PROMOTING A RESILIENT AND INCLUSIVE PRIVATE SECTOR IN FRAGILE CONTEXTS - SOMALIA

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ABOUT INTELLECAP

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ABBREVIATIONS AND ACRONYMS

ATM	Automated teller machine
B2B	Business to Business
B2C	Business to Consumer
BDS	Business Development Services
BMGF	Bill and Melinda Gates Foundation
CBS	Central Bank of Somalia
CEO	Chief Executive Officer
CIFF	Children's Investment Fund Foundation
COMESA	Common Market for Eastern and Southern Africa
DANIDA	Danish International Development Agency
DCA	Development Credit Authority
DCI	Development Corporation for Israel
DFAT	Department of Foreign Affairs and Trade
DFC	Development Finance Corporation
DFI	Development Finance Institutions
DHF	Doses of Hope Foundation
ECB	External Commercial Borrowings
EMI	Equated Monthly Instalments
EMR	Electronic Medical Record
ESO	Ecosystem Support Organisations
FCA	Finn Church Aid
FCDO	Foreign, Commonwealth & Development Office
FCV	Fragile, Conflict, and Violent
FDI	Foreign Direct Investment
FI	Financial Institutions
FMO	Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden N.V.
GAM	Global Acute Malnutrition
GDP	Gross Domestic Product
GEEL	Growth, Enterprise, Employment, and Livelihoods
HNI	High Networth Individuals
ICT	Information and Communications Technology
IDP	Internally Displaced Population
IFAD	International Fund for Agricultural Development
IFC	The International Finance Corporation
IFU	Investment Fund for Developing Countries
IGAD	Inter-Governmental Authority on Development
IIX	Impact Investment Exchange
IMF	International Monetary Fund
IT	Information Technology
KWh	Kilowatt-hour
KYC	Know Your Customer
MFI	Microfinance Institution

ABBREVIATIONS AND ACRONYMS

MIGA	Multilateral Investment Guarantee Agency
MoPIED	Ministry of Planning, Investment, and Economic Development
MTB	Money Transfer Businesses
NBFC	Non-Banking Financial Companies
NCRI	National Commission for Refugees, and Internally Displaced Persons
NGO	Non-Governmental Organisation
NIPS	National Investment Promotion Strategy
ODA	Official Development Assistance
OEF	One Earth Future Foundation
OIC	Organization of Islamic Cooperation
PE	Private Equity
PFI	Potential Financial Institutions
SBCF	Somali Business Catalytic Fund
SBIN	Somali Business Investment Network
SCALED – UP	Somalia Capacity Advancement, Livelihoods and Entrepreneurship, through Digital Uplift Project
SCORE	Somali Core Economic Institutions and Opportunities Programme
SDG	Sustainable Development Goals
SIDA	Swedish International Development Cooperation Agency
SIMA	Social Investment Managers and Advisors
SME	Small and Medium Enterprises
SMEF	Small and Medium Enterprise Facility
SMS	Short Message Service
SOMINVEST	Somalia Investment Promotion Office
SPV	Special Purpose Vehicle
SRA	Somali Revenue Authority
TA	Technical Assistance
UK	United Kingdom
UN	United Nations
UNDP	United Nations Development Programme
UNHCR	United Nations High Commissioner for Refugees
UNICEF	United Nations Children’s Emergency Fund
UNIDO	United Nations Industrial Development Organization
UNOPS	United Nations Office for Project Services
USA	United States of America
USAID	United States Agency for International Development
USD	United States Dollar
VC	Venture Capital
VC4A	Venture Capital for Africa
WB	World Bank
WFP	World Food Programme
WTO	World Trade Organization

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EXECUTIVE SUMMARY

More than 20 years of civil war (1991 – 2012) devastated Somalia's economy, infrastructure, and public institutions. The country has slowly and steadily started to rebuild its economy and has seen sustained progress in the past decade. The country has grown at a moderate pace of 2.5 percent real GDP growth from 2013 – 2017, and the growth rate was forecasted at 3.2 percent in 2020 before the advent of Covid-19[1]. On the other hand, the civil war stagnated progress on most SDGs related to education, health, sanitation, and electricity access

Somalia is heavily dependent on remittances form the diaspora and they enable household[2] consumption at 132 percent of GDP and are a vital source of income for the bottom 40 percent of households. The years of disruptions and disturbances have affected economic growth, and several of its social dynamics. This has led to more than 69 percent of the population below poverty line as of 2017[3].

Somalia is highly dependent on foreign aid. The country received more than USD 2 billion in Official Development Assistance (ODA)[4] in 2017 and 2018 - a 57% increase compared to the previous five years levels (2012 – 16). ODA forms more than 27% of Somalia's GDP, making it highly dependent on foreign aid[5]. The domestic revenue for the Federal Government of Somalia is USD 184 million in 2018[6] compared to an ODA of USD 2.2 billion. The high dependence on external aid and remittances has added to the vulnerability of the economy, as remittance incomes have been hugely hit with the advent of the Coronavirus pandemic across the globe, leading to a 40 percent decrease in remittance income (estimates of the Federal Government of Somalia)[7].

The Government of Somalia has come up with a comprehensive National Investment Promotion Strategy (NIPS) to attract and retain foreign investment to enhance growth, create jobs, and consolidate economic growth and development. The Foreign Investment Law of 2015 guarantees foreign investors treatment equal to that given to domestic investors, fair compensation in the event of expropriation, international arbitration of disputes between the investors and the Government, the right to remit profits and access to foreign exchange.

Almost all of the stakeholders including investors, donors, ecosystem enablers such as incubators, accelerators and NGOs believe development of private sector holds the potential to catalyse economic growth and increase income levels across the country. The private sector landscape in Somalia is dominated by micro, small, and medium enterprises (MSMEs) that employ majority of the total workforce. Most of the businesses are established through bootstrapping and funds from friends and family. Access to finance remains on the foremost challenges

faced by entrepreneurs in the country. Most of the enterprises are engaged in trading of goods which are imported from other countries and sold locally.

To gain a more in-depth understanding of the impact-focused private sector in Somalia and its potential, Intellecap conducted detailed interviews with around 30 enterprises from the country. The study has categorised the interviewed enterprises into three broad categories to derive improved insights:

1) Access: These include enterprises that have developed innovative solutions to facilitate access to essential products and services for the communities. Somali citizens face severe challenges in accessing quality healthcare, nutritional food products, and affordable energy. Access enterprises are offering innovative solutions to address these challenges. Of 30 enterprises interviewed, around 53% of them provided access services. While some enterprises such as Abu Najib Fishing Co, a fish harvesting and processing entity, want to have a wider customer reach and therefore use an indirect distribution model of partnership with various retailers to sell their products, others, such as Durdur Onion, provide high quality, nutritious, and healthy onion for consumption in Somaliland, sell their products through direct marketing. Many of these enterprises rely on word-of-mouth for marketing, and their customer retention strategy is based on the provision of flexible payment options.

2) Ability: These include enterprises that develop and design solutions to improve income and employability, leading to an overall increase in quality of living. Of the 30 enterprises interviewed, around 33% were offering ability services. Many of these enterprises targeted the most relevant sectors such as agriculture to help farmers overcome the adverse effects of severe drought conditions. Enterprises such as Afri-tech manufacture organic fertilizers insect killer devices, & agriculture technology equipment to control weeds based on the local requirements. Few enterprises, while offering employment, also serve as an enabler for the wider private sector by providing essential services such as Information Technology and e-commerce.

3) Network and Knowledge: These include enterprises that build awareness and share information to initiate behaviour change and allow communities to reach unreachable markets. Of the 30 enterprises interviewed, around 14% were part of this category. Many of the enterprises in Somalia lack an understanding of the global norms of business operations, including governance, documentation, and fundraising. Some enterprises. Majority of the enterprises interviewed have cited the lack of training and capacity building as a major challenge for their business's growth. Enterprises such as Shaqadoon and Onward Endeavour offer consulting services, including training and other business development services for entrepreneurs and their staff. Shaqadoon visits other enterprises, assesses the problems, and has a pool of over 100+ consultants to provide relevant training. Some enterprises also adopted the strategy.

Having detailed discussions with the enterprises highlighted some of the private sector's critical challenges in Somalia. Lack of access to finance, high cost of finance, lack of critical infrastructure, lack of skilled manpower, and security related issues are the major challenges faced by enterprises in Somalia. More than 98% of loans from banks and financial institutions are provided to real estate and trading enterprises. Women and women-owned enterprises face a greater degree of discrimination and challenges in growing their businesses in Somalia. While women in Somalia own 60 percent of microbusinesses. they face greater challenges such as lack of access to information (due to lack of mobility outside the home and lower technological literacy), access to finance (some financial institutions still mandate a male signature), lack of women-friendly financial products, and lack of information regarding avenues of finance

To develop a holistic understanding of the country's impact sector, Intellecap undertook an in-depth analysis of the impact investment landscape as part of the study. The study included detailed interviews with industry stakeholders, including investors and ecosystem enablers. According to the research, there is a significant mismatch between demand and supply of impact capital in Somalia. Between 2005 and 2020, Somalia is estimated to have received USD 175 million in impact capital, from which the majority (75%) is contributed by donor agencies.

The study mapped several DFIs, including IFC, FMO, Swedfund, Norfund, IFU, and Islamic Development Bank. While some of the DFIs have directly invested in enterprises, others such as Norfund and IFC have indirectly invested through local financial entities. Some of the major sectors of direct DFI intervention in the country include agriculture and telecommunications. Apart from direct debt and equity investments, DFIs have also provided grants, political insurance, and technical assistance to impact enterprises across the country. While political risk insurance provides a backup for investors investing in fragile countries such as Somalia, technical assistance provides capacity building for these enterprises to streamline their operations. DFIs have also provided credit guarantees to banks and financial institutions for on-lending to impact enterprises.

Donors such as the World Bank, USAID, SIDA, FCDO, and DANIDA invested around USD 138 million between 2005 and 2020. While donors provided far greater funds for the overall development of the country, we have only considered the investments utilized for the growth of private sector in the country. Donors prioritize assisting enterprises in the impact sectors such as agriculture, financial services, fisheries, and dairy. Apart from providing grants and other financial investments, donors mostly involve themselves in market linkage activities such as introducing efficient irrigation systems, seeding export-oriented crops, constructing irrigation canals, access roads, landing-piers for boats, and training relevant personnel. Donors have also pioneered projects such as GEEL (Growth Enterprise, Employment, and Livelihoods) to increase the pace of Somalia's integration into the world economy. The programme aims to provide technical services to enterprises and address challenges and opportunities across multiple sectors through policy and regulatory reforms. Donors have also provided grant funding to enterprises through enterprise challenges and through incubators/accelerators. Donors have also provided on-lending credit facilities to banks and other financial institutions to lend to impact enterprises through institutions such as Gargaara.

Private fund managers have invested approximately USD 15 – 17 million in the last ten years in Somalia. Most of these investments are small ticket sizes, usually between USD 5,000 and USD 50,000. Despite these investments being small in comparison to DFI and Donor investments, they are of the utmost importance to the growth of entrepreneurship in Somalia. Many of the private deals go unreported due to investors' unwillingness to disclose and cultural factors that see fundraising as an enterprise's weakness. More than 67% of the investments are in the agriculture, Fisheries and Livelihood sector followed by manufacturing and energy. Private investors prefer to co-invest with a local investor to reduce the risk and mostly prefer to invest through debt (Islamic Finance). Somali diaspora has contributed significantly towards the growth of entrepreneurship scenario in the country.

Investors highlighted a few intriguing challenges that can be considered as reasons for the limited flow of private capital in the country. Financial challenges in transacting within Somalia, investing through Islamic finance, high macroeconomic and political risk and related currency risk along with lack of investible enterprises are the most common obstacles cited by investors. Other challenges include lack of country-level data and context due to limited research pieces and credible aggregated data sources.

Innovative investment instruments can help reduce the risk of investing in fragile economies such as Somalia. Many global organisations, DFIs, donors, and private impact investors have already started to find alternate ways of investing in these geographies; some of such models are i) offering a guarantee or political risk insurance cover to investors, ii) use of instruments such as mezzanine debt and returnable grant iii) providing concessional capital to financial institutions that provide credit to MSMEs and, iv) offering technical assistance to enterprises to build investable pipeline. Direct investments to sectors that can support private sector growth such as Information Communication Technologies (ICT), power, road and other transport, and Digital Financial Services (DFS) is another indirect way of promoting the private sector in these countries. Intellecap in the study discusses three models that can work in Somalia given the context. These are a) Diaspora Bond, b) Outcome-based financing, c) Guarantee backed blended debt fund.

Proposed Model	Description	Pros	Cons	Examples
Diaspora Bond	*Diaspora purchases bonds for investing in the home country. These bonds can be sold at a premium and can be raised for a longer duration*	*Large diaspora sending in more than USD 1.4 billion in remittances (2018)*	*Limited success in fragile and conflict affected countries across the globe*	*Kenya, Senegal, Ghana, Nigeria, and Rwanda have all issued diaspora bonds*
Outcome-Based Financing	*Funding is based on certain pre-agreed milestones*	*Investors are assured of the progress of the enterprise/ initiative*	*Lengthy and laborious process which involves constant presence on the ground*	*Outcome Based Financing for Educate girls campaign in India*
Guarantee Backed Blended Debt Fund	*Combines capital from various sources including grant, equity, and debt sources. The capital is backed by guarantees from donors, corporates, foundations and others*	*Low-cost debt available to impact enterprises*	*Structuring of the fund is a complex process and needs approval of many stakeholders*	*IIX Women's livelihood bond with DCA and DFAT as the guarantee providers*

While these models might face some limitations such as limited usage across the globe, complex structuring, high cost of implementation, and legal and regulatory challenges, the recommended models overcome the common obstacles for both investors and enterprises. Few of the critical success factors for these models would include policy advocacy, having competent and skilled on-ground implementation team, and developing effective monitoring and evaluation mechanisms.

BACKGROUND AND MOTIVATION OF RESEARCH

To showcase business and investment opportunities in fragile countries, there is a need to bridge the knowledge gap & create an opportunity mapping. There is still very limited information available on the social entrepreneurship ecosystems in fragile countries. More so, in-depth mappings on the various sectors and stakeholders involved are almost non-existent. Through the provision of key data points and insights, this can shed light on the investment opportunities in these countries. Although private sector investments are currently low, their economies are growing and ripe for anyone willing to take the risk to invest. Data aggregation and digitization can go a long way in bridging the information gap and make it easier to create beneficial interventions in these countries.

This research report seeks to provide insights into the current state of the impact investing and entrepreneurship ecosystem in Somalia and recommendations on impact investment models and ecosystem building strategies to build a resilient and inclusive private sector in Somalia. The report maps the activities by a diverse pool of impact investors across Somalia and highlights opportunities to increase the impact of capital flowing into the private sector. It also provides an assessment of the stakeholders requiring social capital, such as social enterprises, and the ecosystem enablers in the social investment sector. The report is part of a series of three reports, where the other two reports focus on other fragile and transition countries in Africa i.e. Sierra Leone and Mozambique.

REPORT STRUCTURE

The report is organised in six chapters. In Chapter 1, the report introduces the reader the context of Somalia's economy in regards to fragility and conflict. Chapter 2 provides an overview of the private sector in Somalia and its relevance for the growth of the country. The findings and case studies from the social enterprises are laid out in Chapter 3. An in-depth examination of the different categories of impact investors active in the region, and their investment strategies and trends are provided in Chapter 4. An assessment of the enabling ecosystem, including regulation and business support services, is provided in Chapter 5. And finally, Chapter 6 provides recommendations and three innovative impact models that can promote resilient and inclusive private sector in Somalia.

RESEARCH METHODOLOGY (DATA COLLECTION & ANALYSIS)

The report presents both qualitative and quantitative insights generated from secondary and primary research sources. The study leveraged concurrent triangulation, which is a mixed-method approach involving a collection of qualitative and quantitative information from structured interviews and ongoing secondary research.

a) Selection of three fragile countries for research - The research team established a 'selection framework' to identify three fragile economies that will be focused on in this study. The team followed a mix of quantitative and qualitative approaches to identify the target countries for the study. The process began with data collection on various parameters for all 54 countries across Africa. The countries were then filtered and selected based on parameters, including GDP per capita, fragility, and domestic credit to the private sector.

- The first filter in the selection framework included 'GDP per capita'; the countries were arranged as per their GDP per capita. It helped the team to arrive at a list of top economically weak countries from the continent.

- The second filter used was the 'Fragility ranking (OECD)' to identify the countries based on their fragility degree. The OECD index is a combination of each country's political, societal, economic, environmental, and security situation.

- The third filter applied to the remaining countries was of the 'domestic credit to the private sector' (as a percentage of GDP). This parameter highlighted the amount of credit available for the private sector. Domestic credit to the private sector refers to financial resources provided to the private sector by financial entities through loans, equities, trade credits, and accounts receivables. It is crucial for developing the private sector as a lack of financing is often cited as a significant challenge in the ease of doing business in each country.

- The final filtration criteria were a qualitative determination, including the level of impact enterprise activity and the need to develop the country's private sector.

Using the above selection framework, the team selected Somalia, Sierra Leone, and Mozambique as three focus countries for this research.

b) Literature review/Desktop Research - Secondary research was undertaken at the onset of the research to (i) provide an understanding of the macroeconomic and demographic context of the focus countries and identify key development gaps/challenges facing these countries, (ii) evaluate existing research on the impact investment industry and outline key research gaps, (iii) demand-side research on the prevalence of entrepreneurs, presence of formal versus informal businesses, women-owned enterprises, gaps in access to capital, and indicators of 'need' (ecosystem support, infrastructure, supportive policies, etc.) and, finally (iv) compile a list of active players in the supply, demand and ecosystem level to be engaged for primary research. The data gathered helped shape the primary research tools e.g., questionnaires and discussion guides. The team also developed ethical and security protocols for the fieldwork in each of the selected countries.

c) Stakeholder interviews - Existing work was cross-referenced with primary research to corroborate findings, identify opportunities to ask more profound questions during interviews, or both. The report relies heavily on insights from one-on-one interviews conducted with 48 stakeholders in the country, including impact investors such as DFIs, foundations, donors, and impact investors; demand-side players including the private sector and social enterprises; and ecosystem enablers such as incubators, accelerators, professional service providers/firms, research and academia. These interviews aimed to collect quantitative (investment activity data) and qualitative information on investment deployment strategies of different investors, partnerships established, key challenges facing the investors, and their perception of the country. Further, interviews with the demand side players were conducted to identify critical financial and non-financial needs, while interviews with ecosystem enablers provided insights on the type of support offered to the sector and key gaps in organizational support. Annexure I present a full list of stakeholder interviewed from Somalia. While the team spoke to most of the investors, donors and ecosystem enablers active in the country, it selected 30 enterprises to be part of the research. These enterprises were selected from various impact sectors, including agriculture, clean energy, healthcare, financial inclusion, etc. Special attention was paid for enterprise selection, ensuring selected enterprises are of different sizes, providing different type of services, operating across various regions of the country and having women representation in the leadership, to include diverse set of enterprises which are representative to great extent of the private sector in Somalia and provide an understanding of the overall ecosystem in the country.

d) Impact investment deal mapping- To collect data for the impact investment deals in the country, the research team examined publicly available information, evaluated investor websites, and reviewed press releases. Throughout the report, the research team incorporated highlights from its desk research to complement primary findings.

The research team synthesized all the information gathered through desktop research and primary interviews to derive country-level insights presented in this report. The research team will like to emphasize that while the data collected is non-exhaustive, it sufficiently provides directional guidance for the trends reported in this section.

01

CONTEXT TO SOMALIA'S ECONOMY – THE FRAGILITY AND CONFLICT

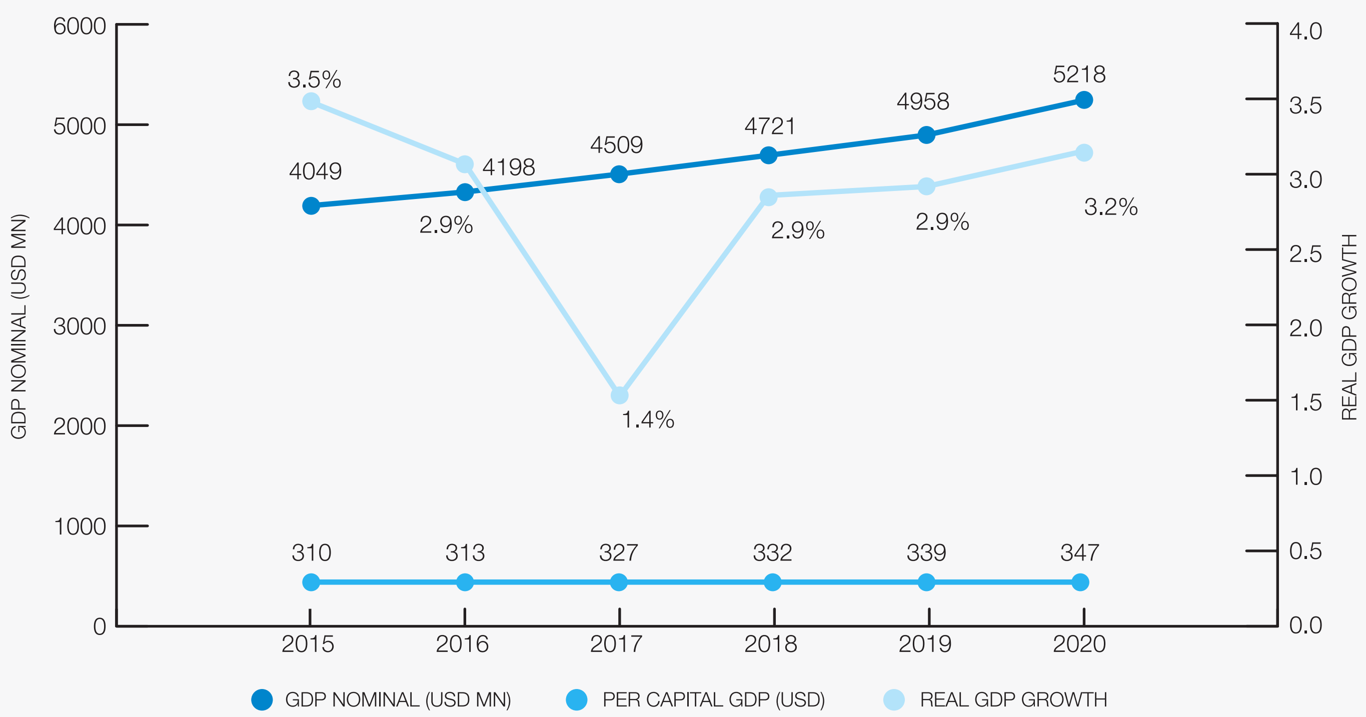
Somalia has made substantial progress in the last five years (2015 – 2020) to lay the foundations for stability and progress in the future. The long civil war (1991 – 2012) devastated the country's economy, infrastructure, and public institutions. However, in the last decade, the country has started to see a sustained political, economic, social, and security-related progress. Despite the progress made, an estimated 69 percent of the 14 million population was deemed inadequate in 2017[1] - the sixth highest globally. Many Somalis have become refugees in other countries due to the conflict conditions prevalent in some parts of the country. United Nations High Commissioner for Refugees (UNHCR) estimated that as of 2019, 2.6 million people were internally displaced, and an additional 820,000[2] live in neighbouring countries, making them one of the world's largest refugee populations.

80%
of entire somali population are vulnerable to external shocks such as natural disasters, conflicts, and economic disruptions

Somalia faces daunting economic challenges coupled with low economic growth and high dependence on remittances. With an estimated per capita Gross Domestic Product (GDP) of USD 327 in 2017, Somalia remains one of the world's poorest countries. The economy has grown at a moderate pace, averaging 2.5 percent (real GDP growth between 2013 and 2017). The economy was also severely affected by the 2016-17 drought, which led to considerable losses in crop production and livestock, reducing GDP growth. Domestic consumption enabled by large remittance is the primary growth driver in the country. The diaspora's remittances help household consumption at 132 percent of GDP and represent a vital income component for the bottom 40 percent of households[3]. This high level of dependence has caused a short-term setback to many households as remittance incomes have been hugely hit with the advent of the Coronavirus pandemic globally, leading to a 40 percent decrease in remittance income (estimates of the Federal Government of Somalia)[4].

An estimated USD 1.38 billion was sent by the diaspora in 2018 which accounted for almost a third of the total GDP of the country.

