiative and an MDRI-like or beyond-HIPC debt relief operation. Currently, the IMF is working to develop a proposal on different modalities to clear Somalia's arrears with the Fund in

83 The arrear amounts stated above were calculated from SDR amounts provided in the IMF Financial Statements 2019 using 30 April 2019 US$/XDR exchange rate, as the amounts stated in SDR were as of 30 April 2019.
84 As at 23 April 2019 (see the Demand for IDA19 Resources and the Strategy for their Effective Use - May 2019; IDA19).
85 As at 31 July 2019 as per information shared in an email correspondence with senior AfDB staff, August 14, 2019.
86 The World Bank has the resources available to clear all of Somalia's arrears (~US$ 346 million), and the AfDB has enough to clear about a quarter (~US 28 million). Hence, there is a need to mobilize ~ US$ 404 million (US$ 322 million for IMF arrears and US$ 82 million for 75% of AfDB arrears) to enable both the IMF and AfDB to entirely clear Somalia's arrears to both institutions.
87 The TSF is an operationally autonomous trust fund within the AfDB.
88 The AfDB is the Bank's non-concessional financing window.
89 Email correspondence with senior AfDB staff, July 19, 2019.

advance of the upcoming IMF-WB Annual Meetings.[90] The Liberian model will inform the proposal for arrears clearance, and will likely contain fundraising modalities that include member country contributions from the First Special Contingent Account.[91] Moreover, the IMF will take a slightly different approach than in Liberia by looking to seek member grant contributions beyond the G7.[92]

**World Bank:** When the Bank was raising resources required for the clearance of Liberia's World Bank arrears during the IDA15 replenishment, it not only mobilized resources for the clearance of Liberia's arrears but also factored in the resources that would be required to clear the arrears of many other protracted arrears cases.[93] Since then, the Bank had utilized these Funds to clear arrears when countries had neared their respective Decision Points. The World Bank's IDA-18 financing envelope had allocated US$ 1.1 billion for an arrears clearance set-aside, which is more than enough to clear Somalia's arrears with the Bank.[94] The IMF's most recent staff report states the following on the IDA arrears clearance set-aside: "The World Bank has sufficient resources set aside for an arrears clearance operation as soon as the HIPC DP is reached."[95] Furthermore, a recent IDA19 replenishment paper, notes the following: "Somalia is making progress and could reach the HIPC decision point towards the end of IDA18. Thus, the proposed size of the set-aside assumes that Somalia clears arrears in IDA18, and that the remaining unused IDA18 fund for arrears clearance would be carried forward to IDA19."[96]

90 Email correspondence with senior IMF staff, July 30, 2019.
91 Ibid.
92 Ibid.
93 See IDA's Further Elaboration of a Systematic Approach to Arrears Clearance, June 2007, IDA15.
94 See the Demand for IDA19 Resources and the Strategy for their Effective Use - May 2019; IDA19
95 See IMF Country Report No. 19/256.
96 See the Demand for IDA19 Resources and the Strategy for their Effective Use - May 2019; IDA19

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## About the Debt Cancellation Advocacy Working Group:

To help Somalia tackle its external debt problem as a means of helping the country address its humanitarian and development challenges, a diverse group of non-governmental organizations (NGOs) that work in Somalia have come together to offer support to the people of Somalia and its government in their bid for expeditious and full debt cancellation. This Debt Cancellation Advocacy Working Group is under the banner of the Somalia NGO Consortium.

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