Figure 1: GDP of Somalia

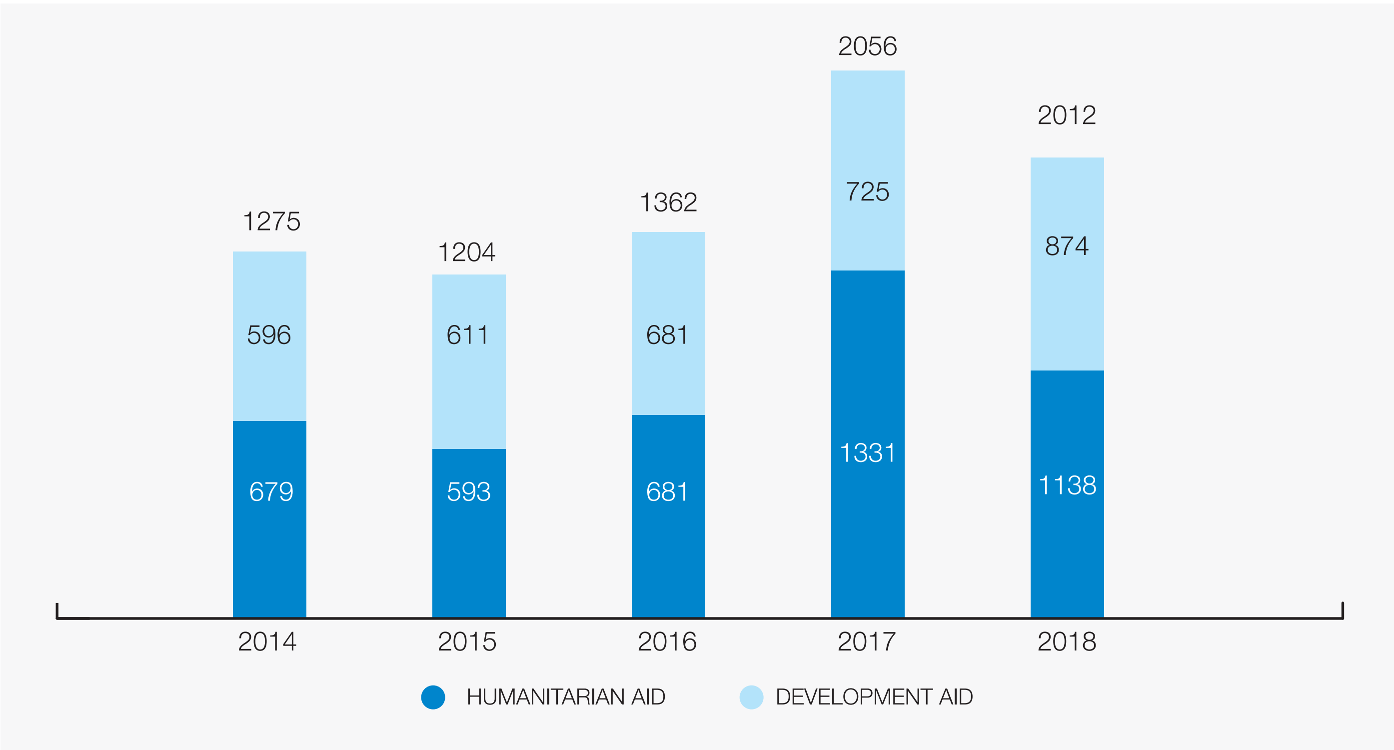


Source: World Bank

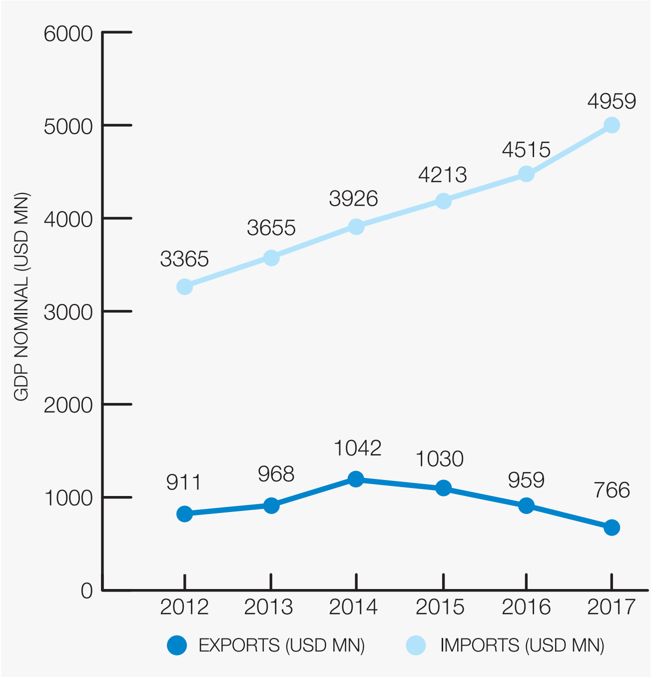
In addition to diaspora remittances, foreign aid has also contributed significantly to the growth of Somalia's economy in the last decade. Somalia is one of the largest recipients of foreign assistance. The country received more than USD 2 billion in Official Development Assistance (ODA)[6] in 2017 and 2018 - a 57% increase compared to the previous five years levels (2012 – 16). ODA forms more than 27% of Somalia's GDP, making it highly dependent on foreign aid[7]. European Union, United Kingdom (UK), and Germany were the most prominent development aid providers in 2018, accounting for more than 50% of the total development aid. The United States of America (USA) and the UK were the most significant humanitarian assistance providers, amounting to more than 55% of the total humanitarian aid. The sudden surge in humanitarian assistance in 2017 was primarily for drought relief in the country and had likely played a key role in averting famine. The high level of dependence on aid is due to the government's relatively small tax revenues. ***The domestic revenue for the Federal Government of Somalia is USD 184 million in 2018[8] compared to an ODA of USD 2.2 billion.*** Apart from the ODA, international donor partners also spent more than USD 1.5 billion per year[9] on peacekeeping, counterinsurgency, and maintaining security in the country[10].

Table 1: Official Development Assistance for Somalia (USD Mn)[11]

2014	2015	2016	2017	2018
Largest Humanitarian Aid Donors				
USA: 249 Mn	**USA: 221 Mn**	**USA: 131 Mn**	**USA: 368 Mn**	**USA: 437 Mn**
UK: 59 Mn	**UK: 61 Mn**	**UK: 104 Mn**	**UK: 232 Mn**	**UK: 189 Mn**
Largest Development Aid Donors				
Turkey: 109 Mn	**EU: 227 Mn**	**EU: 214 Mn**	**EU: 175 Mn**	**EU: 233 Mn**
UK: 97 Mn	**UK: 130 Mn**	**UK: 95 Mn**	**Germany: 117 Mn**	**UK: 125 Mn**

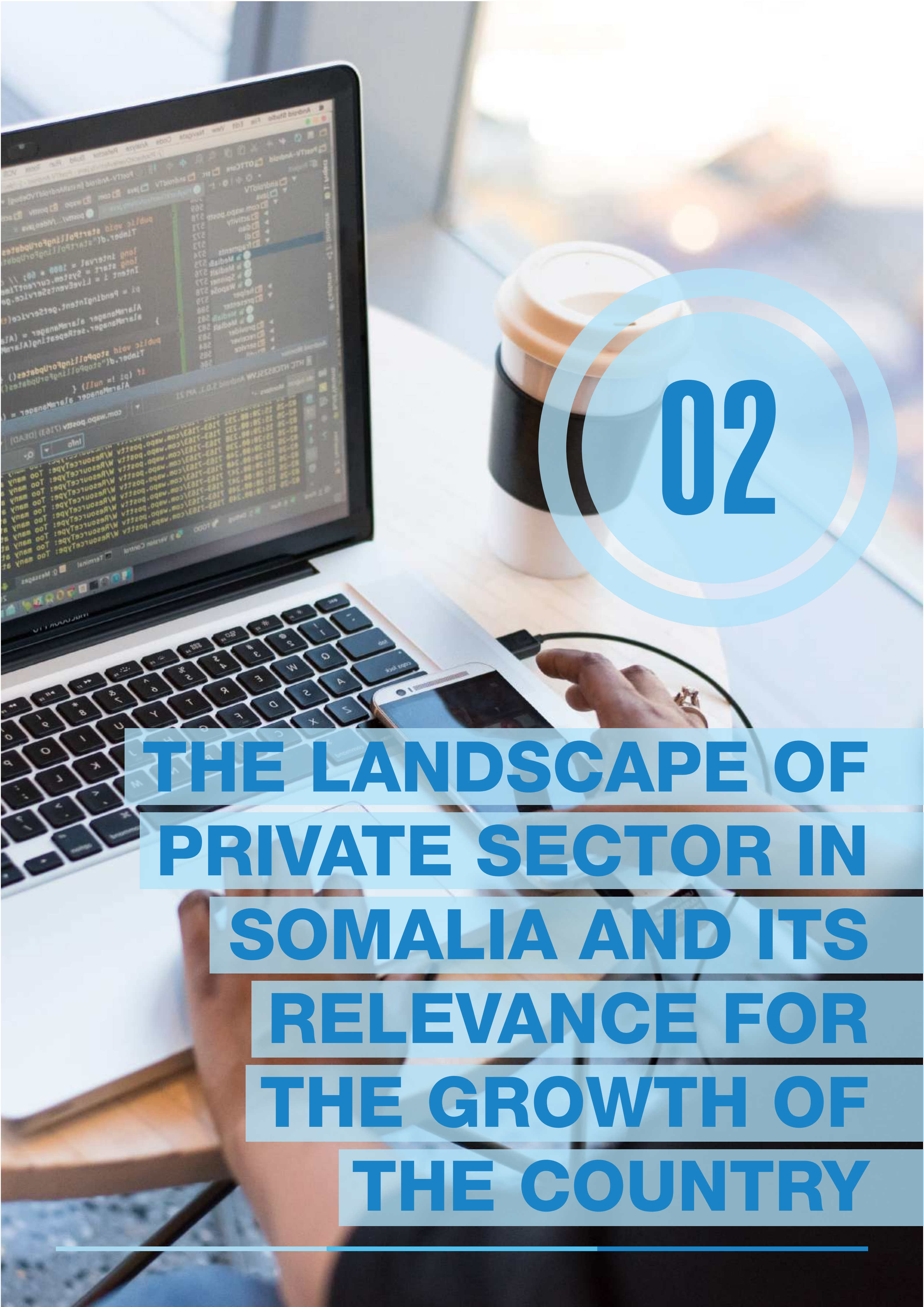


Somalia has a large trade imbalance as the country is highly dependent on imports, which account for two-thirds of GDP. In 2017, the trade deficit rose by 18% as exports fell and imports increased due to severe drought conditions. It was partly due to a significant decrease in livestock export, which otherwise accounts for more than 70 percent of the country's export earnings. Remittances and donors' flow mainly finance the trade deficit, but it needs to be reduced for the economy to sustain itself. The current Covid-19 crisis has severely impaired the remittance inflow, which is expected to lead to a more significant trade deficit.



Somalia fares poorly on most Sustainable Development Goals (SDGs) and has one of the world's lowest social indicators. Education access is deficient, with only 33 percent of children between ages 6-13 enrolled in primary schools (2019). It is extremely low even compared to other low-income countries within Sub-Saharan Africa, which had an average enrolment of 74 percent (2019)[12]. Health indicators are also among the lowest globally, with the country having one of the world's highest malnutrition levels. While the overall level of acute malnutrition has improved over the years, it still hovers at the severe phase, with a Global Acute Malnutrition (GAM) median of 14 percent[13]. Over 90 percent of births occur at home, and a skilled birth attendant attends only 33 percent of those. It results in one of the highest mortality rates for children under five years - 117 per 1000 live births in 2019[14]. The country also has low access to sanitation, with only 50% of the households having access to sanitation[15]. Poor access to water and sanitation facilities increases the risk of contracting preventable diseases such as diarrhoea, cholera, and respiratory infections. Over 900 people have died from cholera in the last three years (2017-2019), with most children under the age of five[16]. The Federal Government of Somalia has launched various programs and policy initiatives such as The Education sector plan (2018 – 2020), the National Development Plan (2020 – 2024), the National Education Curriculum framework, and others to improve its social indicators. International bilateral and multilateral partners, including DFIs, donors, and other foundations, have also stepped up their efforts to contribute to the country's growth.

Given Somalia's fragile context, it is widely believed that various international stakeholders jointly with the country's private sector have a crucial role to play in rebuilding the economy. Somalia's government has also recognised the fact and has partnered with various international institutions to prioritise the private sector's development to reduce poverty.



02

THE LANDSCAPE OF PRIVATE SECTOR IN SOMALIA AND ITS RELEVANCE FOR THE GROWTH OF THE COUNTRY

Somalia has a labour force participation rate of 66 percent (2014)[17], which is relatively high in comparison to similar countries that have experienced civil war, such as Afghanistan (51 percent, 2014 and 47 percent, 2017) and Yemen (26 percent, 2014)[18]. The female labour force participation is only half of the males, primarily due to society's patriarchal nature[19]. Somalia has one of the highest unemployment rates globally, with the youth unemployment in Somalia is at 68 percent (2017)[20]. Due to the country's high unemployment rates, remittances and humanitarian aid remain insufficient to develop sustainable livelihoods. In this context, private sector development is one of the priority areas for the Federal Government of Somalia and the international community.

Private sector can help break the cycle of fragility, conflict, violence, and poverty in Somalia. It is seen that private sector's growth can substantially reduce the economic barriers in fragile countries, subsequently leading to a reduction in conflict and violence. The private sector's growth can also reduce poverty and mitigate political, social, and economic vulnerabilities.

The private sector landscape in Somalia is still in its nascent stages. Most of the Small and Medium Enterprises (SMEs) in the country are in the Services sector, while the bulk of micro-enterprises represent the domestic trade sector[21]. Most of the businesses are established through bootstrapping and funds from friends and family. ***This is primarily due to a lack of access to finance in the domestic market - the domestic credit to the private sector (as a percentage of GDP) is 7.5 percent (2017)[22], which is one of the lowest in Sub-Saharan Africa.*** Many of these enterprises grow by investing their profits back into the business and not leveraging credit from financial institutions. The private sector in the country is primarily informal, making market-based financial intermediation challenging, especially in critical sectors of agriculture, livestock, and fisheries.

Figure 2: Advantages of a coherent Private Sector in Somalia

Lack of regular income often encourages individuals to choose a path of violence and conflict. Private sector can provide jobs, engagements, and contracts required to increase the income levels of individuals and society at large. The increase in income often discourages individuals from engaging in conflict and violence.

Private sector provides much needed goods and commodities to communities affected by conflict and violence in Somalia.

Private sector also contributes to building trust between various sections of society which are inter-dependent on each other including the government, markets, financial institutions among others. This interdependence prohibits conflict as every stakeholder stands to lose in case of outbreak of violence

Growth in Private sector also contributes to the overall development of the economy. The sector can also contribute directly through social programs, and work with various government bodies to enhance the investment climate in the country.

Private sector can play a huge part in developing parts of the infrastructure, enhancing connectivity and economic progress.

Discussed below are some of the country's critical impact sectors and the business activity in these sectors :

AGRICULTURE

Agriculture and livestock remain the backbone of the country's economy. The agriculture sector (including livestock) accounts for the largest share of GDP. Agriculture contributed to more than 72 percent[23] of GDP in 2016. Within agriculture, livestock was the major contributor, with over 83 percent (2016)[24] share. Agricultural exports constituted 93 percent of total exports in the early 2010s, primarily driven by the export of livestock, and reached more than USD 634 million in 2015. The vegetable and fruit export is only 20 percent (2015)[25] of the pre-civil war level. The slow growth can be attributed to long conflict and resulting insecurity, displacement of a large proportion of the rural population, dilapidated irrigation infrastructure due to collapse of state-run maintenance services, and effects of droughts and floods linked to climate change. As a result of these factors, many farmers have started to favour livestock rearing over crop production, increasing agricultural contribution to GDP. Livestock and livestock products alone provide 77 percent (2015) of total exports by value and are an essential source of livelihood for many of the country's population. Livestock exports fell in 2017 due to the prolonged drought and a renewed import ban by Saudi Arabia, the largest importer of Somalia's livestock products.

FINANCIAL SERVICES

Somalia's financial services sector is still in its nascent stages, with the formal sector serving only around 7 percent (2018)[26] of the credit demand. Somalia had five banks and 11 Money Transfer Businesses (MTBs) as of January 2019, with Dahabshiil Bank and Salaam Bank being the largest banks. Most of the banks' branches are only present in the urban areas, and only a few offer ATM and credit card services. Only 39 percent of individuals over the age of 15 have a bank account in Somalia[27]. The current lending is also heavily focused on short-term trade financing, which leads to significant unmet demand for finance. However, bank deposits have tripled from 2014 to 2018, indicating increasing confidence in the formal financial institutions. ***Remittance companies (MTBs), which have good geographic coverage across Somalia and Somaliland, fulfil some of the country's critical financial service gaps.*** Taaj Remittances (owned by Hormuud Telecom), Dahabshiil Remittances, Jubba Express, and Tawakkal Express are among the largest MTBs in Somalia and Somaliland. These MTBs mainly deal in international remittances as mobile money services have largely taken over domestic money transfer business. Somalia's economy is heavily dollarized (in both banking and mobile money systems) - a significant factor resulting in disparities in financial access and opportunities for a large section of the population. Only a few individuals in urban areas have access to dollars and can purchase essential goods that are mostly imported. ***The Central Bank of Somalia (CBS) has not issued a legal tender, i.e., Somalia banknotes, since 1991. International Monetary Fund (IMF) estimates that almost all of the current banknotes in circulation are counterfeit.*** The absence of a legitimate national currency creates difficulties for the poorer households who do not earn income in dollars or other hard currency (except for the 15-20 percent who receive remittances and those working in the formal service sector)[28]. The Central Bank of Somalia has limited to no monetary instruments to regulate the national currency and inflation due to the economy's heavy dollarisation. Because of this lack of national currency, the country's base of the pyramid population is adversely affected. However, the Central Bank is currently working with the World Bank to issue a new national currency to stem this systemic issue.

TELECOMMUNICATION AND ICT

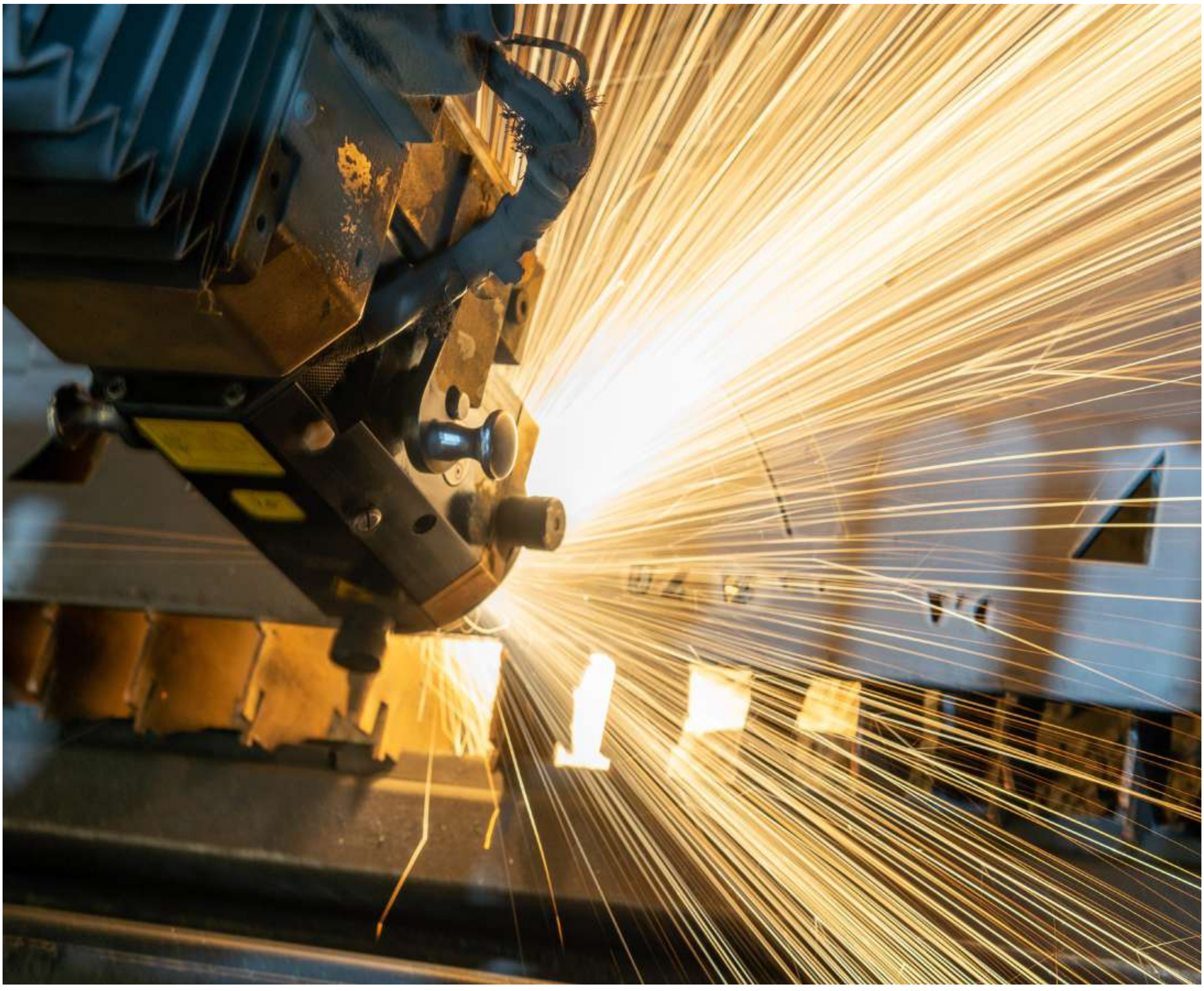
The telecommunication and Information and Communications Technology (ICT) sector is among the largest sectors in Somalia. The telecom and internet sector comprises five major operators: Hormud, Somtel, Golis, Telesom, and NationLink. Somalia had 51 mobile subscriptions per 100 people in 2018 - a considerable increase from 2010 when the country only had 5.4 subscriptions per 100 people[29]. The sector is one of the country's largest employers, with over 25,000 individuals employed (2019)[30] in the sector. The sector has been the driving force that propelled Somalia's economy and has contributed to its growth through mobile money services, remittances, payment of bills, and other services. The Government of Somalia has also come up with a National ICT policy and strategy that aims to ensure the development of ICT infrastructure that supports expanded connectivity to attract investment and promote employment opportunities.

MANUFACTURING

Manufacturing has been one of the hardest-hit sectors during the conflict years. Manufacturing contributes 10 percent (2018)[31] to the overall GDP of the country. The sector has been one of the most affected since the civil war broke out in 1991. During the war, most manufacturing units were closed down, infrastructure was destroyed, and many factories were looted, resulting in enormous losses for the sector. The sector continues to remain sluggish amidst a difficult security situation coupled with limited infrastructure. However, over the years, some small-scale manufacturing units have been established in the urban areas of Mogadishu, Hargeisa, Bosaso, Kismayo, and others. These manufacturing units primarily belong to fish-canning, meat processing, mineral water, and stone processing. The sector faces many challenges, including a lack of a supportive regulatory environment with significant licensing delays, lack of technical skills and human resources, lack of regulatory standards, and lack of business financing. ***Somalia has one of the most expensive electricity rates globally, ranging from 50 cents to USD 1.25 per kWh in comparison to USD 0.15 – 0.2 cents per kWh in Kenya and 0.6 cents per kWh in Ethiopia***[32]***.*** It is one of the major bottlenecks for the country's manufacturing industry's growth as it has to compete with cheaper goods imported from other countries. These factors have contributed to a decline in manufacturing and have subsequently increased imports and trade deficit.

The Federal Government of Somalia has initiated various steps to improve the manufacturing sector in the country. Some of these initiatives include:

- Development of industrial hubs along the trade corridors
- Building technical skills necessary to support growth, including vocational training, with a particular emphasis on the inclusion of women, young people, and displaced persons
- Embed manufacturing into the Somalia Power Plan to address energy constraint
- Improve investment in the sector through Somalia Investment Promotion Office (SOMINVEST)



03

THE LANDSCAPE OF SOCIAL ENTERPRISES IN SOMALIA

As per the recent World Bank Enterprise survey (2019) for Somalia, most enterprises operate in the retail and restaurant sector. More than 50 percent of the enterprises owned the entire business without any external partners. Somali nationals living abroad owned less than 8 percent of the enterprises, and more than 16 percent had female ownership. More than 82 percent of enterprises consider insecurity, fire, and natural disasters to be the business's biggest threats. Access to finance was mainly through personal contribution and contribution from friends and family. The survey also stated that more than 80 percent of enterprises did not approach a bank or financial institution for a loan[33].

Social Entrepreneurship is a nascent concept in Somalia that has been seeded by the efforts of DFIs and donors active in the country. Traditionally, many enterprises focused on trading (importing goods to satisfy local demand), retail, hospitality, and real estate. The majority of the individuals relied on subsistence agriculture and fishing for meeting their daily needs. Over the years, entrepreneurs have realised social entrepreneurship's potential, specifically in fisheries, renewable energy, healthcare, and agriculture. Due to the heavy interest of donors and DFI programs in the sectors and the great potential of growth in these sectors, entrepreneurs can also receive technical and financial assistance, which helps in their journey.

The chapter covers the Social Enterprise landscape in Somalia and analyses emerging business models in the country – categorised under access, ability, and network and knowledge levers based on their product/service offering. The section also covers detailed case studies of few impact enterprises and demand-side challenges of attracting impact capital. The insights and learnings presented in the section are based on secondary research and discussions with around 30 social enterprises from various regions (rural and urban) in Somalia, across multiple sectors and sizes.

CHARACTERISTICS OF THE SOCIAL ENTERPRISES THAT PARTICIPATED IN THE STUDY

This study examined 30 social enterprises across various regions of Somalia. The study selected these enterprises from multiple impact sectors, including agriculture, agro-processing, healthcare, fisheries, information technology, energy. Female ownership and leadership were also considered critical factors while selecting enterprises for the study. The research focused on analysing enterprises' operations in Somalia with respect to their reach, business models, access to finance, scale, profitability, business process innovation, marketing strategies, etc. The study helps understand the growth trajectory, financial progress, and impact created by social enterprises and how they play a critical role in developing a resilient and inclusive private sector in Somalia. The study of social enterprises is also essential to determine the progress of developmental programs within the country.

Figure 3: Key characteristics of enterprises included in the study[34]

General Characteristics	Financial Parameters	Challenges	Others
• Many of the enterprises are at pilot and growth stage • They belong to agriculture and agro-processing industries • Majority of enterprises have less than 10 employees	• Debt is the number one priority for many enterprises • They have raised initial capital from friends and family • Many of the enterprises are profitable	• Access to finance, Lack of quality labour, and availability of infrastructure are major challenges • Security is not a major challenge for the interviewed enterprises	• Financial training and capacity building are the major requirements • Social media is the number one source of information on funding opportunities • Have a B2C distribution model and operate regionally

The majority of the enterprises in Somalia are micro-enterprises, which also reflects this study's sample. Most enterprises interviewed as part of the study were micro-enterprises and had less than ten employees. Only 25 percent of the interviewed enterprises, majorly belonging to financial services and agro-processing industries, had more than ten employees. A large proportion of the enterprises interviewed are individual and family-owned and operate locally within one country's region. More than 75 percent of enterprises were operational for less than five years and were in the initial growth stages.

Women play a pivotal role in driving social entrepreneurship in the country. Almost 50 percent of the enterprises interviewed have women as founders/co-founders. Additionally, women also constituted more than 35 percent of employees in these interviewed enterprises. The team ensured to include women-owned or women-managed enterprises as part of the study. The study also identified and analysed differences in challenges and support available to these women enterprises. Most women at interviewed enterprises were involved in administration, finance, customer care, and ancillary activities. It also observed that sectors such as manufacturing and fisheries are male-dominated and have the minimum female employment in the country.

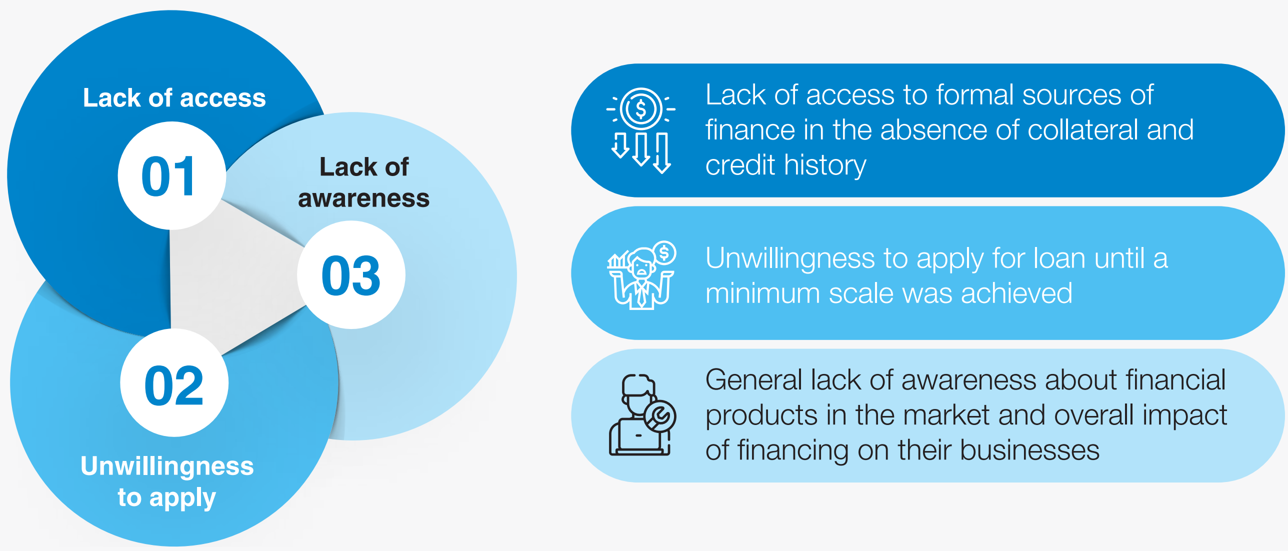
The majority of the interviewed enterprises are profitable and have experienced an increase in revenue over the years. These enterprises re-invested their profits for business expansion but are facing operational and financial difficulties due to the outbreak of Covid-19. ***Informal financing, which is the primary source of enterprise financing in the country, has decreased due to the outbreak of Covid-19, as many funders are cautious about lending in these uncertain times.*** The decrease in income from remittances has also resulted in a reduction in financing. As a result, many of these enterprises have reported a decline in their revenues in the past year.

More than half of the enterprises interviewed stated to receive information on funding sources through either social media or through word of mouth and from incubators/accelerators. Enterprises, such as Shaqadoon, provide access to funding opportunities to other social enterprises by aggregating funding from HNIs, diaspora, and other interested funders. Some of these platforms, such as Bulshokaab, help communities raise money through crowdfunding. Some incubators and accelerators such as Tethered Up, Harhub, and others connect enterprises to angel investors for fundraising and potential partners who can help expand their business locally and internationally.

More than 90 percent of the enterprises interviewed have indicated that they have grown organically after the initial investment round but would greatly appreciate more investments for faster growth. Only a few enterprises have received debt funding from impact funds in the country but had to hire expensive consultants to build the financial model, investor memorandum, and other necessary documents. Enterprises often are not willing to take a chance on spending money on consultants upfront while not having a guarantee of investment. As a result, most enterprises depend on informal funding sources, including diaspora and local money lenders.

Equity financing is still a nascent concept across the country, with less than 10 percent of interviewed enterprises having raised funding through the equity route. It is also because Somalia is still seen as a fragile country by many equity investors, coupled with the requirements of investing through Islamic financing.

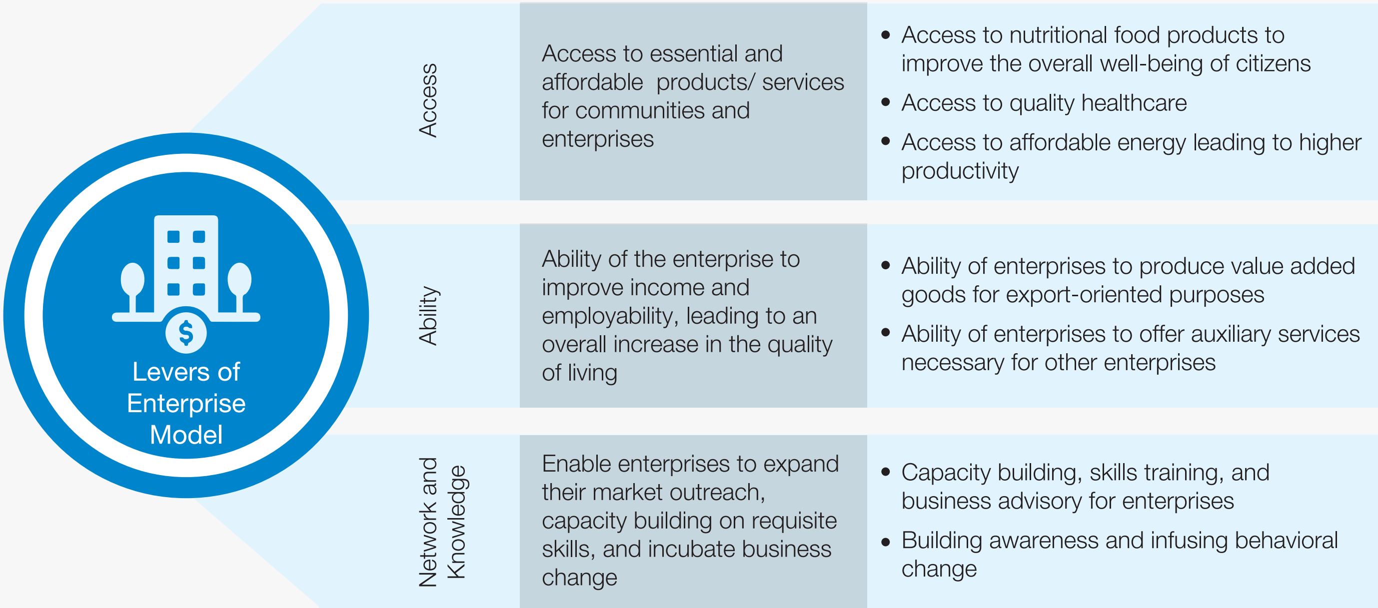
Figure 4: Major reasons cited by entrepreneurs for not raising finance include



DEEP-DIVE INTO SOCIAL ENTERPRISE MODELS IN SOMALIA

The enterprises interviewed as part of the study are analysed based on their approach to solving the country's social and development challenges, including a) Enabling access, b) Improving ability, and c) Facilitating networks and knowledge as described in the figure below.

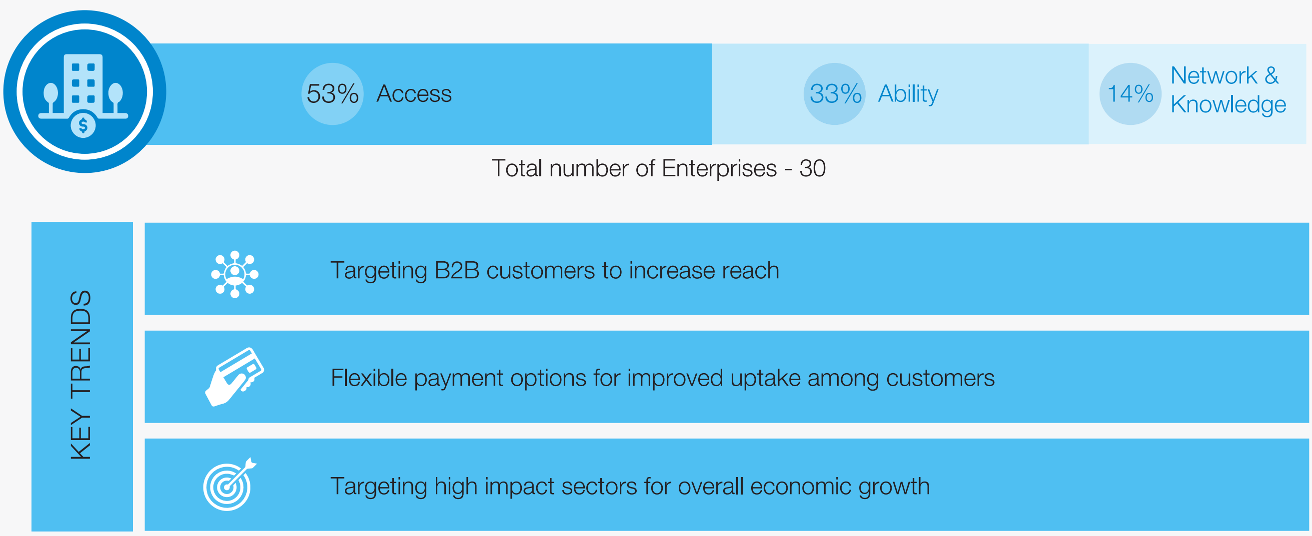
Figure 5: Levers of enterprise model in Somalia



1. ACCESS ENTERPRISES

Access to essential goods and services such as food, healthcare services, financial services, and energy is a significant challenge for communities and enterprises alike in Somalia. Many essential goods, such as food items, clothing, and healthcare equipment, are currently imported from other countries. As a result, many enterprises have designed business models that cater to the demand of these imported products and services' while customising the offerings and solutions to the local population's needs and requirements. Almost 16 of the 30 enterprises interviewed as part of this study have business models providing access to essential goods and services to their customer base. The following section provides details of various access enterprise models.

Figure 6: Key trends of Access enterprises in Somalia



ENABLING ACCESS TO NUTRITIONAL FOOD PRODUCTS TO IMPROVE THE OVERALL WELL-BEING OF CITIZENS

More than 69 percent of the people in Somalia live below the international poverty line. Nearly half of the total citizens cannot meet the average food requirements, even if they spend all their income on food[35]. As a result of acute poverty and limited availability of nutritious food, more than 300,000 children under five were acutely malnourished (2017).[36] The rural, nomadic, and internally displaced population(IDPs) remain at risk of falling into acute food insecurity in the absence of proper nutrition. As a result, solving food security challenges is a crucial focus for many impact enterprises in Somalia. Impact enterprises interviewed as part of this study, such as Durdur Onion Production, Abu-Najib Fishing Co, Ilbarqaaqo Milk, Khayria Farm, Mogadishu Fresh Fruits, Somfresh, aim to address the food security challenges by providing quality food products at affordable prices across various locations of the country.

These Access enterprises use various distribution channels, including retailers, distributors, wholesalers, etc. Some enterprises, such as Abu Najib Fishing Co, a fish harvesting and processing entity, want to have a wider customer reach and use an indirect distribution model of partnership with various retailers to sell their products. Others, such as Durdur Onion, providing high quality, nutritious, and healthy onion for Somaliland consumption, sell their products through direct marketing. Ilbarqaaqo Milk uses a hybrid marketing approach where the company uses its vehicle to collect milk from the rural areas and distributes most milk to hotels and restaurants (Business to Business (B2B) distribution). On the other hand, the company also has a retail outlet to sell directly to the end customers (B2C distribution). Some other innovative Access enterprises, such as Ridwa Nutrition Center, cater to the urban population and provide nutrition advice, planning food programs, nutrition screening, and other services. Such enterprises with niche target customer segments often find it challenging to tap into the existing distribution networks due to low product volumes, limited working capital to service orders at scale, and direct customer interaction requirements. As a result, they often engage in door-to-door sales and primarily rely on word-of-mouth publicity for their products.

Most of the interviewed 'access enterprises' deploy traditional production methods, with minimal automation and staff training, resulting in similar product offerings. Moreover, many of these manufacturing enterprises face increased competition from businesses importing the goods and providing similar products at a lower cost. Somali companies find it hard to compete with the businesses importing cheaper goods and are therefore forced to modify their business models constantly. Many such enterprises continuously adapt themselves by using strategies such as (i)exploring more relevant customer segments, (ii) providing commercially unviable services for larger businesses, (iii) using door-to-door marketing to boost brand loyalty and recall, (iv) providing tailor-made products local economy, and (v) providing after-sales support in rural areas. For instance, SOGI Foods Complex produces affordable products tailor-made to the tastes of the local people. It sells Mooshali, a Somali pancake made from different cereals; Basho, a drink made from natural wheat; and Shuuro, made from maize. The company primarily employs a B2B strategy for distributing its products targeting super-stores and grocery shops.

CASE STUDY 1: ABU-NAJIIB FISHING CO

Description:

Abu Najiib Fishing Company is a fish harvesting and processing company established in 2017 in Berbera, Somaliland. The firm fishes out of Berbera and has retail and processing locations in Berbera and Hargeisa. The company started small by selling 2 tons of fish per week but has slowly expanded its operations to sell more than 10 tons per day.

Operating Model:

The company is engaged in harvesting and processing fish for local consumption in Somalia. With only one fishing boat initially, the company started to sell the fish to local retailers as it does not have the scale to operate at the distribution level. It has a network of around 1,300 distributors and retailers across Somalia. The company joined a community fishing cooperative that held collective licensing permission from the Somaliland Ministry of Fishery and Marine Resources and the Berbera Regional Government Authority. It plans on expanding its distribution operations to other cities, including Bosaso, Kismayo, and Mogadishu.

Financial Sustainability:

While the company was bootstrapped at the initial stages, it secured a debt investment from the Shuraako Impact Fund to construct a new processing location in Burao. The investment allowed the company to procure three additional fishing boats and processing equipment for its Berbera, Hargeisa, and recent Burao processing locations.

Challenges:

Lack of government support, poor roads, expensive electricity, expensive rents, and lack of insurance were cited as critical challenges. Covid has had an indirect impact on the sector due to a decrease in remittances. Many people are unable to afford fish, affecting the company's short term growth targets. The company also had to hire expensive consultants to get the documentation ready for the Shuraako investment, which is a significant challenge for many enterprises in the region.

Impact:

The enterprise created more than 42 jobs, including 12 female jobs providing much-needed livelihoods for the local community. It has also set up its training facility to train staff which it plans to expand.

ENABLING ACCESS TO QUALITY HEALTHCARE

***Somalia has one of the lowest health indicators globally, with an infant mortality rate of 132 per 1,000 live births and a maternal mortality rate of 732 per 100,000 live births*[37].** Many parts of the country witness shortage of pharmacy stores and limited availability of quality medicines, along with a lack of diagnostic and laboratory services. Enterprises interviewed as part of this study, such as Kaafi Community Health Center, provide modern laboratory facilities and medical consultancy. Additionally, high-quality drug stores such as European Pharmacy, Polyclinic, and Diabetic Center provide quality and affordable healthcare facilities and medicines to patients in rural and urban areas. Hargeisa Diabetic Center provides patients with diabetic care, along with giving heart and eye checkups. It was the first clinic providing exclusive diabetes treatment in Hargeisa. Oxfam offered technical assistance for the enterprise, followed by USD 6,000 funding.

Most of these enterprises rely on word-of-mouth for marketing, and their customer retention strategy is based on the provision of flexible payment options. For instance, European Pharmacy has a monthly payment option for its vetted clients for the services availed during the year. On the other hand, some innovative enterprises such as OGOW EMR help the healthcare centres in Somalia through integrated electronic medical records and practice management systems specifically designed for hospitals and clinics in Somalia. Enterprises such as European Pharmacy majorly rely on imported medicines from abroad given the weak pharmaceutical supply chain. The drugs are sourced by a single distributor, which distributes the drugs to various pharmacy stores.

CASE STUDY 2: OGOW EMR

Description:

OGOW EMR is an electronic medical record (EMR) and practice management system designed specifically for Somali hospitals. OGOW EMR was one of the top ideas at the Bill and Melinda Gates Foundation (BMGF) innovation challenge and was subsequently connected to Johnson Inc and United Nations Children's Emergency Fund (UNICEF). The company hopes to implement electronic solutions to monitor trends and find disparities in care patterns and outcomes in resource-constrained communities across Somalia.

Operating Model:

The company's portal provides tools for practitioners to improve infant vaccination coverage by reaching patients who need specific vaccines, collecting and managing patient data and administrative processes such as scheduling. All of these services are currently being provided to hospitals in partnership with DFIs and global aid agencies such as world vision, BMGF, UN agencies and others.

Financial Sustainability:

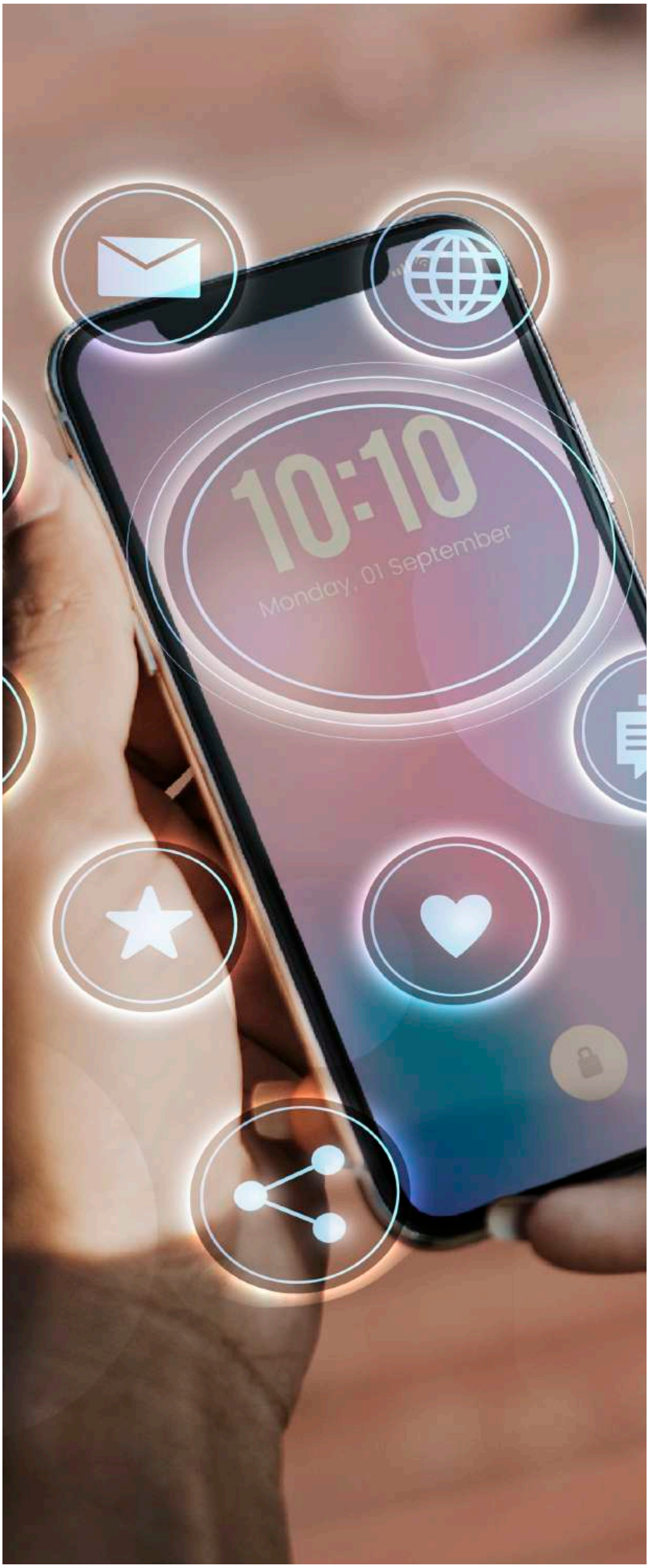
The enterprise had launched a fundraising program in Canada on GoFundMe. The company primarily relies on grant funding for its operations and has not yet reached the planning stage for an investment round.

Challenges:

While the product has many suitors, achieving sustainability has been a challenge as many of the customers are not willing to pay the appropriate price for the product. As a result, the company has to rely on UN agencies and other' grants to support Somalia's healthcare institutions. Healthcare education is also a significant area of improvement in the country, improving the demand for services like OGOW EMR.

Impact:

OGOW EMR provides much-needed information to healthcare providers and caregivers to benefit and empower all Somalis to access community health and primary care services in times of Covid. OGOW EMR has also helped thousands of kids (especially internally displaced kids) get their vaccination on schedule.



ENABLING ACCESS TO ELECTRICITY

Access to affordable and reliable energy sources, particularly electricity, is seen as a significant economic growth driver. Somalia's Ministry of Planning, Investment and Economic Development have estimated electricity access rates at only 15 percent, with rural access limited to just 4 percent[38]. Despite substantial improvements in electricity access in the past five years, Somali businesses face an acute shortage of electricity and often face blackouts for long periods. They thus mainly rely on diesel generators, which increases the cost of electricity manifold. ***Private sector players supply more than 90 percent[39] of electricity in urban and peri-urban areas through diesel-based systems.*** Private sector enterprises such as Solargen supply energy to individuals and businesses through mini-grid networks and provide water for irrigation through solar pumps. Due to the lack of a physical national power grid in Somalia, many households use local grids or off-grid solar systems. As a result, more than 100,000 – 150,000 off-grid solar products are sold annually[40]. While Development Finance Institutions such as FCDO, European Union, IFC are the significant source of funding for energy enterprises, few such as Solargen were able to raise funding from seed investors and expanded through debt from financial institutions (Islamic Finance).

CASE STUDY 3: SOLARGEN

Description:

Solargen is an energy, water, and irrigation solution and service provider in Somalia. It started operations in 2012. The company provides solar mini-grids, solar water pumping solutions, solar water treatment systems, and solar cold chains.

Operating Model:

Solargen has a build, operate, transfer model where it operates the mini-grid that it constructs for a fixed period (such as two years for the 48 kW system in Warsheikh). The ownership is transferred to the community-owned utility organisation post the agreed time. While most private electricity enterprises in Somalia use to estimate most customers' power usage and fix a price for households based on the number of lights or appliances present, Solargen has started installing smart meters for an accurate reading.

Financial Sustainability:

The company had its first installation in 2013 and raised a USD 500,000 seed funding from the Somalia Stability Fund. The funding included a grant of USD 100,000 and a debt of USD 400,000. The company's revenues have grown more than 250 times in the last ten years and has been profitable from the first year. It had recently raised a further USD 600,000 from the SIMA fund in 2019. All of its funds are in the form of Sharia complaint debt.

Challenges:

Bureaucracy and lack of international payment systems are significant challenges for Solargen. The company has to use its Kenyan entity to streamline the procurement process, financial payments to equipment suppliers, and facilitate investor interactions as most of the companies clientele are international donors.

Impact:

Solargen has installed more than 5 MW of solar capacity, 250 borewells, has helped irrigate more than 1400 acreages, served more than 750000 people, and saved more than 18220 tons of CO2.

2. ABILITY ENTERPRISES

Ability enterprises in Somalia have developed innovative solutions that improve the base of the pyramid population's income levels, subsequently improving their purchasing power parity. These enterprises improve people's employability and the community's livelihoods by implementing innovative enterprise models. About 10 of the 30 enterprises interviewed as part of this study provide or expected to provide Ability related services to their target customer base.

Figure 7: Key trends of Ability enterprises in Somalia

ABILITY ENTERPRISES PRODUCING VALUE-ADDED GOODS FOR EXPORT PURPOSES

Most Somali enterprises export agricultural produce as raw materials, with only a few of them doing any value addition. However, enterprises such as Aragsan Organics (which produces natural and organic cosmetics) are doing value-addition and exporting its value-added products to Ethiopia, creating employment in a new sector, i.e., organic cosmetics. Covid-19 has severely impacted enterprises such as Aragsan Organics as it relies on its customers' discretionary spending. The company markets its products through social networking sites and primarily depends on word of mouth to expand its reach. Enterprises such as Taam fishing have contracts with other fishermen in the region for purchasing their catch, which is then processed and exported to Jordan, Malaysia, and China.

CASE STUDY 4: TAAM FISHING

Description:

Taam fishing was started in 2017 by an entrepreneur with no prior experience in fisheries and agriculture. After conducting background research in Turkey, Sri Lanka, Indonesia, and Mauritania, the entrepreneur formed Somalia International Fishing in 2017, which was ultimately unsuccessful due to lack of funding and experience. Taam fishing was later formed and started exporting live lobsters to Kenya and Hong-kong.

Operating Model:

The company currently operates in Mogadishu and have a processing centre (on lease). The produce is exported to Jordan, Malaysia, and China. The company has contracted fishermen (40 boats) to buy their catch, process the product, and then sell it abroad. The company employs 25 people at its processing facility and has two transport boats to transport the produce. The company is looking at boat manufacturing, increasing the size of its processing facility, establishing a manufacturing facility for logistic material, and establishing a training institute for the fisherman in the region.

Financial Sustainability:

The company is funded by Taam Petroleum, which owns five petrol stations in Somalia and South Sudan. The company is currently looking for joint ventures for leasing fishing boats. The company has decent revenues during the three months of March, April, and May 2020 and aims to achieve 3X revenues in the next season (August to January).

Challenges:

Transfer of money is a critical challenge for the enterprise as it receives most of its payments from abroad. It takes a lot of time as some banks do not have a corresponding bank in the country of operations. While there is a lot of opportunity for the fishing industry in Somalia, funding is a significant challenge.

Impact:

The company employs more than 25 people at its processing facility, and 14 people are employed on the fishing boats. The company has also provided purchase guarantees to more than 40 boats providing them with sustained income.

Some innovative Ability enterprises are developing solutions that will significantly help the farmers in Somalia from the adverse effects of severe drought conditions. Enterprises such as Afri-tech manufacture organic fertilisers, which is an innovative concept for the Somali agricultural community. The enterprise is in the pilot stage and is currently testing the acceptance of its solution in rural communities.

CASE STUDY 5: AFRI-TECH

Description:

Afri-Tech is a small manufacturing enterprise that produces agricultural organic fertilisers, technology devices, modern nursery. The company also delivers vegetables and fruits to maintain profitability in the short term. Established in 2019, the company is still in the pilot stage and experimenting with various customer segments, product portfolio, and operating models.

Operating Model:

The company has conducted market research that revealed a shortage of agricultural input products such as fertilisers, pesticides, agriculture equipment, and a shortage of fresh fruits and vegetables, primarily in urban areas. To address these issues, Afri-Tech has developed organic fertilisers, insect killer devices, & agriculture technology equipment to control weeds based on the local requirements. The company has been targeting farmers in rural areas for the sale of these products. Besides, the company targets households and hotels to deliver fresh fruits and vegetables through a customer care centre.

Financial Sustainability:

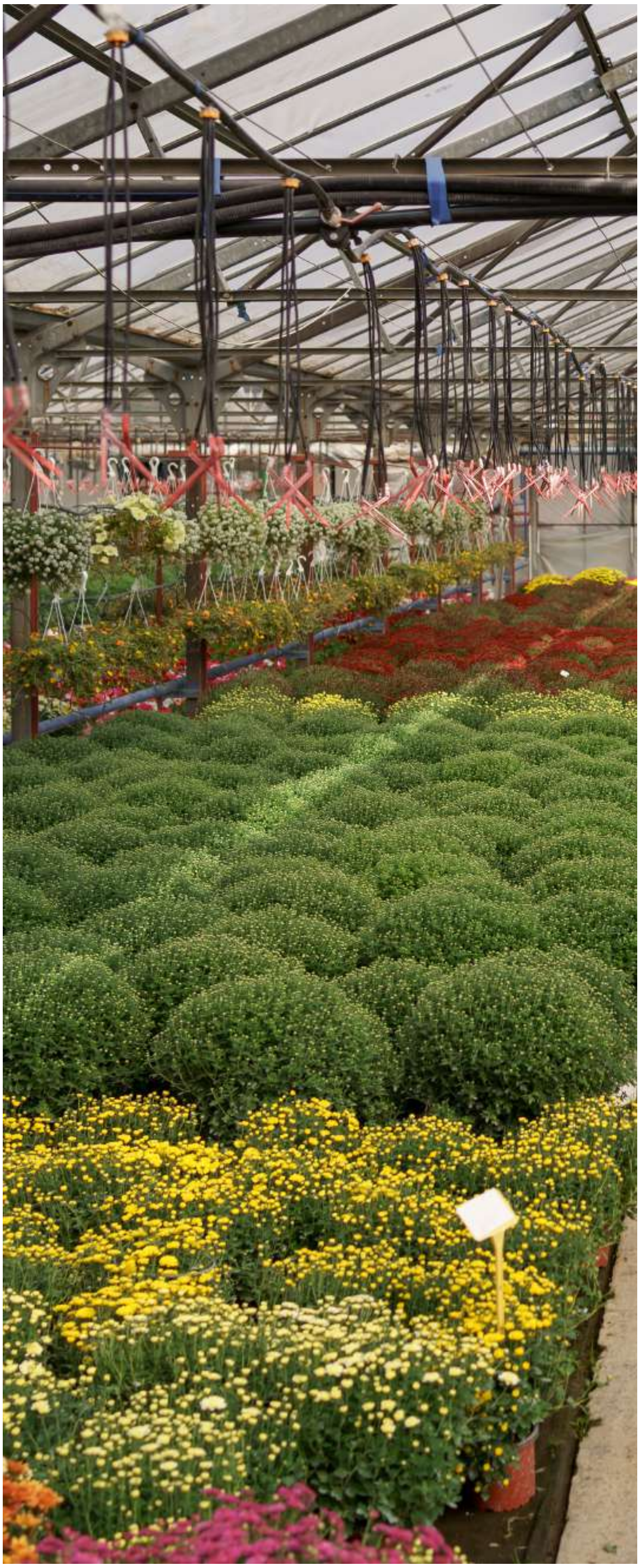
The company is bootstrapped, with the founders investing with the help of family and friends. As the company is in the pilot stage, it focuses on alternate revenue sources, such as delivering fruits and vegetables for survival. The company hopes to get funding and focus on core products such as organic fertilisers and agriculture equipment in the future.

Challenges:

Lack of access to finance, both for Afri-Tech and for the farmers, is a critical challenge. Farmers need loans to purchase agriculture equipment and fertilisers, which is extremely difficult across the country. This is due to the banks' requirement of collateral and their focus on larger SMEs and corporates.

Impact:

Afri-tech provides organic fertilisers tailor-made for the local climate, providing farmers with an increased yield. The company has also reduced the impact of weeds and water evaporation by pioneering a specific form of organic mulch that the farmers can apply directly to the surface of the soil.



ABILITY ENTERPRISES OFFERING AUXILIARY SERVICES NECESSARY FOR THE GROWTH OF OTHER ENTERPRISES

Sectors such as Information Technology(IT) are essential for Somalia's private sector's rapid growth. Somalia has a lot of potential in the IT and e-commerce industry as these sectors are still in nascent stages. Some of such services outsourced by enterprises include cybersecurity, automation workforce management, and contingent IT workforce management. Enterprises such as Super Services provide Managed-IT services for many enterprises across the country. E-commerce firm Saami Online provides consumer to consumer, business to consumer and business to business services online. While the concept of e-commerce isn't new, it is at a very nascent stage in Somalia and can create a lot of jobs and improve the country's purchasing power.

More than 80 percent of the Ability enterprises interviewed as part of the study started their business by bootstrapping or taking contributions from friends and family. Some social enterprises received seed funding from incubators, but most others raised capital from MFIs. MFIs are an important segment of Ability enterprises that solve the challenges of access to finance for both individuals and businesses. Informal lending from HNIs of society is also another common form of financing for enterprises. They offer similar interest rates as banks and financial institutions without a collateral requirement. This informal lending is often based on trust between parties and does not require any concrete guarantees. Equity and debt funding are only available for formal enterprises and have achieved a particular scale. The microfinance industry is the only option available for Somalia's informal enterprises as they cannot provide collateral to banks. Unlike the banks, the microfinance industry operates in rural areas of Somalia and is currently unregulated by the Federal Government. Besides six MFIs currently operational in Somalia, many NGOs also provide heavily subsidised microfinance products. Kaaba Microfinance Institution (K-MFI) is one of the oldest microfinance institutions in the country and is now looking into transforming itself into a micro bank to provide loans to small and medium enterprises. Despite loans being provided at a high-interest rate of more than 22 percent, this is the only means of finance for many women entrepreneurs and SMEs across the country, both in urban and rural areas.

CASE STUDY 6: KAABA MICROFINANCE INSTITUTION (K-MFI)

Description:

Kaaba Microfinance Institution (K-MFI) provides loans to poor and low-income population groups, specifically to Somaliland women and youth. These loans enable the target groups to become self-reliant and serve as agents of change. From 1999 to 2007, Kaaba was a project of the Doses of Hope Foundation (DHF). DHF's first microfinance project began in 1999 with 150 women. Between 1999 and 2007, the microfinance project directly reached out to 7000 clients and indirectly benefited another 38,000, 80% of which were low-income women. In partnership with Oxfam Novib, DHF began transforming its microfinance project into an independent microfinance institution known as K-MFI in 2008.

Operating Model:

The entity has a typical microfinance operating model. In 2016, K-MFI embarked on a new strategy that sought to transform the MFI into a micro bank (Grameen style) in the midterm. The strategy entails offering finance to small and medium businesses, offering additional products and services, funding a larger volume of loans and accessing a stable and potentially cheaper local source of funds. The process has not yet completed the transformation as it is awaiting government clearance. The entity provides Islamic financing in the form of Murabaha (cost plus markup sale contract). K-MFI purchases the requested commodity and then sells it to the customer for the cost plus profit, being a 'mark-up' that both K-MFI and the customer agree on upfront. Musharaka (partnership) is a joint enterprise or partnership structure with profit/loss sharing implications used in Islamic finance. Musharakah allows each party involved in a business to share in the profits and risks. Instead of charging interest as a creditor, the financier achieves a return in the form of a portion of the actual profits earned, according to a predetermined ratio, and Ijara (lease), which the clients mainly use to finance the acquisition of equipment.

Financial Sustainability:

Kaaba Charges a 10%-16% markup for their investments, which forms the base of their income from the disbursed loans. K-MFI raised funding in its initial stages but has been self-funded since then. More than 80 percent of K-MFI's clients are women, and these loans have contributed substantially to increasing women customers' income levels.

Challenges:

Covid-19 has severely affected the micro-enterprises that form a bulk of K-MFI's portfolio. This will indirectly impact the repayment schedule of these enterprises. Raising funds in Somaliland is a massive challenge as the country's status is unclear concerning international investors.

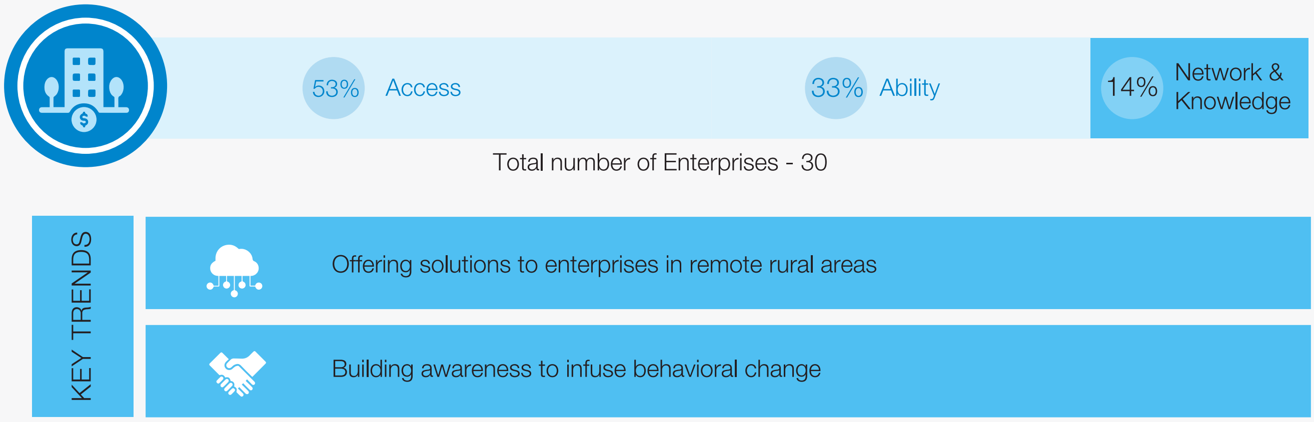
Impact:

K-MFI provides financing to more than 6000 clients currently and has directly benefited more than 14000 clients and more than 38000 clients indirectly.

3. NETWORK AND KNOWLEDGE ENTERPRISES

Many Somali enterprises lack an understanding of business operations' global norms, including governance, documentation, and fundraising. These enterprises also have limited networks resulting in a slower enterprise growth trajectory. Knowledge of these processes, procedures, and networks is essential for the sustained growth of these enterprises. While incubators and accelerators provide the requisite services to a few enterprises, yet a vast majority do not have access to them. More than 80 percent of interviewed enterprises stressed the need for business advisory support through mentorship, financial advisory support for raising investment, and facilitation of market linkages to drive their businesses' scalability and sustainability[41]. Most of these enterprises view strategic mentorship and advisory services as vital to their profitability and scalability.

Figure 8: Key trends of Network and Knowledge enterprises in Somalia



ENTERPRISES PROVIDING CAPACITY BUILDING, SKILLS TRAINING, AND BUSINESS ADVISORY SUPPORT TO ENTERPRISES

DFIs and Donors dominate the funding landscape for small-scale enterprises in Somalia through programs such as GEEL (Growth, Enterprise, Employment, and Livelihoods); many such programs insist on proper documentation as part of the due-diligence process. As such, the number of service providers who can provide these services within the country is minimal. More than 70 percent of enterprises do not know the requisite financial documents necessary[42] for raising financing from banks and other financial institutions. The consultants that are engaged to prepare these documents are costly for these micro-enterprises. As such, these enterprises do not have access to funds for working capital and expansion. Knowledge enterprises such as Onward Endeavour provide consulting services and help other businesses prepare necessary fundraising documents.

The majority of the Somali enterprises cite lack of training and capacity building as a significant challenge for their business's growth. Many enterprises also pointed- the lack of market linkages and business development support as critical expansion challenges. Knowledge enterprises such as Shaqadoon and Onward Endeavour offer consulting services, including training and other business development services for entrepreneurs and their staff. Shaqadoon visits other enterprises, assesses the problems, and has a pool of over 100+ consultants to provide relevant training. Donor grants cover the majority of the funding for these training programs undertaken by Shaqadoon. In high-security risks areas, the organisation provides training to entrepreneurs through radio talk shows and interactive SMS based programs.

ENTERPRISES BUILDING AWARENESS AND INFUSING BEHAVIOURAL CHANGE

Lack of enforcement of environmental laws has led to a lack of proper waste collection practices. Only 15 percent[43] of waste is estimated to be collected by private companies, and the rest of the waste lies scattered across the country. Enterprises such as Plastic Venture recycle plastic bottles and turn them into affordable, sustainable, and durable interlocking tiles, reducing some of the inadequately disposed waste.

CASE STUDY 7: PLASTIC VENTURE

Description:
Plastic Venture recycles plastic bags and empty bottles, turning them into affordable bricks and stone pavement for construction. The company aims to reduce vast volumes of plastic waste that has accumulated in the country.

Operating Model:
Plastic Venture uses social media platforms such as Facebook and Instagram to promote their products for retail customers. The largest customers include construction companies in Hargeisa who purchase the interlocking tiles in bulk. This provides the company with a steady stream of revenue. Plastic Ventures has recycled more than 1.4 million plastic bags and water bottles and has employed more than 30 people to collect plastic waste. The company aims to recycle more than 4 million plastic bags and water bottles over the next two years.

Financial Sustainability:
The company raised USD 4000 from a seed program and partnered with Innovate Venture, a start-up accelerator based in Hargeisa. The company is in the post-revenue stage and targets to increase its revenue in the next few years significantly.

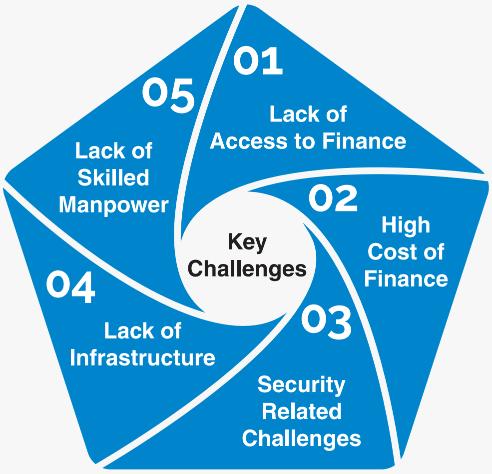
Challenges:
Access to finance is proving to be a significant challenge for Plastic Ventures.

Impact:
Plastic Ventures has recycled more than 1.4 million plastic bags and water bottles and have employed more than 30 people to collect plastic waste. The company aims to recycle more than 4 million plastic bags and water bottles over the next two years.

CHALLENGES FACED BY SOCIAL ENTERPRISES IN SOMALIA

Private sector social enterprises face a multitude of challenges in Somalia. Some of these challenges and their impact on enterprises' growth and scale are described in the section below.

Figure 9: Key challenges faced by private sector enterprises in Somalia



01 More than 88% of the loan portfolio was lent to trade financing and close to 11% for real estate financing. Less than 1% was lent to enterprises operating in other sectors with Renewable energy enterprises being the largest borrowers

02 Banks charge upwards of 20% interest rate per year making loans extremely expensive for SMEs. Banks are able to charge such high interest rates because of demand from the trade sector which borrows for short time duration.

03 Lack of security in some parts of the country often creates a problem for enterprises looking to expand beyond their city of establishment

04 Lack of roads and electricity is a major challenge for enterprises. Lack of infrastructure typically leads to a higher cost of production
High cost of electricity (sometimes costing as much as USD 1 per Kwh) is also a major barrier for enterprises

05 Lack of skilled manpower ranging from technical, vocational, accounting, and other necessary skills

- ***Lack of access to finance*** is a significant challenge for private sector enterprises in Somalia. ***Trade financing and real estate are the two sectors that received more than 98 percent of loans from banks and formal financial institutions***[44]***.*** Banks prefer lending to the trading sector as it borrows for a short duration of time. On the other hand, the real estate sector mortgages the properties with the bank, as a result of which it can get longer duration loans. It leaves only 1-2% of the financial institutions' lending portfolio for agriculture, livestock, healthcare, and other sectors that require long-term loans but are unable to afford the high cost of financing[45].

> *It is very difficult to raise money from banks due to their high interest rates and short tenures. The repayment period for most of the loans is only 12 months*
> *CEO – Livestock Enterprise*

In most cases, banks do not accept land as collateral. There have been multiple land grabbing incidents during the civil war, and the land registry with the federal government is outdated. Women-led businesses in the country face even more discrimination and socioeconomic barriers in securing finance. It is primarily due to the lack of financial products targeting women and a cohesive policy to encourage lending to women SMEs. ***Many enterprises that have successfully raised funding have raised it on a parent entity based outside of Somalia.*** One of the social enterprises interviewed mentioned that it has raised money for its Kenyan entity but has not raised for its Somali entity despite it being much bigger in revenue.

> *Business like mine find it difficult to raise funding from banks or any other financial institutions, because they don't provide working capital support. My business needs funding to cover the operation expenses and vendor cloud subscription expenses but all available investors provide capital only to buy physical products.*
> *CEO – IT Enterprise*

Enterprises often need an office outside of Somalia to procure equipment and goods as there are limited banking linkages with the international financial system. As such, there are considerable delays in payment processing. Most international banks place restrictions on the transfer of funds to Somalia, which has been a pressing issue for many enterprises and investors alike. On the other hand, the study observed that investors hardly travel to Somalia and are much more comfortable meeting in Nairobi or other countries. Even if the investors travel to Somalia, they barely get out of the Green Zone[46] and cannot adequately evaluate the enterprises' investment viability.

> *There are no mainstream banks ready to take on the risk of investing in small scale enterprises.*
> *CEO – Plastics Enterprise*

• ***Women and women-owned enterprises face a greater degree of discrimination and challenges in growing their businesses.*** Women in Somalia own 60 percent of microbusinesses[47]. However, they face greater challenges such as (i) lack of access to information (due to lack of mobility outside the home and lower technological literacy), (ii) access to finance (some financial institutions still mandate a male signature), (iii) lack of women-friendly financial products, (iv) lack of information regarding avenues of finance, and (v) linkages for accessing informal financing sources. Many of the women who have started the businesses to supplement household income are hesitant to take on more financing, which adds to the debt burden. Women also have lower ownership of identification documents leading to difficulties in establishing a formal enterprise.

Somalia is one of the few countries that has failed to ratify the 'convention on the elimation of all forms of discrimination against women'

Gender Inequality Index	0.776 (2012)	4th highest level of inequality recorded globally
Parameter	**Women**	**Men**
Labour Force Participation (2018)	37%	58%
Employment rate (2016)	10%	32%
Use of Traditional banking services (2017)	11.5%	19%
Current banking customers (2017)	36.7%	63.3%
Mobile money accounts (2018)	70%	75%

• ***The high cost of finance hinders the growth of most enterprises in Somalia.*** Interest rates for loans from banks and other financial institutions range from 20% - 30%, making it untenable for enterprises to borrow for long-term purposes[48]. Moreover, Somali banks and financial institutions are not experienced in lending to enterprises outside of trade-financing and real estate. They have a weak pipeline of bankable micro, small, and medium enterprises operating in the economy's high-impact sectors such as agriculture, livestock, and fisheries. Social Enterprises also have a minimal understanding of what constitutes a well-prepared and documented loan application. They often do not possess the requisite documents, thereby resulting in the minimal provision of credit.

• ***Lack of a national identification system limits enterprises' financial access and creates difficulties for banks and financial institutions in assessing the customers' creditworthiness.*** More than 77 percent (2018) of Somali citizens were estimated to lack official proof of identity[49]. Women are more likely to lack an identification document with an estimated gender gap of 9 percent[50], mainly due to Somali society's patriarchal nature. International development organisations such as World Food Programme (WFP), United Nations Office for Project Services (UNOPS), National Commission for Refugees, and Internally Displaced Persons (NCRI), among others, collect identity data and issue credentials. These, however, have limited utility. Since these programmes are often concentrated in a particular area, the identification systems are fragmented and designed to meet specific program needs rather than serve as a multipurpose identification for the entire population. Lack of a robust identification system makes it difficult for financial institutions to fulfil international customer due-diligence and Know Your Customer (KYC) verification, thereby failing to adequately comply with the global anti-money laundering and countering the financing of terrorism requirements. It has resulted in many Somali financial institutions and remittance providers losing their corresponding banking relationships with international banks, further impeding financial access to individuals and enterprises. Having a unique identification system will help increase financial access and other essential services for individuals and enterprises. It will also be instrumental in improving business registration's robustness and increasing transparency around Somali companies' ownership and financing.

WFP's SCOPE system, which is used to register and manage benefit transters to the beneficiaries of WFP assistance in somalia, contains information on over 4 million individuals (biometric registrations of 2 million individualsm and additional 2 million individual registeres by collecting their biographic data only).

• ***Infrastructure challenges pose one of the critical challenges to the private sector development in Somalia's economy.*** High costs of electricity and transportation severely limit the growth of sectors such as manufacturing. The cost of electricity in Somalia (USD 0.5 – USD 1 per kWh)[51] is amongst the highest in the world in comparison to electricity rates in Kenya (USD 0.2 per kWh), India (USD 0.08 per kWh)[52], and China (USD 0.08 per kWh). The high cost of electricity makes Somali manufacturing non-competitive. This further drives up imports and provides a boost to the trading sector. Bad roads increase transportation costs, especially in rural areas, from where agricultural commodities are transported. Transportation of perishable items in the rainy season is challenging from the hinterlands. Illicit roadblocks collecting huge charges and multiple tax collection often render agricultural produce unprofitable. ***Capital spending on infrastructure is a small fraction (less than 6% in 2018) of the Federal Government of Somalia's budget, which is insufficient to meet the infrastructure needs in post-conflict Somalia*[53] *and results in enormous losses for rural enterprises.***

> *"The cost of electricity is prohibitively expensive in Mogadishu. This coupled with the extremely high rentals in the area makes it very challenging for enterprises to operate in the area"*
> *CEO – IT Enterprise*

• ***Lack of regulatory oversight is also a significant issue for many of the enterprises operating in the country. Despite 70 percent of Somali citizens with cell connectivity using mobile money regularly and transacting for USD 2.7 billion per month in 2017*[54]*, there is no regulatory oversight on mobile money transactions.*** Currently, the regulation on financial institutions (FIs) by the Central Bank of Somalia only governs banks and Money Transfer Businesses (MTBs), even excluding the microfinance sector. Lack of regulatory oversight is often seen as a red flag by both enterprises and investors looking to trade and transact. Many enterprises have also suggested that while relevant laws exist, the poor implementation of these laws results in low confidence in the investor and investee system. It often leads to non-compliance with contractual obligations, bribery, and protracted legal battles. All of these factors slow the private sector's progress, thereby stagnating the country's economic progress.

Enterprise view of the security situation in somalia

Most of the private sector enterprises in Somalia are not concerned about the security situation in their area of operations. However, these enterprises are concerned about expanding their business to other parts of Somalia as this exposes them to the various regional factions operating in these regions. The enterprises feel is due to the fragmented nature of the govement and the regional conflicts ongoing within the country. Most of the regional groups have their own strongmen and businesses loyal to the clans. These clans do not often allow outsides businesses to operate without their consent.

• ***Lack of a skilled workforce is another major challenge for enterprises in Somalia.*** Enterprises in the country face human resource challenges, with many individuals lacking the necessary technical, vocational, and accounting skills. School enrolment rates in the country are among the lowest in the world, with only a 32 percent gross enrolment ratio (2015/16 levels) in comparison to the average gross enrolment of 74 percent in other low-income Sub-Saharan countries[55]. The lack of literacy and education levels is because more than 75 percent of existing educational institutions were destroyed during the civil war, coupled with one of the world's lowest teachers' qualifications with only 37.9 percent qualified primary school teachers[56]. Higher education is primarily unregulated in Somalia. The Higher Education Act designed to remedy this problem has been stuck in the Somali Parliament since 2018. Somaliland is the only state-level government to pass a law that lists out the requirements for university registration. The faculty qualification is also not monitored closely, and only 9 percent of the universities' academic staff have a PhD degree[57].

04

THE LANDSCAPE OF IMPACT INVESTORS IN SOMALIA

The chapter covers the supply of impact investment in Somalia, focusing on the type of impact capital providers present in the country and their investment strategies. The section also covers various challenges faced by investors in the country. The sections' insights and learning are based on a combination of secondary research and discussions with 17 investors and ecosystem support organisations (ESOs) present in Somalia.

CURRENT IMPACT INVESTMENT LANDSCAPE IN SOMALIA

There exists a vast mismatch between the demand and supply of impact capital in Somalia. Being a fragile war-torn country, many of the impact sectors, including agriculture, healthcare, energy, and others, have decreased productivity, mangled infrastructure, and inadequate human resources. As a result, the country needs assistance in the capital and advisory services to rebuild its economy. While the international community, particularly Development Financial Institutions (DFIs) and donor agencies have contributed to humanitarian aid, impact investing in the private sector is still in its nascent stages.

Investments in Somalia have the potential to deliver higher than expected results for investors. Traditionally, investments in fragile and conflict states have provided investors with a higher return rate than other countries' investments. According to the Multilateral Investment Guarantee Agency (MIGA), the average rate of return on Foreign Direct Investment (FDI) in fragile and conflict states from 2006 to 2011 has been 14.5 percent, which is higher than FDI in low-income countries (9.7 percent) and the global average (6.2 percent)[58].

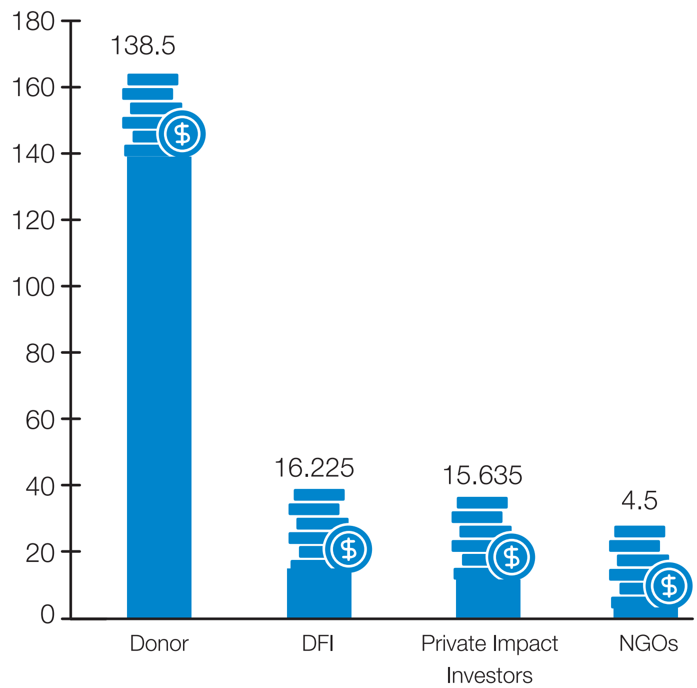
Impact stakeholders (including DFIs, Donors and Private Impact Funds) have invested a total of USD 175 million[59] (2005 – 2020) towards equity and debt investments in enterprises, providing grants, technical assistance, and credit guarantees. Islamic Finance is the most common investment mechanism, which has been a challenge for some investors. Most of the impact investment was by donors (more than 75 percent of total investment). These impact investments have been directed towards entrepreneurial ecosystem building, i.e., providing technical assistance, building enterprises' capacity, establishing market linkages, establishing incubators and accelerators, and other enterprise-related activities. DFIs, on the other hand, have invested both directly and indirectly through local private funds.

While investments by private impact funds make up less than 9 percent of the total impact capital deployed, they have played an essential role in showcasing Somali enterprises' potential to DFIs, donors and other foreign investors looking to invest in the country. *The majority of the capital by these private impact funds was deployed through investment funds operating locally in Somalia.*

Impact Investment definition in Somalia

Based on the discussions with the stakeholders from Somalia, 'Impact Investment' is defined as investment that aims to create sustainable impact ob the society. For a country like Somalia, the definition of impact investing is much broader than the normal context in which it is used. The major focus of impact investing in fragile countries such as Somalia is on employment generation and poverty alleviation.

Figure 10: Impact Investments in Somalia (by various category of investors - USD Mn)[60 61]



Source: Intellecap Analysis

OVERVIEW OF KEY IMPACT INVESTORS IN SOMALIA AND THEIR INVESTMENT/ FUNDING STRATEGIES

Impact investors operating in the country have primarily adopted five key funding strategies shown in the image below.

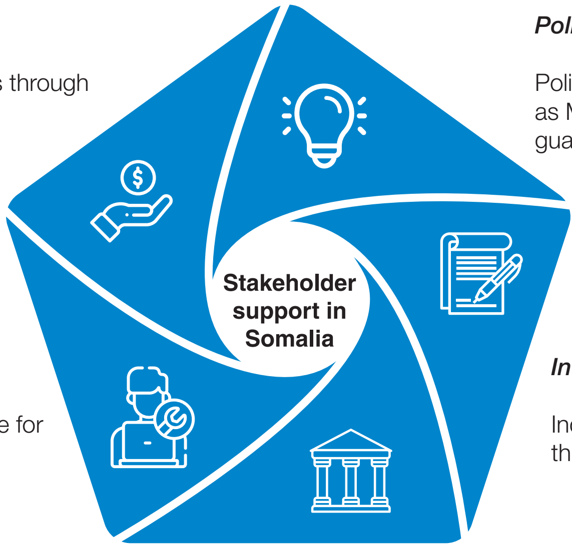
Figure 11: Overview of funding strategies used by investors in Somalia

Providing Grants

Providing grants to enterprises through various contests and facilities

Political Risk Insurance/Guarantee

Political insurance through facilities such as MIGA and risk insurance through credit guarantee facilities



Technical Assistance

Providing technical assistance for enterprises and institutions

Investing in Enterprises

Indirectly investing in enterprises through financial entities

Assisting the Federal Government

Working with the federal government to issue new currency and build monetary policy

Source: Intellecap Analysis

Figure 12: Analysis framework for impact investments in Somalia

	Design Stage Grants	Technical Assistance Funds	Debt/Equity Investments	Guarantee/Risk Insurance	Concessional Capital
Angel Investors			*Diaspora, Expats, and HNIs*		
Incubator & Accelerators	*Harhub*	*iRise, Somali Innovation Hub, Innovate Ventures, Next Economy, Tethered Up*	*Next Economy, Innovate Ventures*		
Foundations & NGOS	*Silatech, Oxfam*	*itfin Foundation, Silatech, Shaqadoon, Response Innovation Lab, CARE, Spark, Oxfam*	*Shaqadoon, Arsenault Foundation*		*Silatech*
DFIs		*IFC, Islamic Development Bank, Finnfund*	*FMO, Swedfund*	*MIGA, Development Finance Corporation, SIDA*	*Norfund, IFC, IFU*
Impact Investors		*Shuraako*	*Hayaan Capital, Shuraako, Somali Agrifood fund, FCA Investments, K-MFI*		
Bilateral/ Multilateral Donors	*IFAD, USAID, World Bank, UNDP*	*Danida, USAID, World Bank*			*USAID, DFID, World Bank*

Investor-wise Investment Instrument Preference Scale *High* ●●●● *Low*

Source: Intellecap Analysis

Many of the impact investors, including Norfund, FCA Investments, DFC, Shuraako and IFC, have directly and indirectly contributed to the growth of social enterprises in Somalia. Many of these investors primarily focus on the productive sectors, including agriculture, agro-processing, fisheries, livestock, and livelihood, as enterprises from these sectors cannot obtain financing from banks and other financial institutions. While some investors such as Shuraako invest directly in social enterprises, others such as Norfund and IFC invest indirectly through lending to banks and investing in financial institutions.

Investors provide a wide range of services ranging from design stage grants, technical assistance, impact investments, guarantee and risk insurance, concessional capital, among others. While most of the donors and multilateral agencies operating in the country provide humanitarian and inter-governmental aid, a few of them work directly with enterprises to expand and streamline their operations. Incubators and accelerators have only started operations in Somalia as recent as 2015-16[62]. Still, they have contributed significantly to the private sector's growth by providing technical assistance, assisting with investment readiness support, among others. Some of the incubators, such as Harhub, have also directly invested in their enterprises. Donors have mainly provided concessional capital along with technical assistance to enterprises and funds in Somalia. In most cases, there is often a collaboration between various DFIs and donor agencies to provide capital, technical assistance and guarantee facilities.

ROLE OF DFIS IN THE IMPACT INVESTMENT SECTOR IN SOMALIA

DFIs often have a crucial role to play in the FCV countries across the globe. They are often pioneers in investments across these countries. IFC estimates that in 2018, DFIs catalysed around 400 percent more investment against FCV countries' commitments[63]. In addition to directly providing impact capital, DFIs also play a critical role in mobilising investments from other investors by providing credit guarantees, risk assurance, etc. DFIs in Somalia have deployed more than USD 16 million towards investments and capacity building of enterprises and other relevant institutions. Some of the significant DFIs operating in the country include Norfund, FMO, IFC, IFU, Swedfund, Development Finance Corporation(DFC), and the Swedish International Development Corporation (SIDA).

Figure 13: Summary of activities of major DFIs in Somalia between 2005 and 2019[64]

Name of the DFI	Capital Deployed (USD Mn) (2005 – 2020)	Sector Priorities	Key Investment Strategies
FMO	*11.75 Mn*	*Telecommunications*	*Debt and Grant*
Swedfund	*4.2 Mn*	*Telecommunications*	*Equity*
Islamic Development Bank	*0.275 Mn*	*Multiple Sectors*	*Technical Assistance*
IFC	*NA (as part of investment into Gargaara – Indirect investment)*	*Financial Services*	*Convertible*
Norfund	*5 Mn (Indirect investment)*	*Agriculture and Fisheries, Healthcare, Water and Sanitation and others*	*Equity (into a local fund) and Debt (while investing in enterprises)*
IFU	*2 Mn (Indirect investment)*	*Agriculture and Fisheries, Healthcare, Water and Sanitation and others*	*Equity (into a local fund) and Debt (while investing in enterprises)*

Source: Intellecap Analysis

SECTOR PRIORITISATION BY DFIS

DFIs play a significant role in the development of impact sectors in the country. In Somalia, DFIs have directly invested in agriculture and telecommunications and indirectly invested in agriculture, clean energy, fisheries, healthcare and other impact sectors. These indirect investments have been made through local funds such as Shuraako and have focused heavily on the impact sectors. DFIs in the past haven't had a profitable experience investing in Somalia. FMO and Swedfund, for example, invested in Somalia Telecom when there was no regulatory framework for telecommunication companies' operations. They provided a grant of USD 250,000 to create a regulatory framework for the sector. Unfortunately, the company had to file for bankruptcy due to cost escalations arising from the country's deteriorating security situation. The political risks, including employing soldiers to guard telecom towers, pirates using the telecom network, and Al Qaida's involvement in business ownership, made it almost impossible for the company to continue operations[65]. Taking a cue from such instances, Norfund has put its proposed investment in one of the large Somali entities on hold due to corporate governance issues and lack of clarity on the source of funds.

INVESTMENT STRATEGIES ADOPTED BY DFIs

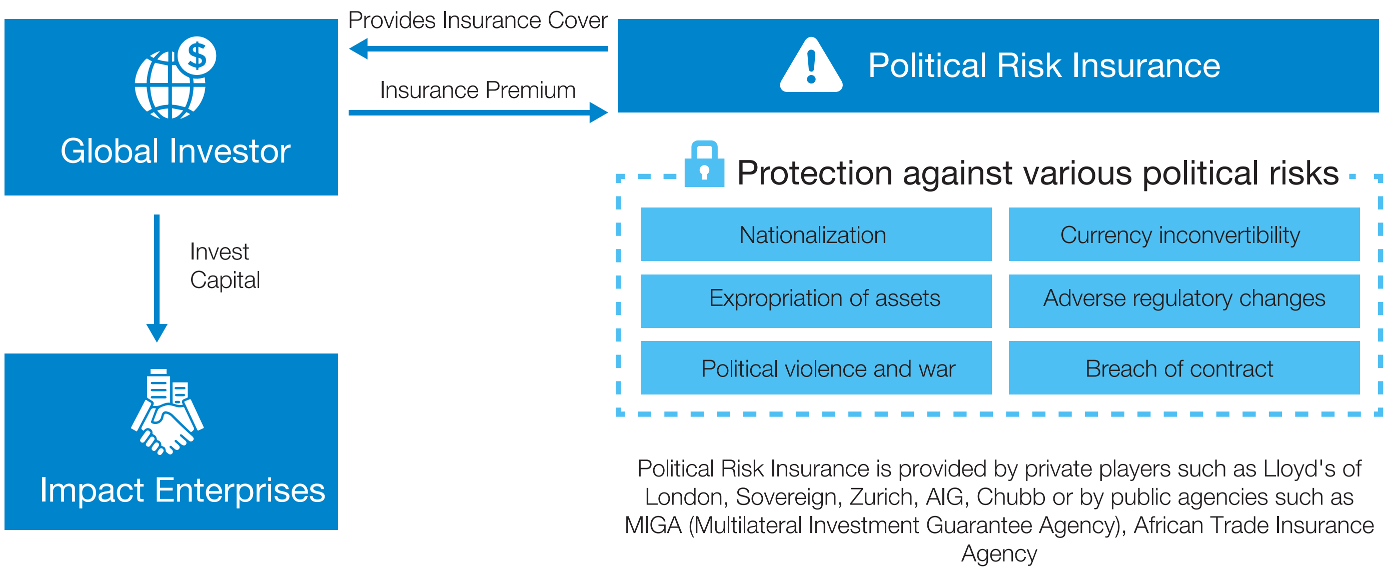
DFIs have catalysed the investment landscape through various tools and engagements. DFIs typically provide grants, technical advisory support, and investments into funds, banks, and financial institutions for on-lending to enterprises in Somalia.

Technical Assistance: Technical Assistance (TA) services compliment the financial services provided by DFIs in Somalia, as the entrepreneurial ecosystem is still very nascent in the country. Enterprises and ESOs in Somalia often lack knowledge and know-how of the various processes, procedures, and technologies that contribute to the faster growth of private sector. Islamic Development Bank provides technical assistance to prepare the legal, regulatory, supervisory, and Shari'ah governance framework for Islamic banking in the country. Many investors outside Somalia do not know the country's Islamic banking regulations and are apprehensive about investing in the country. Finnfund, through the Finn partnership program, carried out matchmaking and technical advisory services for Finnish and Somali enterprises. This partnership was supported by the Somali diaspora living in Finland and had participation from various Nordic countries, various government agencies, and more than thirty local companies. World Bank, the African Development Bank, the Islamic Development Bank, and UNIDO[66] also supported the initiative.

Political and risk insurance: Many Investors look for political risk insurance while investing in Somalia due to the inherent risks involved while investing in the country. Political risk disrupts enterprise operations due to political instability, violence and war-like situation, government expropriation of assets, adverse regulatory changes, breach of contract, the wrongful calling of debt letters, arbitration award defaults, inability to repatriate funds, among others. DFIs in Somalia provide a wide range of political insurance tools, including a) currency inconvertibility and transfer restriction cover for inability to convert or transfer dividends due to foreign exchange restrictions, b) exproportion cover when the government nationalises or makes it impossible to operate the project, c) war and civil disturbance cover for destruction and interruption of business due to political violence, breach of contract cover for government defaulting on its obligations among others. DFIs' supported political risk insurance is provided by private and public insurers, with MIGA being the largest provider. MIGA is an arm of the World Bank Group and provides extensive political risk insurance for fragile countries' investments. FCA investments, which is looking to invest in Mogadishu based enterprises, is currently working with MIGA to provide political insurance for its investments[67]. MIGA can provide insurance for up to 15 years (in some cases, 20 years). The agency conducts project due diligence, environmental and social due diligence, and technical and commercial due diligence on all projects before deciding on insuring the project itself or through syndication.

Credit guarantee facility: The financial sector in Somalia is underdeveloped. The financing costs are also high, which makes only short-term lending feasible for both banks and enterprises. Some of the DFIs, such as DFC, SIDA, have started providing credit guarantees to banks and financial institutions to lend to high-impact sectors such as agriculture, livestock, and fisheries. In Somalia, SIDA has provided credit guarantees to One Earth Future Foundation (OEF), under which the Shuraako program was implemented[68]. In turn, OEF has signed agreements with Dahabshil Bank, Premier Bank, Amal Bank, and the International Bank of Somalia, which will provide loans to the target group

Figure 14: Overview of Political Risk Insurance

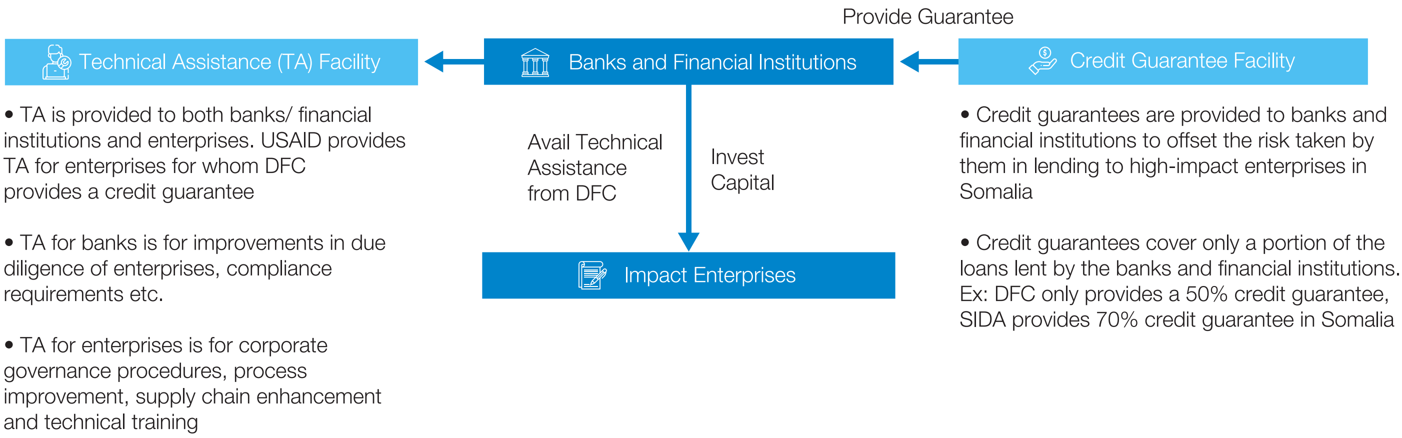


Source: Intellecap Analysis

by utilising the credit guarantee. Through this arrangement, the banks' risk is reduced by up to 70% in case of non-repayment of loans[69]. This USD5 million credit guarantee is complimented by a TA facility provided to both banks and enterprises[70]. DFC also provides similar credit guarantees where the banks' risk is reduced by 50-70% while delivering TA through USAID[71].

Direct investments (Equity/Debt) in enterprises: DFIs haven't directly invested in many Somali enterprises. Many DFIs, such as Norfund, have invested indirectly in enterprises either through Somalia-focused funds such as Shuraako or through investments in financial institutions such as the Gargaara facility. It is mainly because of DFIs' lack of experience and knowledge of the country and capabilities to conduct on-ground due-diligence. Some of the other reasons for the lack of direct DFI investments in Somalia include lack of enterprises with the appropriate scale to warrant funding from DFIs, lack of corporate governance, lack of clarity on the source of funds, among others. For example, the minimum size of investment on Norfund's balance sheet is USD 5 Mn for not more than a 35% stake. If it's a debt investment, it should not be more than 49% of the balance sheet (minimum of USD 5 Mn). It is challenging to find enterprises that can absorb that level of investment in Somalia. FMO and Swedfund invested more than USD 15 million in Somalia Telecom Group in 2007-2008. The sizeable urban population of Puntland and Somaliland and Somalia Telecom Group's strong position in the market contributed to a strong business case at the time. Due to several factors, including difficulty establishing a proper business model in the region and lack of corporate governance practices, the company had to file for bankruptcy in 2010.

Figure 15: Overview of a Credit Guarantee Facility



Source: Intellecap Analysis

Case Study 8: Somalia Telecom

TELECOMMUNICATIONS

Somalia Telecom

The Somalia Telecom Group was established in 1992 by Somali diaspora. A grant of USD 250,000 was provided to create a regulatory framework for the telecom sector.

FMO led the investment process and invited Swedfund to participate with Ericsson as equipment supplier. The situation in the country deteriorated quickly with bombings in Mogadishu and Somaliland and the company filed for bankruptcy in 2010

- *Investor (s): FMO and Swedfund*
- *Amount: USD 15.95 million*
- *Investment Type: Equity and Grant*
- *Year of Investment: 2007 and 2008*
- *Sector: Telecommunications*
- *Status: Bankruptcy*

Source: FMO and Swedfund

ROLE OF DONORS IN THE IMPACT INVESTMENT SECTOR IN SOMALIA

Donors play a crucial role in the development of the private sector in fragile and conflict countries. They provide grants, technical assistance and often assist with the overall ecosystem development. It, directly and indirectly, helps in the private sector's growth and impact enterprises in the region. Donors have invested close to 80 percent of the total capital (approximately USD 138 million) for the growth of the private sector social enterprises in Somalia between 2005 – 2020. Some of the significant donors active in the country include USAID, World Bank, FCDO, and DANIDA.

Figure 16: Summary Table for Major Donors in Somalia between 2005 and 2020[72]

Name of the Donor	Capital Deployed (USD Mn) (2005 – 2020)	Sector Priorities	Key Investment Strategies
World Bank	*59.5 Mn (through syndication of funds from various donors and DFIs)*	*Multiple sectors including agriculture, financial services, healthcare*	*Debt, grants, and technical assistance*
USAID	*74 Mn*	*Agriculture, fisheries, dairy*	*Debt and technical assistance*
SIDA	*5 Mn plus undisclosed investment as part of investment into Gargaara – Indirect investment*	*Financial Services*	*Credit guarantee, Convertible*
DFID	*NA (Indirect investment as part of Gargaara)*	*Financial Services*	*Convertible*
DANIDA	*NA (Indirect investment as part of Gargaara)*	*Financial Services*	*Convertible*

Source: Intellecap Analysis

SECTOR PRIORITISATION BY DONORS

In Somalia, donors prioritise assisting enterprises in the impact sectors such as agriculture, financial services, fisheries, and dairy. They also provide grants to small and medium businesses and help these businesses with market linkages. Donors work with various stakeholders within the value chains, including food processors, investors in boat-building, refrigeration, transport providers, financial institutions and others to create the maximum impact. Apart from providing grants and other financial investments, donors mainly involve in market linkage activities such as introducing efficient irrigation systems, seeding export-oriented crops, constructing irrigation canals, access roads, landing-piers for boats, and training relevant personnel. Most donors in Somalia offer these grants as matching funds, wherein the donors contribute half of the required investment, and the enterprise invests the same amount. It is done to increase the accountability of the enterprises in utilising the grant money effectively. Donors also work with various government agencies to help create an ecosystem for the private sector's growth. World Bank Group is working with the Federal Government of Somalia to help issue new currency and design a monetary policy for the overall development of the impact sectors.

Case Study 9: Somalia Business Catalytic Fund

SME FINANCING

Somalia Business Catalytic Fund

World Bank launched the Somali Business Catalytic Fund (SBCF) to invest in the establishment and expansion of profitable small and medium enterprises (SMEs).

The SBCF supported companies to innovate and enhance their productivity, competitiveness against imported products, and improve overall profits, enhance efficiency in the economy as a whole and increase employment. In addition, SBCF provided grants targeted at developmental priority groups such as women-owned enterprises and youth employers.

- *Investor (s): World Bank*
- *Amount: USD 6.5 million*
- *Investment Type: Grant*
- *Year of Investment: 2007 and 2008*
- *Sector: Multi-Sector*
- *Number of enterprises reached: 82*

Source: World Bank

INVESTMENT/FUNDING STRATEGIES OF DONORS

Technical Assistance: The donors in Somalia are actively involved in providing technical assistance and capacity-building support to Somalia enterprises. Some of the crucial areas of technical assistance for enterprises in Somalia include the following:

- ***Offer Knowledge:*** Modern technologies can help improve productivity. Donors offer enterprises knowledge such as modern fishing methods, knowledge of agricultural equipment, improved farming practices etc.

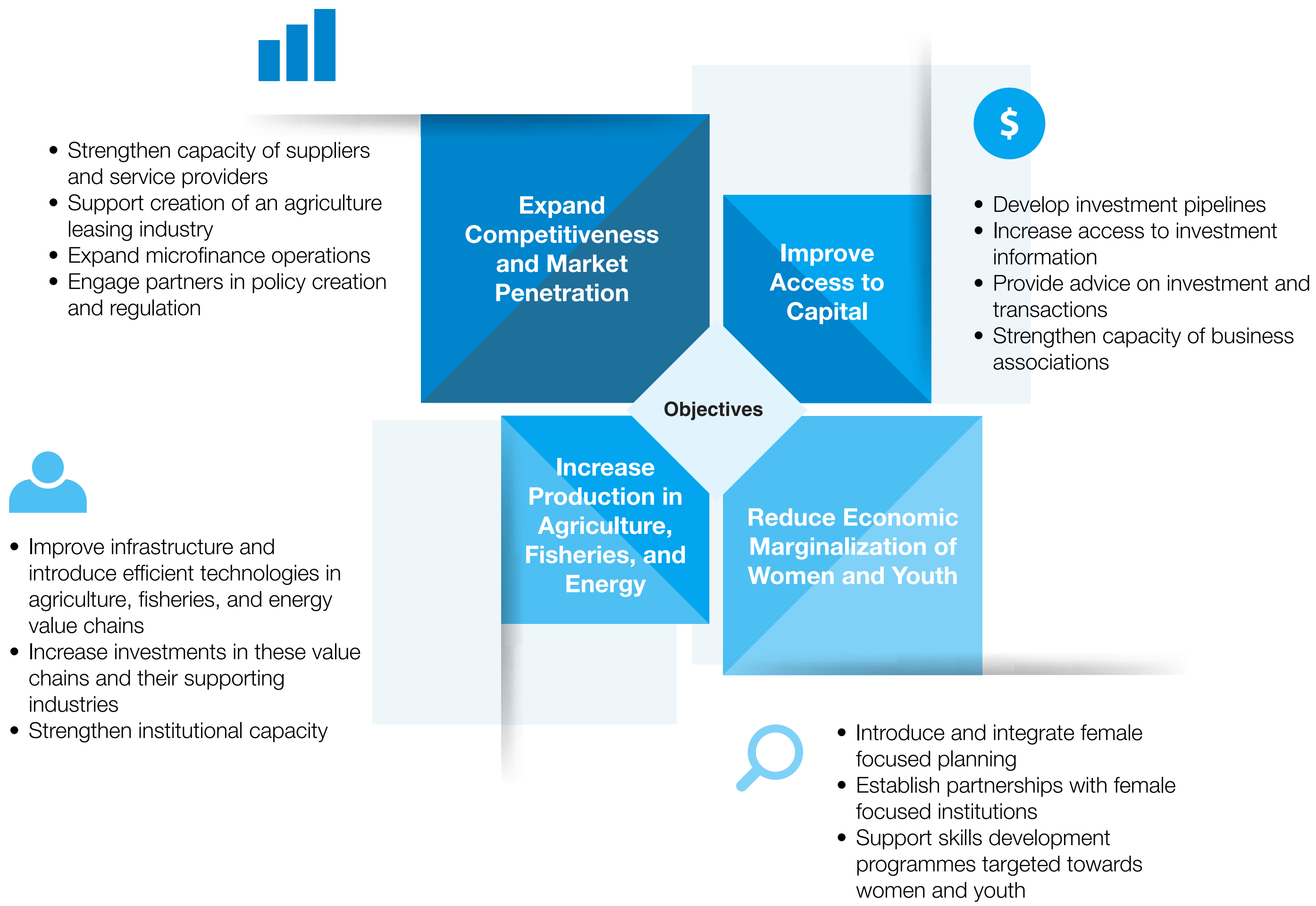
- ***Provide Assistance:*** Many of the Somalia enterprises often lack the knowledge of globally recognised and accepted financial and accounting practices. Many, as a result, are viewed with suspicion by investors. Thus, offer enterprises assistance with financial and accounting practices to make them investor ready.

- ***Facilitate Linkage:*** Donors, through their global network, have access to many buyers and suppliers across the world. Facilitating market linkages for enterprises can help them market their products worldwide, thereby enhancing their finances.

- ***Forge Partnerships:*** Many of the Somalia enterprises require partnerships with other successful businesses worldwide to understand their growth trajectory, procure necessary equipment, and understand new technologies. Donors in Somalia help enterprises with these partnerships resulting in improved competitiveness of the enterprises.

Some of the donors, including USAID, have created technical advisory programs that complement other institutions' funding mechanisms. Through the Growth, Enterprise, Employment, and Livelihoods (GEEL) program, USAID aims to increase the pace of Somalia's integration into the world economy. The program aims to reduce the trade imbalance, increase market linkages and business partnerships, and spur new investments to create jobs. The GEEL program is a USD 74 million project from 2015-2021 and aims to provide technical services to enterprises and address challenges and opportunities across multiple sectors through policy and regulatory reforms. The program has provided technical assistance to over 800 micro-enterprises, created over 4,600 new direct and indirect jobs. It has helped generate more than USD 39 million in recent sales by Somali enterprises[73]. GEEL program also allows enterprises to market their products through their group network of other businesses, corporates, NGOs and others. For example, in 2016, GEEL supported a group of enterprises to establish the first Somali exhibit to promote Somali products at the Gulfood trade show in Dubai, the world's largest food exhibition. Three years later, there has been a five-fold increase in the number of exhibitors supported by GEEL. In addition to supporting the enterprises exhibit their products, GEEL also facilitates meetings with buyers resulting in Somali export sales increase by more than USD 4 million over three years[74].

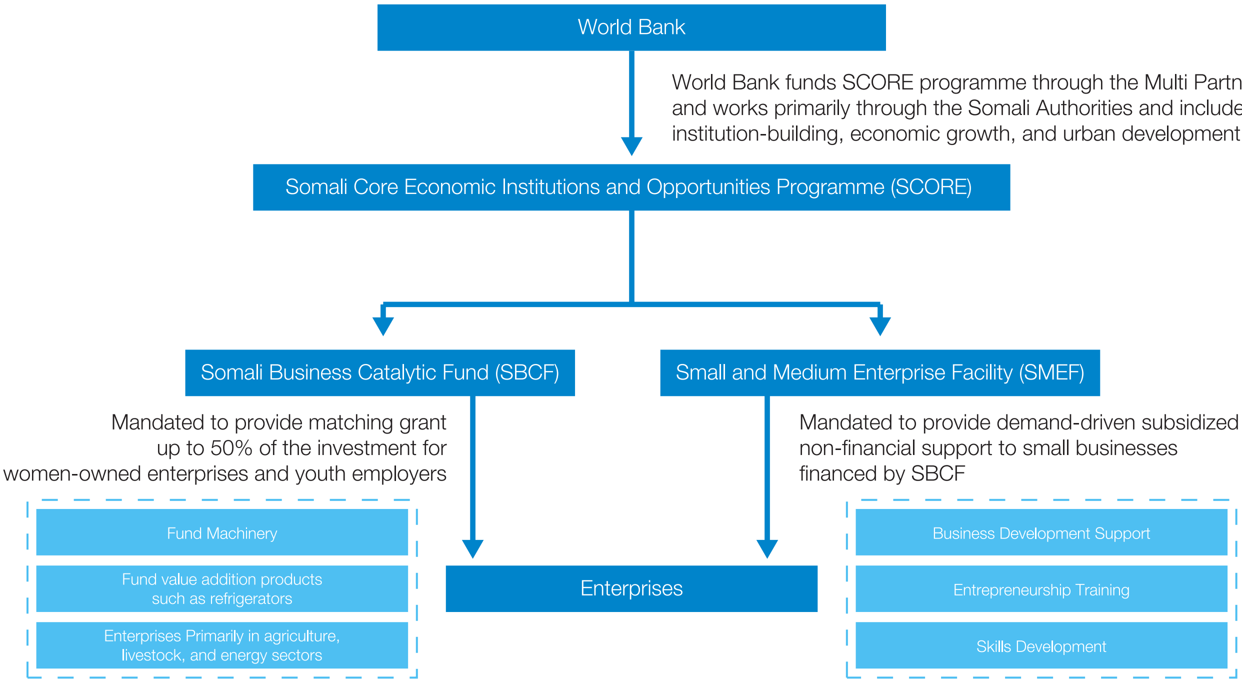
Figure 17: Growth, Enterprise, Employment, and Livelihood (GEEL) project[75]



Source: USAID

Grant Funding: ***Donors also support enterprises in Somalia by providing them with grant funding.*** These grants are both offered directly to the enterprises and indirectly through incubators and accelerators. While some of the grants are provided through organised facilities such as the Somali Business Catalytic Fund (SBCF), others are provided to enterprises as part of business competitions, conferences, and seminars. Through the Somali Core Economic Institutions and Opportunities Programme (SCORE) (2016 – 2020), World Bank has also contributed to the development of entrepreneurship in Somalia. The SCORE project has launched a USD 5.5 million Business Development Services (BDS) for entrepreneurs. The BDS facility has mobilised SME financing through the Small Business Catalytic Fund (SBCF) and the Small and Medium Enterprise Facility (SMEF). SBCF provided grants targeted at developmental priority groups, including women-owned enterprises and youth employers. The fund has disbursed more than USD 6.5 million to 82 enterprises in high-impact sectors such as agriculture, manufacturing, and fisheries sectors as of June 2018[76]. In the course of the entire project cycle, it hopes to disburse USD 10 million. On the other hand, SMEF provides demand-driven subsidised non-financial support to enterprises financed by SBCF.

Figure 18: Somali Core Economic Institutions and Opportunities Programme (SCORE)



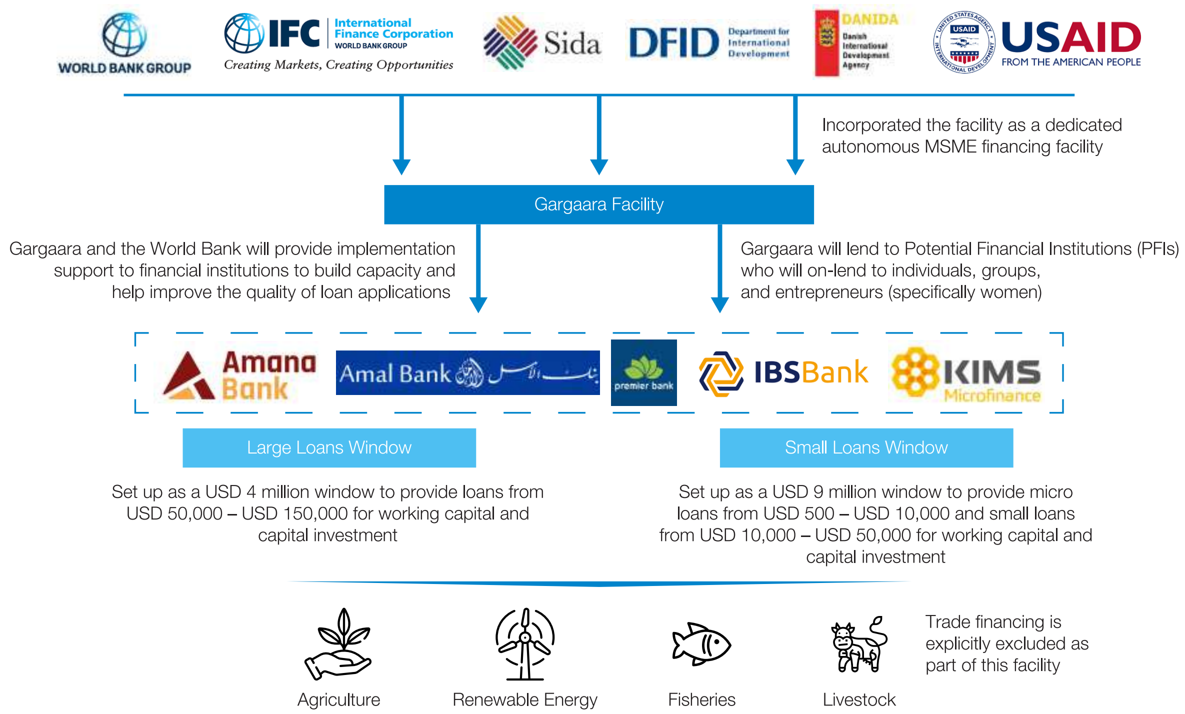
Source: World Bank

On-lending credit: Due to lack of capital, Somalia's financial institutions are unable to lend to enterprises in the impact sectors. Many donors also lack institutional capabilities to lend to enterprises in fragile economies without having on-ground personnel. In such cases, donors come together to establish an on-lending facility that can be used to lend to impact enterprises. Donors, such as the World Bank, have collaborated with DFIs, including IFC, SIDA, European Union, Foreign, Commonwealth & Development Office (FCDO), USAID, DANIDA, and the Federal Government of Somalia, to set up the Gargaara facility. The facility acts as an apex institution financing the bank and non-bank financial institutions. The facility is structured to operate through private sector management and governance principles. The facility also has provisions to allow for the transition towards private sector majority shareholding over time. The facility will on-lend to eligible financial institutions; FIs are free to decide on granting loans to enterprises on a commercial basis. The loans from the facility aim to target small-scale enterprises, especially women and youth. Gargaara and World Bank would also provide technical assistance to build the capacity of banks and financial institutions in loan application screening, evaluating the health of the enterprise, and improving the overall quality of the loan application. The program provides funding in two categories:

- Large scale window with a total corpus of USD 4 million providing loans of USD 50,000 to USD 150,000 to eligible Potential Financial Institutions (PFIs) for sub loans to formal SMEs, aiming to improve financial access, improve affordability, and maximise geographic coverage. These loans would be mainly for working capital and capital investment and would not be used for trade finance[77].

- Micro and small loans window with a corpus of USD 9 million for eligible PFIs who will extend microloans to micro-enterprises, individuals, and household enterprises range from USD 500 to USD 10,000. The facility will also provide loans of USD 10,000 to USD 50,000 to more formal enterprises.

Figure 19: Gargaara Facility in Somalia



Source: Gargaara

Assisting the federal government: Apart from enterprise-related activities, international agencies such as World Bank are also supporting the Federal Government of Somalia in (i) issuing a new currency, (ii) normalising financial relations with the global banking system, and (iii) developing the financial infrastructure of the country. These activities will play a vital role in enlarging Somalia's perception by foreign investors and create a conducive atmosphere for impact investments to flow into the country. The World Bank has a USD 7 million facility as part of the Somalia Capacity Advancement, Livelihoods and Entrepreneurship, through Digital Uplift Project (SCALED – UP). The project aims to strengthen various institutions such as the Central Bank of Somalia, Financial Reporting Centre, Ministry of Interior and New ID Administration Body, Ministry of Posts, Telecommunications and Technology & National Communications Authority[78].

ROLE OF IMPACT FUND MANAGERS (PE/VC) IN THE IMPACT INVESTMENT SECTOR IN SOMALIA

Impact Fund Managers have invested approximately USD 15 – 17 million in the last ten years in Somalia[79]. While many of these investments are small in ticket size (USD 5,000 – USD 50,000)[80], they are of the utmost importance to Somalia's entrepreneurship growth. Many of these investments by impact funds also go unreported due to investors' unwillingness to disclose and cultural factors that see fundraising as an enterprise's weakness.

Figure 20: Summary Table for Major Private Fund Managers in Somalia between 2005 and 2020

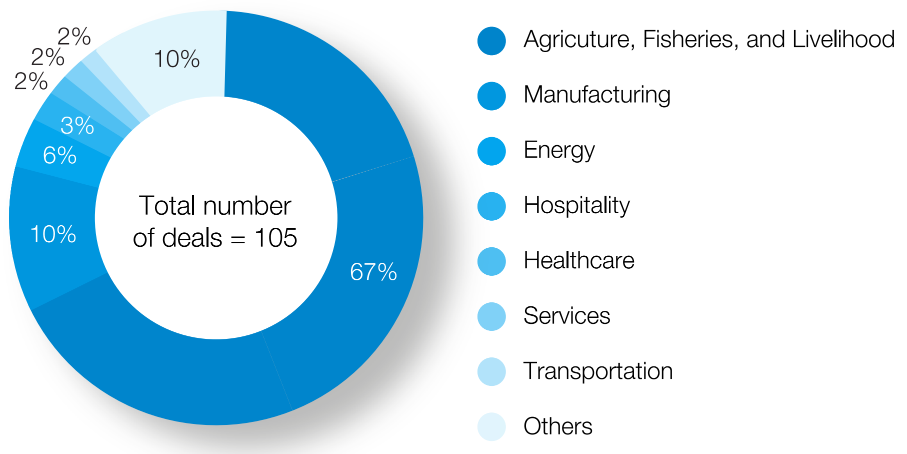
Name of the Investor	Capital Deployed (USD Mn) (2005 – 2020)	Sector Priorities	Key Investment Strategies
Nordic Horn of Opportunities Fund	*8 Mn*	*Agriculture, fisheries, dairy, dairy, healthcare, hospitality*	*Debt*
AgriFood Fund	*2.3 Mn*	*Agriculture*	*Debt*
Somaliland Youth Enterprise Fund	*0.55 Mn*	*Multiple Sectors*	*Debt*
Somalia Stability Fund	*NA*	*Multiple Sectors*	*Debt*
FCA Investments	*0.3 Mn*	*Agriculture*	*NA*

Source: Intellecap Analysis

SECTOR PRIORITISATION BY IMPACT FUND MANAGERS

Impact funds often invest in family-owned and operated enterprises, mainly in the agriculture, construction, fisheries, and livestock sectors. Private impact funds such as Shuraako receive capital from DFIs, including Norfund, IFU and invest in impact enterprises across the country.

Figure 21: Sector-wise investments by Private Impact Investors, by no of deals[81]



Source: Intellecap Analysis

Case Study 10: Nordic Horn of Africa Opportunities Fund

SME FINANCING

Nordic Horn of Africa Opportunities Fund

Nordic Horn of Africa Opportunities Fund is an impact fund targeting Somali SMEs. The fund provides Sharia compliant loans with a focus on job creation and empowerment of female entrepreneurs

The fund will focus on all regions of Somalia including Somaliland, Puntland, and South Central Somalia with a funding of USD 50,000 to USD 750,000 per enterprise for a period of five years.

- *Investor (s): Norfund, Norwegian Ministry of Foreign Affairs, Arsenault Family Foundation, and IFU (Investment Fund for Developing Countries)*
- *Fund Manager: Shuraako*
- *Amount: USD 8 million*
- *Investment Type: Debt*
- *Year of Investment: 2018*

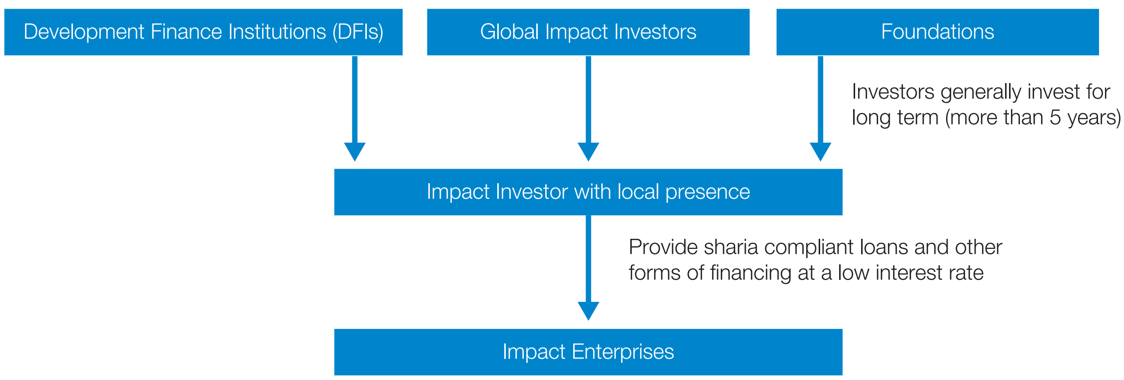
Source: Intellecap Analysis

INVESTMENT STRATEGIES OF IMPACT FUND MANAGERS

Our research identified that private impact funds often prefer debt for investments in Somalia. Islamic finance is the preferred form of investment by many enterprises and local investors. Equity financing still has a long way to go, as most investors are unsure of valuations and corporate governance practices.

• ***Co-Investment: Potential first-time impact funds look for local partners while investing in Somalia.*** Investors worldwide are wary of political, economic, and security challenges while considering investing in Somalia. As a result, many investors look for local partners while investing to mitigate the risks and challenges. Global DFIs such as Norfund and Investment Fund for Developing Countries (IFU) and the Arsenault Foundation has invested more than USD 8 million in Shuraako, a locally based impact fund with offices in Hargeisa, Garowe, and Mogadishu[82]. Shuraako has, in turn, deployed risk capital to finance SMEs with sharia-compliant loans and other self-liquidating structures with a focus on job creation, empowerment of female entrepreneurs, and improving the overall private sector. These loans are provided at a low-interest rate of 5 percent and aim to create an impact and momentum on the country's private sector landscape. Shuraako has financed over 100 enterprises primarily in fisheries, livestock, water supply, and healthcare, among others. The average ticket size ranged between USD 30,000 and USD 40,000 per enterprise[83].

Figure 22: Operational Model of Shuraako



Source: Intellecap Analysis

Somali Agrifood Fund, a seed-capital matching investment fund, focuses on driving diaspora and enterprise investments into Somali agriculture and rural businesses. The AgriFood Fund was intended for project sizes from USD 20,000 to USD 250,000, with the AgriFood Fund contributing between USD 8,000 and USD 100,000. The fund in total leveraged USD 2.28 million[84], of which Agrifood seed capital contributed 29 percent, diaspora contributed 43 percent, external investors contributed 7 percent, and the enterprises contributed remaining. The fund in total invested in 14 enterprises and had 21 investors in total.

Finnish Church Aid (FCA) investment is one of the few impact funds that directly invested in Somalia. While FCA Investments provides the necessary capital, it has partnered with USAID to provide technical assistance support for its investee companies. FCA has seven more deals in the pipeline (one in fisheries, one in agriculture, one in leather and tanning, two in livestock, among others). The entity is only looking to invest in the Somaliland region at the moment. They can invest in Puntland with the board's approval but cannot invest in the Mogadishu region without political risk insurance due to security concerns. It is also currently working with MIGA (Multilateral Investment Guarantee Agency) to provide the political risk insurance necessary to invest in Mogadishu[85].

Somalia Youth Enterprise Fund has been established to provide financing to micro-enterprises and individuals. The fund is intended to support 130 growth-oriented small businesses over four years. The fund exceeded its initial target and provided livelihood opportunities for 189 youth entrepreneurs from June 2015 to May 2017[86].

Case Study 11: Somali AgriFood Fund

AGRI-ENTERPRISE FINANCING

AgriFood Fund

Somali AgriFood Fund is a capital matching investment fund that is focused on driving diaspora investments into Somali agriculture and rural businesses.

The Fund was intended for projects ranging in size from $20,000—$250,000, whereby the AgriFood Fund contributes between $8,000—$100,000 in investment, matching investments from the Somali diaspora and other investors

- *Investor (s): IFAD and Somali Diaspora*
- *Amount: USD 1.8 million*
- *Investment Type: Debt and Grant*
- *Year of Investment: 2016*
- *Sector: Agriculture and Fisheries*
- *Status: Exited*

Source: Somali Agrifood Fund

Case Study 12: Somalia Youth Enterprise Fund

YOUTH ENTERPRISE FINANCING

Somalia Youth Enterprise Fund

The Somaliland Youth Enterprise Fund (SYEF) is intended for Somaliland entrepreneurs between the ages of 18—35. SYEF is also implemented by Shuraako with support from Silatech and Kaaba Microfinance Institution, and is intended for projects needing a capital infusion of between $1,000—$25,000.

These loans are provided in the form of Islamic finance (Murabahah loans) and are intended for entrepreneurs interested in starting their own businesses or funding existing businesses.

- *Investor (s): AFIF, a non-profit Qatari development program launched by Al Asmakh Charity Foundation, Silatech, Kaaba Microfinance Institution*
- *Fund Manager: Shuraako*
- *Amount: USD 550,000*
- *Investment Type: Debt*
- *Year of Investment: 2014*
- *Sector: Multi-Sector*

Source: Somali Youth Enterprise Fund

ROLE OF ANGELS, TRADITIONAL FIs & DIASPORA IN THE IMPACT INVESTMENT SECTOR IN SOMALIA

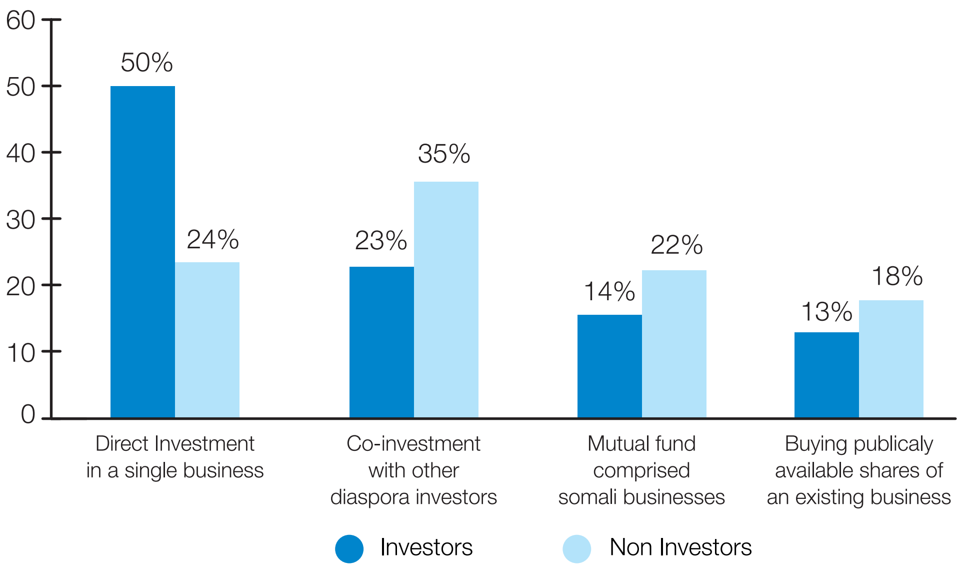
Angel investment is a nascent concept in Somalia, and the country doesn't have an organised angel network. Some of the Pan-Africa networks, such as Africa Business Angel Network and Venture Capital for Africa (VC4A), operate in the country to a limited extent. Institutions such as Somali Business Investment Network (SBIN) bring together global investors, including donors, the public sector, investment funds, individuals, and corporates seeking to invest in Somali enterprises. The network is mainly aimed at diaspora investors and invests via debt and equity.

Traditional capital provides, such as banks, provide limited capital for impact enterprises. They primarily lend to enterprises in the real-estate and trading sector. The interest rates range from 22 – 28 percent makes it unsustainable for enterprises in impact sectors. As such less than 20 percent of enterprises even apply for bank loans in Somalia[87]. Other financial institutions such as MFIs have a higher interest rate and majorly cater to small-scale enterprises such as retail and restaurants. These MFIs also operate in rural areas, while banks and other major financial institutions are only present in the country's urban areas.

Diaspora has contributed a significant portion towards the development of productive and high-impact sectors in Somalia. Around 34 percent of the diaspora remittances are classified as financial investments, including savings, infrastructure investments, and business investments. Only 2.8 percent of remittances are used for business investments. More than 50 percent of Somali diaspora investments have been in agriculture and livestock (from 2012 – 2015), with most investments ranging from USD 5,000 to USD 50,000. More than 60 percent of diaspora trust business partners, family, and friends for recommendations on investment opportunities[88].

While existing investors were more comfortable investing directly into a business in Somalia, others prefer to co-invest with diaspora investors as they are apprehensive of the risks. More than 55% of the diaspora are not aware of co-investment opportunities, and a lot is desired in engaging the diaspora for successful investments in Somalia. The majority of the diaspora population (39%) prefer investing in sustainable social enterprises, with only 29% investing to maximise their financial return[90]. Political instability, security, lack of contract enforcement & the rule of law, corruption, and inadequate banking system are some of the most pressing challenges for the diaspora to invest in Somali enterprises[91]

Figure 23: Investment options for Somali diaspora (2015)[89]

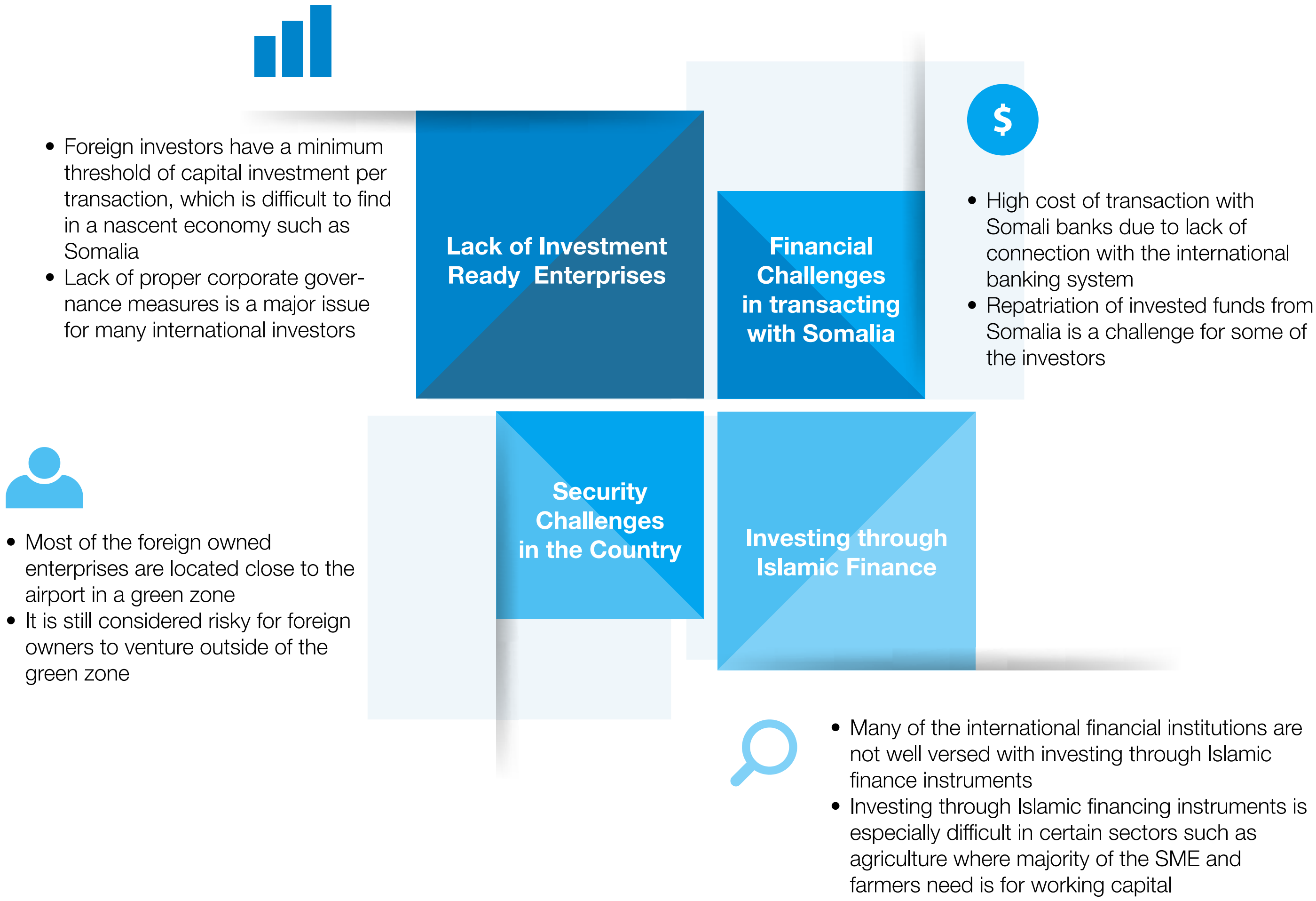


Source: Shuraako

CHALLENGES FACED BY IMPACT INVESTORS IN SOMALIA

Despite all the opportunities presented by Somalia enterprises, investors face many challenges in investing in the country.

Figure 24: Key challenges faced by investors in Somalia



Source: Intellecap Analysis

Investors often struggle to get investment-ready enterprises in the country. Lack of access to finance slows down the growth of the enterprise. As a result, most Somalia enterprises are small and require a small capital injection (usually less than USD 50,000) to expand their business. Most of the investors have a minimum ticket size requirement, and they find it difficult to source enterprises that meet their criteria. Investors often look at the cost of staff deployed, due diligence, risk of investment, and returns expected before considering an investment.

In many cases, these costs do not justify the investment of less than USD 2 million for many investors based outside Somalia. Some global investors such as IFC and FCA investments have reduced their minimum threshold for investing in fragile countries to meet the local needs and requirements. Local investors, such as Shuraako, can invest on an average between USD 30,000 to USD 40,000 due to their ability to minimise other costs and serve domestic enterprises.

The sourcing of enterprises is also a critical area of concern for investors targeting the country. In most developed and developing countries across the globe, sourcing of enterprises is done in one of three ways;

- Sourcing through incubators/accelerators
- Sourcing through pitch competitions, start-up conferences and other such start-up related events
- Direct sourcing through online applications and references

Many international investors do not have a permanent presence in Somalia and thus do not have a dedicated team to look at enterprises sourcing. As a result, they are unable to source high-quality enterprises from the country directly.

Somalia has a nascent network of ecosystem enablers such as incubators and accelerators. The first business incubator, Innovate Ventures, was launched in Somalia in 2016, and many of them have only been established in the last couple of years. ***As such, the network of these incubators is currently limited. Many enterprises are unaware of the role of incubators and accelerators, and as such, do not approach them for advisory and assistance in fundraising.***

Somalia has only a few notable enterprise events, including the Mogadishu Tech summit, Startupgrind and, Innovate accelerator program. These events bring together start-ups from all parts of Somalia and get them in touch with advisors, government stakeholders, and other interested parties. Some of these events also have pitch competitions that provide intensive training and award grants/equity funding. However, the reach of these events is still limited to major urban areas of Mogadishu and Hargeisa.

Investors are also concerned with the corporate governance practices of the enterprises. Most enterprises have not undergone financial training and are not exposed to the necessary corporate governance practices. As a result, many of these enterprises often do not have the requisite documents which are deemed essential for investors. Many enterprises lack financial and operational records and audited financial statements necessary to track an enterprise's progress and value the enterprise for equity/debt funding. Enterprises in the country also lack documentation on the source of funds, which is a major red flag for many foreign investors as this raises the possibility of an enterprise having been funded through proceeds from terrorism finance. It can expose the investor to scrutiny in their country of origin, resulting in investors staying away from these enterprises. Decision-making protocols that define individuals' hierarchy and roles within an enterprise are also largely lacking, which creates an ambiguity in leadership, leading to uncertainty within investors.

"Bringing funds in to the country and repatriating them from Somalia is the major challenge faced by many investors. Rest of the processes including registration and operation of an enterprise are relatively easy."

Country Head, Shuraako

"Major challenges to investors include a lack of fully functioning judiciary, minimal incentives to enterprises in the productive sectors, and difficulties in banking transactions."

Board Member - Gargaara

"Corporate Governance including audited financials and source of funds is a major challenge for investors."

Regional Director – East Africa, Norfund

"Investing through Islamic finance mechanisms, especially in the high-impact sectors of agriculture is the major obstacle along with the security challenges in Somalia."

Investment Manager – FCA Investments

Many global investors foresee challenges during the repatriation of funds. Only a few Somali banks and financial institutions are connected to the international banking system. While transacting with enterprises based in Somalia, it is essential to use banking intermediaries. These banking intermediaries are present in many countries, including Dubai, Turkey, Kenya, Djibouti. This extra layer of transactions adds to both the cost and time of financial transactions. Many of these intermediary banks often require lengthy documentation and take a minimum of 5-10 days to transfer funds, posing a significant challenge for both enterprises and investors. The transfer fee charged by these banks (primary and intermediary banks) is also high and can vary between 7 – 10 percent making it very costly to invest in Somalia[92]. The dollarisation of Somalia's economy is also a cause of concern among some investors. The Central Bank of Somalia is working with the World Bank to issue a new currency. The new currency's expected value is fuelling concerns among some investors as they feel it might devalue their investments. Even though the Somali government does not impose any restrictions on the repatriation of invested funds in Somalia, the host country banks immediately flag off a high-value transaction from Somalia. The intimation mandates the investor to provide a detailed explanation of the funds. The bank then faces challenges in verifying the information provided as it does not have a direct relationship with the Somalia banks. As a result, the concerned account has the risk of being sealed, thereby creating a massive hurdle for the investors.

The majority of Somali enterprises often require funds through an Islamic financing mechanism such as Murabaha and Musharakah. However, many international investors are not equipped to invest through such instruments. Consequentially, many investors are unable to invest in Somali enterprises. Investing through Islamic finance is also tricky for high-impact sectors such as agriculture, where most farmers and enterprises require working capital. Investors often find it easier to lend to enterprises through Islamic finance mechanisms for capital expenditure than lending for working capital purposes.

05

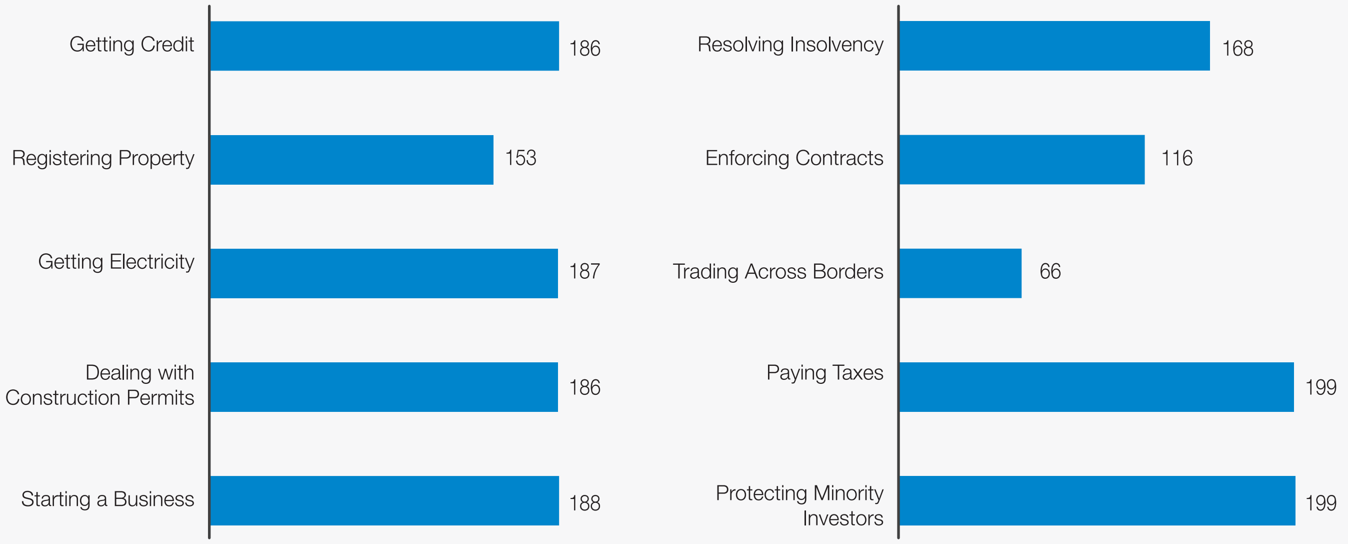
ENABLING ENVIRONMENT FOR SOCIAL ENTERPRISES AND IMPACT INVESTORS IN THE REGION

The assessment of the enabling environment for social enterprises includes reviewing the existing policies and regulations for investment in the country's impact sectors and private sector development. The section also covers the landscape assessment of Ecosystem Support Organisations (ESOs) in Somalia. The entrepreneurial support agencies' evaluation is based both on desk research and conversations with ESOs from the country.

OVERVIEW OF THE POLICY AND REGULATORY LANDSCAPE FOR PRIVATE SECTOR AND INVESTORS IN SOMALIA

Somalia has often lagged behind its peers in the World Bank's Ease of Doing Business rankings and was ranked 190 of 190 countries in 2020. While the country has fared reasonably well in parameters such as trading across borders and enforcing contracts-ranked 66 and 116th respectively, it, however, performed sub-optimally on parameters such as starting a business where it ranked 188 of 190 countries. It is mainly due to the number of days it takes to start a business (70 days compared to 21.5 days of Sub-Saharan average) and the cost of starting a business (198.2 percent of income per capita) compared to 36.3 percent Sub-Saharan average)[93]. The country also fares poorly in protecting minority investors, access to credit and electricity, and dealing with construction permits

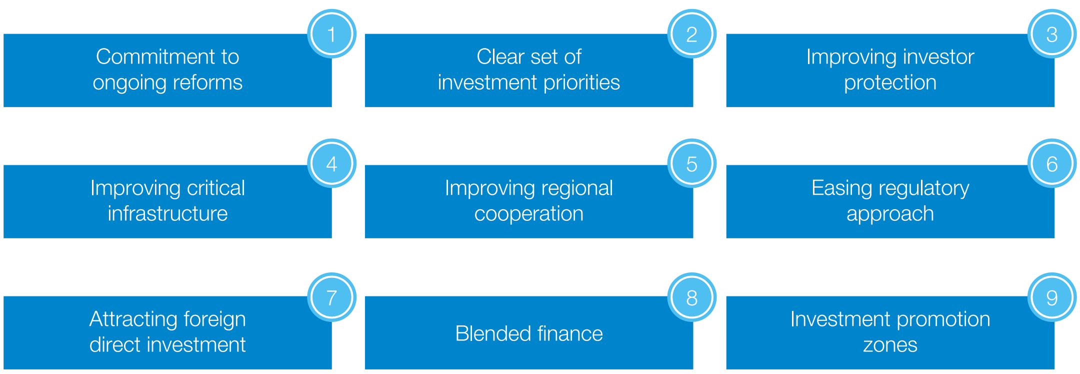
Figure 34: Ease of doing business parameters in Somalia, 2020



Source: World Bank

The Federal Government of Somalia has concluded the need for a comprehensive National Investment Promotion Strategy (NIPS) to attract and retain foreign investment to enhance growth, create jobs, and consolidate economic growth and development. The NIPS aims to increase investment by improving the investment eco-system while pursuing investment promotion by improving Somalia's image abroad, providing investment assistance to investors, and targeting specific priority investment sectors. The overall approach of Somalia in attracting foreign investment is summarised as follows:

Figure 26: Somalia's approach to improve private sector investment in the country



Source: Intellecap Analysis

The government has also ***identified several investment priority sectors,*** including livestock, farming, fisheries, energy, banking & financial services, information and communication technology, manufacturing, transportation and infrastructure, and services.

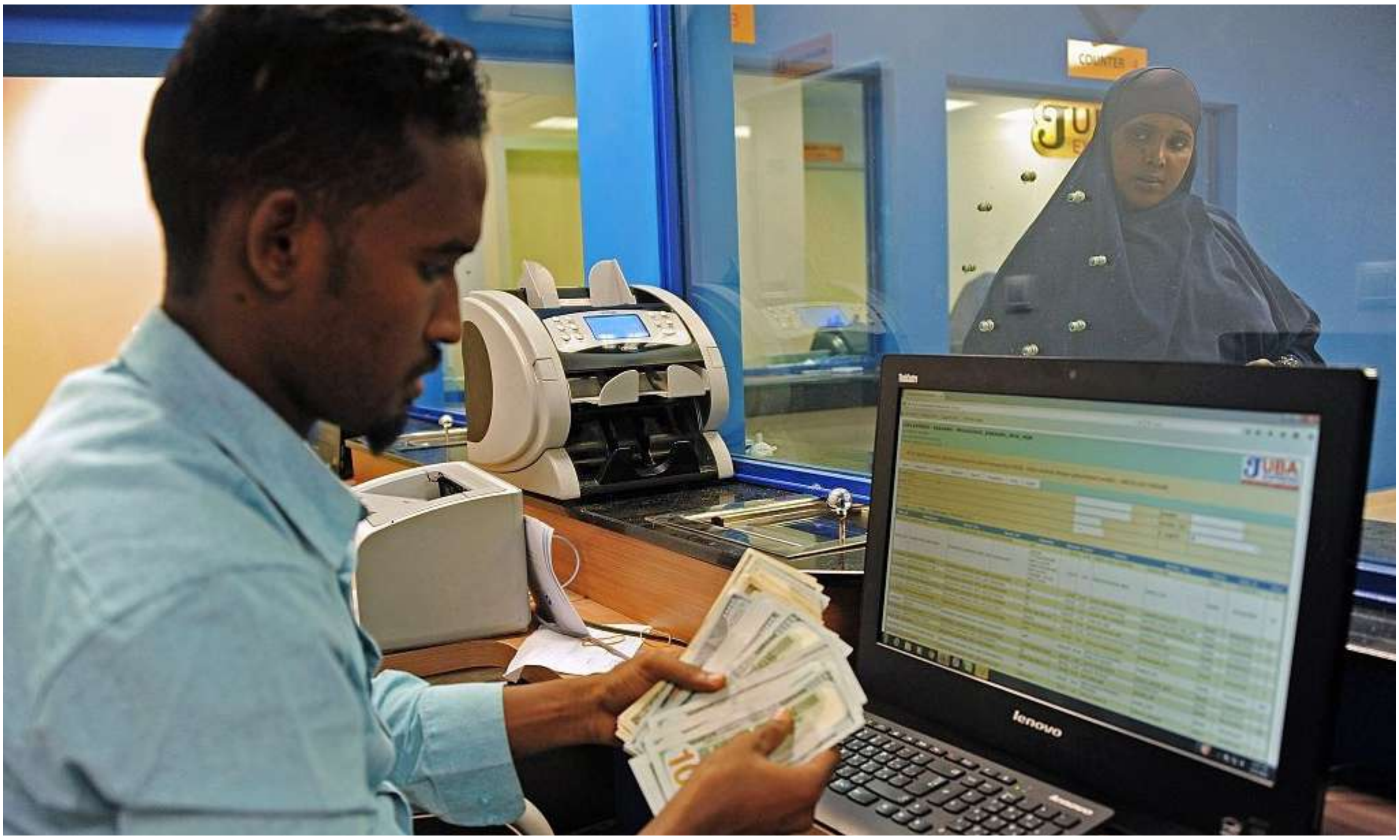
While there is no comprehensive system to protect investors, the Federal Government of Somalia is working on a framework that provides physical protection to investors' lives and property, governance safeguards, and corporate transparency requirements that reduce abuse risk. The Government aims to attract foreign and domestic investments with the launch of the framework. The ***Foreign Investment Law of 2015*** guarantees foreign investors treatment equal to that given to domestic investors, fair compensation in the event of expropriation, international arbitration of disputes between the investors and the Government, the right to remit profits and access to foreign exchange.

Critical infrastructure such as road networks, access to electricity and clean water are significant challenges faced by enterprises in Somalia. The Government often lacks funds for providing these services due to the lack of tax collection policies. The Government has proposed establishing the Somali Revenue Authority (SRA), supported by an appropriate legal framework for developing tax expertise and systems to evaluate imported goods properly. As part of SRA, the government also aims to introduce an efficient and corruption-proof clearing port system essential for a trade-dependent country like Somalia.

The Government is also ***building cooperation among the federal member states of Somalia and other countries in the African Union and worldwide.*** Somalia has bilateral Investment Treaties with Turkey, Germany, and Egypt. Negotiations of similar treaties are in the advanced stages with other countries. The country is also a member of the Inter-Governmental Authority on Development (IGAD) and recently obtained provisional membership in the Common Market for Eastern and Southern Africa (COMESA) with several conditions to fulfil before resuming full membership. Somalia is a member of the Arab League and the Organization of Islamic Cooperation (OIC). Somalia is not a member of the World Trade Organization (WTO)[95]. The country is aiming to increase FDIs in the impact sectors. As part of this push, the Government aims to create Investment Promotion and Special Economic Zones. SOMINVEST also provides tailor-made consulting and site selection and site visit support and legal services to prospective investors.

The Government of Somalia recognises impact investors as critical to the country's private sector's long-term growth. Still, it is yet to create a framework to differentiate impact capital from commercial capital. The government is also working to accelerate blended finance by having conversations with various DFIs and donors but is yet to formulate basic legislation and regulatory controls for the same.

Impact monitoring is an essential aspect of the National Investment Promotion Strategy. The plan aims to develop a macro-economic and enterprise dashboard with baseline data.



The mid (interim) and end-term targets will be established as part of the annual planning and reporting process. Outcome and impact level indicators will be tracked by the Ministry of Planning, Investment, and Economic Development (MoPIED) through its Directorate of Monitoring and Evaluation.

While the Government of Somalia has started focusing more on the private sector and providing requisite policy and infrastructure provisions, it is a work in progress and a lot of effort needs to be invested for uplifting the micro, small, and medium enterprises. The government and the central bank need to rapidly conclude its conversations with various stakeholders and launch the official currency of Somalia which will provide the central bank with monetary policy controls. The government also needs to focus on transparency in providing information regarding the rules and regulations to foreign investors. While Somalia has many of the local laws for governing enterprise operations, implementation of these laws need to be strengthened at the ground level for rapid growth of the industry.

ECOSYSTEM SUPPORT FOR SOCIAL ENTERPRISES

ESOs in Somalia help social entrepreneurs streamline their operations, document their journey, and secure grants and other financial assistance.

They also provide enterprises with technical assistance and market access for goods and services. Services are offered in conjunction with various government and non-government programs such as GEEL, SCORE, and others. Enterprise Support Organisations and Foundations such as Oxfam have invested USD 4.5 million[96 97] to provide tailored business development services to 12 selected SMEs with strong potential for employing women and youth.

Almost all of the enterprise support organisations, including incubators and accelerators, are sector agnostic. Most of these support organisations work with enterprises looking to solve society's most pressing problems, including access to basic goods and the provision of essential services. Incubators and accelerators primarily focus on providing enterprises with knowledge and networks to enable them to raise funding, search for markets within and outside Somalia, documentation processes to enable grant funding.

Incubators and accelerators have inside knowledge of enterprise workings and are best placed to invest in promising businesses. Some incubators and accelerators such as Innovate Ventures, Harhub and others also invest in their incubates. The amount invested by these incubators and accelerators is generally less than USD 15,000 and is meant to give them a first-mover advantage in promising start-ups.

Crowdfunding is slowly starting to pick up in Somalia. Shaqadoon, Premier Bank, Oxfam, and Spark enabled the Tarmiye Crowdfunding Platform launch in 2019. The platform aims to provide USD 1 million for Somali entrepreneurs through crowdfunding and create more than 1,000 jobs in the process. The fund does not have any collateral requirements for funding requirement below USD 5,000 and has a 90 day grace period for the loans' payback[98].

CHALLENGES FACED BY ESOs IN SOMALIA

- ***Challenges in offering services across the country:*** Almost all significant ESOs are present in the major towns, i.e. Mogadishu and Hargeisa, limiting their services to other less developed regions. Setting up offices in other regions is often considered unviable due to the limited infrastructure available in those regions.

- ***Lack of support from Government and Donors:*** There is often no support offered, either in monetary or technical means by the Federal Government. Government support will encourage more enterprises to avail ESOs' services resulting in a larger pool of investible enterprises. The donor community often focuses on supporting entrepreneurial programs and enterprises directly and have a narrow focus on helping the ESOs community.

- ***Lack of networking initiatives in the country:*** Many enterprises often have to travel outside the country to network with potential investors, donors, and other relevant stakeholders. It diminishes the role of enterprise support organisations expected to provide access to potential investors and capacity building.

06

RECOMMENDATIONS ON INNOVATIVE IMPACT INVESTMENT MODELS FOR PROMOTING PRIVATE SECTOR IN SOMALIA

The financing models/instruments currently available in the country are primarily tailored for short-term borrowing and need to be backed by assets/collateral. Debt (using Islamic finance) is the leading financial instrument used in Somalia. Some of the critical shortcomings of the current financing instruments in Somalia include the following:

• Credit guarantees do not address the issue of lack of capital. The entire formal lending portfolio of banks and financial institutions in Somalia was a little over USD 110 million in 2018[99], which is insufficient for developing the country's private sector. Direct lending to enterprises in the impact sectors is the need of the hour, which can be achieved through investments in a local fund/fund with local operations.

• To facilitate loans to the impact sector/SMEs, DFIs provide low-interest loans to banks and financial institutions. However, banks still provide loans at high-interest rates (22 – 26 percent) to SMEs, which is unsustainable for enterprises/sectors with long repayment tenures. Many of the bank branches outside of Mogadishu and Hargeisa are unaware of the facility and often do not take the risk of lending to enterprises in the impact sectors

Given the lack of credit history, a credible national currency, and negative investor perception, the country needs innovative financing mechanisms to grow private sector enterprises. Some of these innovative models which can mobilise more capital for Somalia include:

Figure 27: Recommended Financial Models for Financing Enterprises in Somalia

Proposed Model	Description	Pros	Cons	Examples
Diaspora Bond	*Diaspora purchases bonds for investing in the home country. These bonds can be sold at a premium and can be raised for a longer duration*	*Large diaspora sending in more than USD 1.4 billion in remittances (2018)*	*Limited success in fragile and conflict affected countries across the globe*	*Kenya, Senegal, Ghana, Nigeria, and Rwanda have all issued diaspora bonds*
Outcome-Based Financing	*Funding is based on certain pre-agreed milestones*	*Investors are assured of the progress of the enterprise/ initiative*	*Lengthy and laborious process which involves constant presence on the ground*	*Outcome Based Financing for Educate girls campaign in India*
Guarantee Backed Blended Debt Fund	*Combines capital from various sources including grant, equity, and debt sources. The capital is backed by guarantees from donors, corporates, foundations and others*	*Low-cost debt available to impact enterprises*	*Structuring of the fund is a complex process and needs approval of many stakeholders*	*IIX Women's livelihood bond with DCA and DFAT as the guarantee providers*

Source: Intellecap Analysis

A. DIASPORA BONDS

Somalia has one of the largest diaspora populations in Africa. In 2018, the community sent more than USD 1.4 billion in remittances[100]. Remittances augment household income and create a buffer against the shocks faced by a fragile country. These remittances are spent on consumption (majorly on education and healthcare) and household level investments (mainly in residential construction). The Somali diaspora can be leveraged to attract investments into the private sector through the issuance of bonds.

Figure 28: Examples of diaspora bonds in other countries

Traditional diaspora bonds have been in existence since 1951 when Israel established the Development Corporation for Israel (DCI) to raise foreign exchange for the state of Israel from Jewish diaspora abroad. Israel has issued diaspora bonds annually since 1951, and the issuance is not limited to the diaspora and is open for other individuals and institutions[101]. Other countries such as India and Lebanon have issued diaspora bonds in times of need to shore up their balance of payments and get through difficult times. In Africa, Ethiopia was the first country to issue diaspora bonds in 2008 to help finance the Ethiopia Electric Power company and in 2011 to finance the construction of a dam on the Blue Nile. Both the issues did not meet expectations and failed to raise the required financing through the diaspora. The primary reason for this was presumed to be a lack of expatriates trust in the government. Kenya also issued its first bond in 2009, raising more than EUR 164 million for transport, energy, and water projects[102]. Other countries in Africa, including Senegal, Ghana, Nigeria, and Rwanda, have also issued diaspora bonds to support development projects in their countries. Nigeria had had the most successful diaspora bond issuance of any country in Africa when they raised more than USD 300 million to fund infrastructure projects[103]. The issue was over-subscribed and has paved the way for similar diaspora bonds by other countries of Africa.

Diaspora bonds are long-dated securities that can be redeemed only upon maturity. Diaspora bonds in Somalia can be modelled on the Islamic finance concept of 'Sukuk', asset-backed securities that provide investors with a share of profit associated with such issuance proceeds. The diaspora purchases of bonds issued by their country of origin are driven mainly by a sense of patriotism and the desire to contribute to their home country's development. ***Some of the significant advantages of issuing diaspora bonds are as follows:***

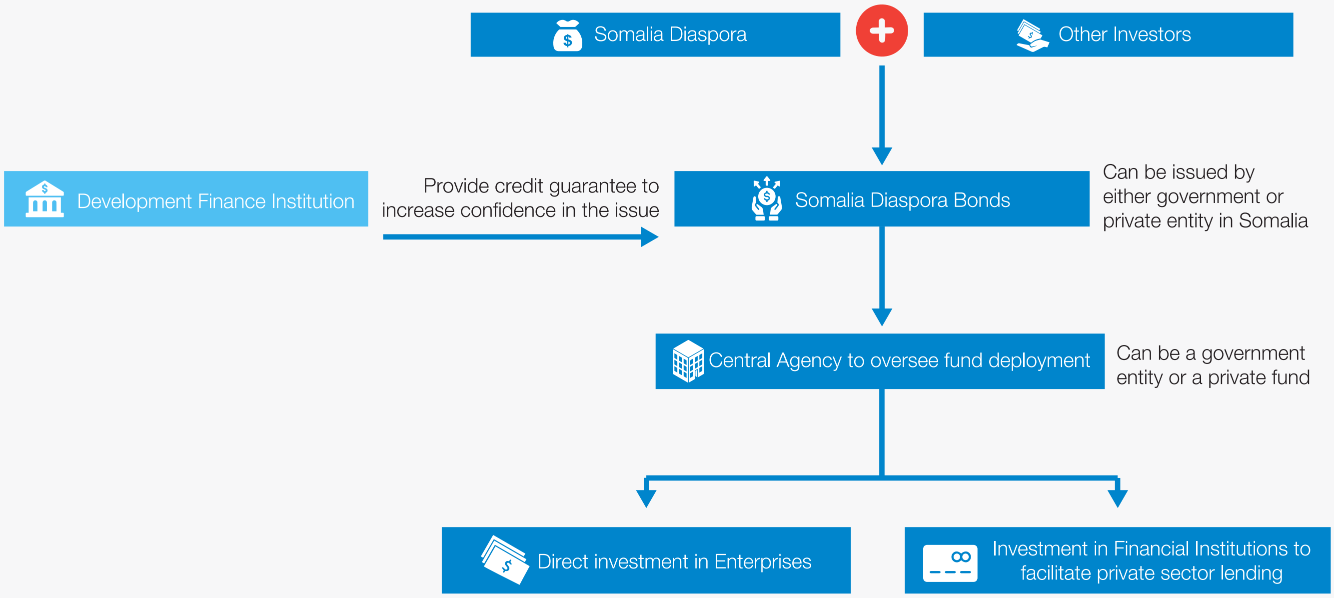
- As a sense of patriotism drives these bonds, they can be sold at a premium, and since most of these bonds cannot be redeemed before maturity, investments can be raised for a longer duration of time.
- They can provide a conduit for remittances to flow back into projects and businesses that stimulate national growth with a positive impact
- These bonds can be used to improve the overall infrastructure of Somalia and invest in private sector enterprises directly or through formal financial institutions.
- Diaspora bonds can also help Somalia improve its sovereign credit rating as they provide a reliable source of funding in good and bad times.

IMPLEMENTATION MODEL: DIASPORA BOND

Diaspora bonds also provide an opportunity for diversifying risk for the investor. The worst-case default risk associated with diaspora bonds is that the issuing country would not be able to make repayments in the currency of issuance and resort to repayments in the local currency. Most diasporas have current or contingent liabilities in their home country and may not be against receiving repayments in the local currency. The diaspora bonds are also the most relevant and effective when targeted at the first generation of immigrants with an intimate connection to the motherland. It is where Somalia has a distinct advantage as many of the country's diaspora have escaped the civil war and are eager to contribute to the development of the country.

The funds raised from diaspora bonds can be used for investments in asset-heavy enterprises such as solar energy, fisheries, logistics, etc. To raise funding from the diaspora, these enterprises can leverage assets as collateral. The diaspora funds can be used as capital for purchasing assets, which can then be hypothecated for the bonds' duration. The prime sectors for investment by the Somali diaspora would be the fisheries and energy sector. Somalia has the longest coastline in Africa and has an abundance of fish stocks. Fishers do not have the latest fishing vessels to compete with international fishing entities and end up catching meagre amounts of fish in comparison. Investment in fishing vessels and subsequent processing units would

Case Study 13: Diaspora Bond for Somalia



Source: Intellecap Analysis

be very profitable for diaspora investments. The energy sector also needs a lot of long-term investments from the diaspora to reduce the cost per unit and increase the competitiveness of various sectors. Kenya issued a similar diaspora bond for investments in transport, water, and energy sectors to the tune of USD 228 million in 2009[104].

ADVANTAGES OF DIASPORA BONDS

The bonds would be an excellent investment for the Somali diaspora. The interest rate received from investment in Somalia would generally be more than the returns in their country of residence as enterprises are willing to pay up to 15 percent per annum. Since the money would be invested in US Dollar, no premium needs to be paid for hedging the currency at the moment. The funds raised by the issuance of diaspora bonds can be parked in a central agency to oversee fund development. The central agency can be a government entity or an investment fund responsible for investments in impact enterprises. These investments can be at lower interest rates for the enterprises than the prevailing market rates providing the investees with much-needed funds for growth. The central agency can either invest directly in businesses or invest in financial institutions such as banks to on-lend to impact enterprises.

LIMITATIONS OF DIASPORA BONDS:

On the other hand, raising funds through diaspora bonds presents a challenge in coordinating with the diaspora in various countries, communicating the requirements and advantages of investing in the bonds, and guaranteeing their investments' safety. Many of the diaspora bonds raised in the past have been with the government's extensive involvement because of the mandate to include them as one of the key stakeholders.

B. OUTCOME-BASED FINANCING

Somalia faces challenges on many social indicators, and impact enterprises are working towards addressing these challenges. These impact enterprises are often constrained by the lack of capital, which is very difficult to access. As a result, many of these enterprises are only able to deliver a limited impact on the ground. These enterprises need low-cost investment and need to be held accountable for the impact they can generate.

Also known as results-based financing, outcome-based financing instruments introduce checks and balances, encourage better corporate governance, transparency, and enhanced accountability across enterprises. It is achieved by linking payments/investments/grants directly to performance and outcomes. A detailed monitoring and evaluation system is set up by the fund/facility to monitor the enterprise's progress and invest as per the progress.

Healthcare, education, public administration, water and sanitation, and energy and extractives have been the largest beneficiaries of outcome-based financing globally, with more than 85 percent of the investments. Sub-Saharan Africa has been the largest recipient of these investments (42 percent)[105]. Somalia lags in all of these sectors and would benefit significantly from Outcome-Based Financing.

Case Study 14: Outcome-Based Financing

1. The fund decides on the impact it wants to achieve through its investments in Somalia
2. Enterprises design a business plan to maximize their performance on the impact and financial parameters
3. To guarantee transparency and accountability, the enterprise performance is constantly monitored and evaluated
4. The enterprises are interviewed and the impact parameters are verified
5. Enterprises are paid according to the verified performance outcomes

Source: Intellecap Analysis

In outcome-based financing, the development funder signs an agreement with the incentivised agent/enterprise and all or a part of its funding is contingent on the achievement of measurable and pre-defined results. An independent evaluator verifies the extent to which results have been achieved. The fund pays the enterprise upon verifying the achieved results as per conditions laid out in the agreement.

Figure 29: Example of outcome-based financing

UBS Optimus Foundation (the investor) invested in Educate Girls (the service provider/enterprise) to increase enrolment, retention, and learning of marginalised boys and girls in Rajasthan, India. The impact bond also involved the Children's Investment Fund Foundation (CIFF) as the results funder
As part of the agreement, UBS Optimum Foundation provided upfront capital to Educate Girls. Upon verifying the achievements, CIFF would pay back UBS Optimum Foundation their initial investment with a return, depending on Educate Girls' performance. UBS shares a portion of the results payment with Educate Girls, incentivising the service provider for delivering on the contract.

ADVANTAGES OF OUTCOME-BASED FINANCING

Outcome-based financing can be one of the most promising financing instruments for Somalia. Due to the high cost of funding from Somalia's formal financial institutions, it makes follow-on funding very expensive for enterprises in the impact sectors. As a result, enterprises would want access to concessional capital as part of an outcome-based financing mechanism. Many of the DFIs and impact investors such as Cordaid, World Bank, and others have already implemented outcome-based financing across Sub-Saharan Africa countries with promising results; they can replicate the same in Somalia.

Outcome-based financing also allows for the constant monitoring of the enterprises, thereby increasing their efficiency and efficacy. This monitoring would be done either directly by the investors or through enterprise support organisations, which allows for timely interventions in times of need.

LIMITATIONS OF OUTCOME-BASED FINANCING

The impact measurement on-ground is a time consuming and costly process. The investors have to rely on the assessment of ESO to evaluate the enterprises. The impact measurement framework which needs to be developed for the process needs to encompass many of the on-ground realities in a fragile country like Somalia. Failure to do so would undermine the process of quantifying the impact created by the enterprises.

C. GUARANTEE-BACKED BLENDED DEBT FUND

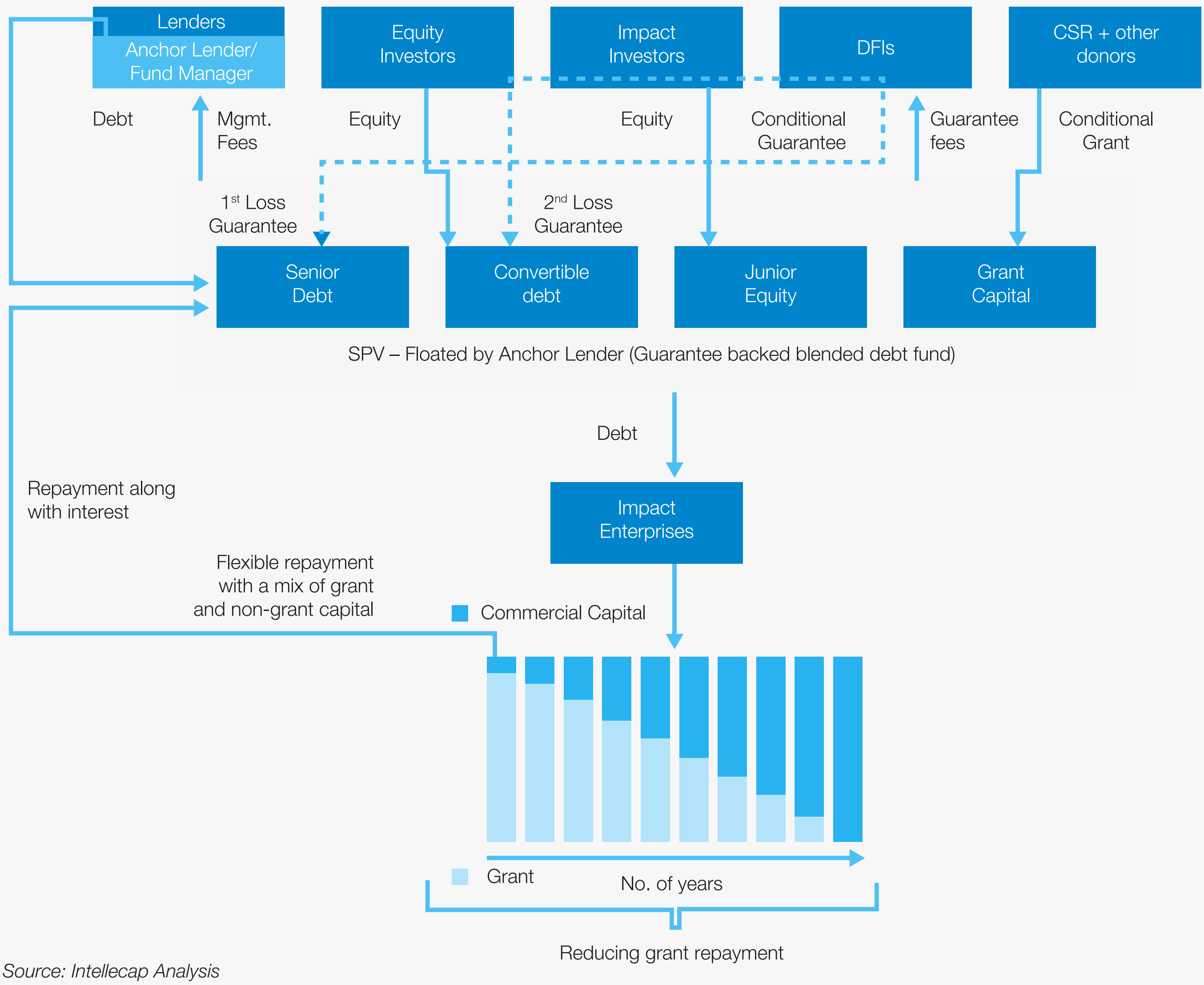
A guarantee-backed debt fund combines capital from various sources, including grant, equity, and debt capital. The structure is also enabled by two guarantees provided by donors, corporates, foundations and others. Guarantee-backed blended debt funds are essential for fragile countries such as Somalia as many investors look for investment assurances from DFIs and donor agencies. This type of blended fund would enable enterprises in Somalia to grow their business without high-interest rate payments, rigid payment structures, and longer repayment tenures. The double guarantees for the fund would provide assurances of payment and encourage more impact investors and traditional equity investors to invest in the fund to help impact enterprises across various Somalia sectors.

A group of lenders (including an anchor lender who can become the fund manager), equity, and impact investors, donors, and corporates come together to enable a Special Purpose Vehicle (SPV) structure. The lenders (Banks and Non-Banking Financial Companies (NBFCs) assume the senior debt position and pool in debt capital to the SPV. The debt capital is provided at market rates and can be raised through external commercial borrowings (ECBs). Commercial investors invest in convertible debt instruments that convert to equity after an agreed-upon time, while impact investors invest in junior equity on relatively lower commercial terms. The funds provided by donors and corporates are used to give a guarantee to the SPV. They can also be utilised to lower the interest rates, in case the cost of borrowing from Banks and NBFCs is on the higher end. A first loss guarantee can be used to cover the first tranche of losses (for instance, 80% of the losses up to 10% of the portfolio) and is provided mainly to capital provided by lenders. In contrast, the second loss guarantee can be used to cover the second tranche of losses (for instance, 80% of losses up to the next 20 – 30% of the portfolio) and is provided mainly for convertible instruments made by equity investors. The impact enterprises need flexibility in repayment as most do not have a stable, consistent, and predictable cash flow. The repayment Equated Monthly Instalments (EMI) is broken into two parts based on the source of funds, commercially available capital and grant capital. This structure enables the impact enterprises to pay only for the commercial capital component of the EMI; the remaining component is a grant and need not be repaid to the SPV. The grant component is the maximum in the first instalment and reduces gradually with constantly increasing commercial component.

Figure 30: Example of Guarantee-Backed Blended Debt Fund

There have been few investments using instruments similar to this, including the IIX women's livelihood bond in which a guarantee of 50% of the loan principal and USD 500K first-loss tranche was provided. USAID's Development Credit Authority (DCA) acted as the guarantee provider, Department of Foreign Affairs and Trade (DFAT) provided guarantee via a grant to USAID's DCA, and Impact Investment Exchange (IIX) provided the first-loss tranche[106].

Case Study 15: Guarantee Backed Blended Debt Fund



Source: Intellecap Analysis

ADVANTAGES OF A GUARANTEE-BACKED BLENDED DEBT FUND:

A guarantee-backed blended debt fund provides capital to impact enterprises at lower interest rates than the prevailing market rates. This helps the enterprise expand its business and create an on-ground impact on a larger scale. A combination of debt and equity leads to a robust balance sheet, providing the enterprise with an opportunity to raise any form of capital in the future. The fund's flexible repayment options also help assist the impact enterprises in case of force major events.

LIMITATIONS OF A GUARANTEE-BACKED BLENDED DEBT FUND:

The complex structuring of a guarantee-backed blended debt fund is one of its most critical limitations. It takes a lot of effort to coordinate with various stakeholders, including local financial institutions, equity investors, impact investors, DFIs, NGOs, and donors. The repayment of the investments also has to be divided among various investors and needs many complex accounting and management skills, which are difficult to obtain in Somalia.

PRINCIPLES FOR IMPACT INVESTING IN SOMALIA

Despite investment interest in Somalia, many investors find it challenging to invest in the country. Conflict-related fragility presents both challenges and opportunities for investors. On the one hand, security and financial restrictions make it difficult to operate businesses in the country; on the other hand, Somalia's developing economy presents investors with a massive opportunity in terms of return on investment. Some of the principles and recommendations for investing in Somalia are as follows:

• ***Understand and prepare for investments in conflict areas:*** Investors should weigh the adverse effects of conflict on their investments against the expected positive impacts of the investment. Investors should start by investing with a local partner who understands the country's economy, politics, and security situation. Many global DFIs and donors, including Norfund, IFAD, IFU, have invested in Somalia through Shuraako, which has a local presence in the country.

• ***Customise financial products to suit the local needs of entrepreneurs:*** Currently, enterprises across Somalia are either using personal capital, borrowing money from informal sources, MFIs, or banks to fulfil their business financial needs at an extremely high cost. Investors need to understand Somalia enterprises' needs, requiring low-cost working capital with short processing time and offering suitable financial products accordingly. Specific focus should be on providing women-specific financial products as they manage most of the country's enterprises. Instruments such as collateral-free loans provide alternatives to traditionally accepted collateral such as gold, purchase contracts, savings balances as a guarantee, and warehouse receipts, revolving credit. Enterprises also require equity investments through which investors will offer suitable guidance and market connections for long-term success.

• ***Invest for the long term:*** Investors looking to invest in Somalia need to invest for a longer duration than they would have invested for in the developing and developed markets. This is due to Somalia enterprises' challenges and the disruptions caused to operations due to these challenges. Investors should start small and invest in stages after gaining knowledge and experience of various enterprises and sectors in Somalia. Investments in impact sectors have to be based on sectoral needs and requirements. Prime sectors for investment would be fisheries, agriculture, and healthcare. Investments in renewable energy and agriculture need to be for more than 5 – 7 years as the enterprise would need that time to consolidate, scale-up, and deliver results. On the other hand, financial services investments can be for 3 – 5 years, coupled with technical assistance provision.

• ***Use blended finance instruments to mitigate investment risks:*** A combination of commercial and grant capital would be the most suited for Somalia's investments. It would decrease the risk for commercial investors and encourage more investors to invest in Somalia's enterprises. The grant capital can be used to reduce lending rates, provide credit guarantees to lenders, and invest in technical assistance programmes for enterprises' growth. Somali Agri Fund is a perfect example of a blended structure where capital from grants, diaspora, local investors, and the enterprise is combined.

• ***Utilise staff with experience of operating in fragile and conflict countries and hire local staff for additional intelligence:*** Operating in fragile countries needs experience in assessing investment risks, political situation, operating risks and others. Investors thus need to hire local personnel to provide them with on-ground intelligence to mitigate risks and increase the sourcing rate of quality enterprises. The GEEL project had hired local personnel and consulting firms such as Amal Consulting to assist them with on-ground operations and identification of suitable enterprises.

• ***Help create international markets for Somalia's goods and services:*** Purchasing power in Somalia is limited. As such, investors should help develop new markets for goods produced by Somali enterprises. It allows enterprises to navigate through conflict situations when the purchasing power of the citizens of Somalia goes down.

Case Study 16: Rikweda Fruit Processing Company (Indicative example of successful investment in a fragile country and the impact created by the investment)

AGRICULTURE ENTERPRISE

Rikweda Fruit Processing Company

The Rikweda Fruit Processing Company aims to help Afghanistan increase export of raisins. IFC has invested USD 3 million in financing to help Rikweda build a greenfield raisin processing plant with a production capacity of 15,000 tons per annum. IFC's investment has also been supported by Global Agriculture and Food Security Program (GAFSP) which has provided a first-loss guarantee of up to USD 1.25 million.

The project has improved livelihoods of approximately 3,000 smallholder farmers in remote rural areas by strengthening their access to the market. The new raisin processing plant has created a total of 50 full time jobs. The project will also help avoid up to 3,000 tons of carbon dioxide equivalent emissions per year as the adoption of commercial-grade processing standards will reduce losses of grapes.

- *Investor (s): IFC*
- *Amount: USD 3 million*
- *Investment Type: Debt*
- *Year of Investment: 2017*
- *Sector: Agriculture*

Source: IFC

In addition to financial commitments, support enterprises with technical assistance, capacity building, and other essential services: Most of the impact enterprises in Somalia are unaware of the rules, procedures, technologies, and governance mechanisms necessary to operate an enterprise. As a result, many of these enterprises fail to raise funding and expand their operations. Investors also need to invest their time in assisting these enterprises with technical assistance to improve productivity, corporate governance to streamline operations, accounting practices to raise funding, and HR practices to acquire the right talent.

The Government of Somalia needs to take a lead in instilling confidence among both investors and entrepreneurs to invest in Somalia. The Federal Government of Somalia needs to provide concrete assurances to various stakeholders including investors, entrepreneurs, NGOs, DFIs, donors, and diaspora across the globe in terms of efforts made to increase access to electricity, prevalence of rule of law, political and monetary stability, and to improve the overall ease of doing business across the country.

ANNEXURE

ANNEXURE 1: PRIMARY INTERVIEW LIST

S. No	Country	Organisation	Organisation Type
1	Somalia	Shuraako	Investor
2	Somalia	BiD Network	ESO
3	Somalia	USAID	Investor
4	Somalia	DFC	Investor
5	Somalia	Federal Government of Somalia	Regulatory
6	Somalia	Response Innovation Fund	ESO
7	Somalia	Onward Endeavour	Impact Enterprise
8	Somalia	Norfund	Investor
9	Somalia	Shaqadoon	Impact Enterprise
10	Somalia	FinnFund	Investor
11	Somalia	Somalia Bankers Association	Regulatory
12	Somalia	Irise hub	ESO (Incubator)
13	Somalia	Harhub	ESO (Incubator)
14	Somalia	IFC	Investor
15	Somalia	World Bank	Investor
16	Somalia	Solargen Technologies	Impact Enterprise
17	Somalia	FCA Investments	Investor
18	Somalia	SIMA Fund	Investor
19	Somalia	Office of the President	Regulatory
20	Somalia	Taam Fishing	Impact Enterprise
21	Somalia	OGOW EMR	Impact Enterprise
22	Somalia	Nuros9 Solutions	Impact Enterprise
23	Somalia	Zaika Fishing	Impact Enterprise
24	Somalia	Hirad International Fisheries	Impact Enterprise
25	Somalia	SOMINVEST	Regulatory
26	Somalia	Abu – Najiib Fishing Co	Impact Enterprise
27	Somalia	Afri-tech	Impact Enterprise
28	Somalia	Aragsan Organics	Impact Enterprise
29	Somalia	Dalbile Landscaping and Agricultural Services	Impact Enterprise
30	Somalia	Dalbo Food	Impact Enterprise
31	Somalia	Durdur onion production	Impact Enterprise
32	Somalia	European Pharmacy, PolyClinic and Diabetic Center	Impact Enterprise
33	Somalia	Ilbarwaaqo Milk	Impact Enterprise
34	Somalia	Kaaba MFI	Impact Enterprise
35	Somalia	Kaafi community health center	Impact Enterprise
36	Somalia	Khayria Farm	Impact Enterprise
37	Somalia	Plastic Venture	Impact Enterprise
38	Somalia	Real Video	Impact Enterprise
39	Somalia	Ridwa Nutrition Center	Impact Enterprise
40	Somalia	Saami	Impact Enterprise

ANNEXURE 1: PRIMARY INTERVIEW LIST

S. No	Country	Organisation	Organisation Type
41	Somalia	SOGI Foods Complex	Impact Enterprise
42	Somalia	SomFarm Fresh	Impact Enterprise
43	Somalia	Somsite	Impact Enterprise
44	Somalia	Super Services	Impact Enterprise
45	Somalia	Wadani Milling factory	Impact Enterprise
46	Somalia	Hargeisa Diabetic Centre	Impact Enterprise
47	Somalia	Cayn Solar	Impact Enterprise
48	Somalia	Tethered Up	ESO (Incubator)

FOOTNOTES - EXECUTIVE SUMMARY

[1] *International Monetary Fund, https://www.imf.org/en/News/Articles/2019/08/01/pr19309-somalia-imf-executive-board-concludes-2019-article-iv-consultation-with-somalia*

[2] *United Nations High Commissioner for Refugees (UNHCR), 2019, https://reporting.unhcr.org/somalia*

[3] *Somalia High Frequency Survey, World Bank, December 2017, Wave 2; https://microdata.worldbank.org/index.php/catalog/3181/get-microdata*

[4] *ODA is the flow of official financing administered with the promotion of the economic development and welfare of developing countries as the main objective. Humanitarian aid is the aid and action designed to save lives, alleviate suffering and maintain and protect human dignity during and in the aftermath of emergencies, while development aid is for uplifting the economy of the country. ODA includes humanitarian as well as development aid*

[5] *Aid Flows in Somalia, Federal Government of Somalia, Ministry of Planning, Investment, and Economic Development, 2019; https://reliefweb.int/sites/reliefweb.int/files/resources/Aid-Flows-in-Somalia-2019-ENGLISH.pdf*

[6] *Somalia National Development Plan 2020 to 2024, Ministry of Planning, Investment and Economic Development; http://mop.gov.so/wp-content/uploads/2019/12/NDP-9-2020-2024.pdf*

[7] *Expected 40 percent drop in remittances threatens Somalia's most vulnerable, Medium, June 2020; https://medium.com/@UNmigration/covid-19-cuts-remittances-for-vulnerable-somalis-d3b6fdba04a3*

FOOTNOTES 1-6

[1] *Somalia High Frequency Survey, World Bank, December 2017, Wave 2; https://microdata.worldbank.org/index.php/catalog/3181/get-microdata*

[2] *United Nations High Commissioner for Refugees (UNHCR), 2019, https://reporting.unhcr.org/somalia*

[3] *ibid*

[4] *Expected 40 percent drop in remittances threatens Somalia's most vulnerable, Medium, June 2020; https://medium.com/@UNmigration/covid-19-cuts-remittances-for-vulnerable-somalis-d3b6fdba04a3*

[5] *International Monetary Fund, https://www.imf.org/en/News/Articles/2019/08/01/pr19309-somalia-imf-executive-board-concludes-2019-article-iv-consultation-with-somalia*

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[7] *Aid Flows in Somalia, Federal Government of Somalia, Ministry of Planning, Investment, and Economic Development, 2019; https://reliefweb.int/sites/reliefweb.int/files/resources/Aid-Flows-in-Somalia-2019-ENGLISH.pdf*

[8] *Somalia National Development Plan 2020 to 2024, Ministry of Planning, Investment and Economic Development; http://mop.gov.so/wp-content/uploads/2019/12/NDP-9-2020-2024.pdf*

[9] *Neither military aid nor aid for enforcement of peacekeeping qualify as ODA*

[10] *ibid*

[11] *ibid*

[12] *Somalia Education for Human Capital Development Project, World Bank, 2020; https://ewsdata.rightsindevelopment.org/files/documents/34/WB-P172434.pdf*

[13] *Integrated Food Security Phase Classification, 2018; http://www.ipcinfo.org/ipc-country-analysis/details-map/en/c/1151668/?iso3=SOM*

[14] *UNICEF; https://data.unicef.org/country/som/*

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