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Report No: PAD3015

INTERNATIONAL DEVELOPMENT ASSOCIATION
PROJECT APPRAISAL DOCUMENT

ON A

PROPOSED GRANT
(PRE-ARREARS CLEARANCE GRANT)

IN THE AMOUNT OF SDR 12.9 MILLION
(US$18 MILLION EQUIVALENT)

TO THE

FEDERAL REPUBLIC OF SOMALIA

FOR A

SOMALIA CAPACITY ADVANCEMENT, LIVELIHOODS AND ENTREPRENEURSHIP, THROUGH DIGITAL UPLIFT PROJECT

February 22, 2019

Finance, Competitiveness, and Innovation Global Practice
Africa Region

CURRENCY EQUIVALENTS

Exchange Rate Effective January 31, 2019

Currency Unit =	Somali Shilling
SOS 578 =	US$1
US$1.40 =	SDR 1

January 1 – December 31

ABBREVIATIONS AND ACRONYMS

ALM	Assets and Liabilities Management
AMC	Annual Maintenance Contract
AML/CFT	Anti-Money Laundering and Countering Financing of Terrorism
AMISOM	African Union Mission in Somalia
ATS	Automated Transfer System
BDS	Business Development Services
CBS	Central Bank of Somalia
CDD	Customer Due Diligence
CPF	Country Partnership Framework
DA	Designated Account
DE4A	Digital Economy for Africa
DFI	Development Finance Institution
E&S	Environmental and Social
EAFS	External Assistance Fiduciary Section
ESMF	Environmental and Social Management Framework
ESMS	Environmental and Social Management System
FATF	Financial Action Task Force
FCV	Fragility, Conflict, and Violence
FGS	Federal Government of Somalia
FIDEP	Financial Institutions Development Program
FIDP	Financial Institutions Development Plan
FIL	Financial Institutions Law
FIU	Financial Intelligence Unit
FM	Financial Management
FMIS	Financial Management Information System
FMS	Federal Member States
FRC	Financial Reporting Center
G2P	Government-to-Person

GBV	Gender-Based Violence
GDP	Gross Domestic Product
GEEL	Growth, Enterprise, Employment, and Livelihoods
GRM	Grievance Redress Mechanism
HIPC	Heavily Indebted Poor Country
ICT	Information and Communications Technology
ID4D	Identification for Development
IDP	Internally Displaced Person
IFC	International Finance Corporation
IFR	Interim Financial Report
IMF	International Monetary Fund
IPSAS	International Public Sector Accounting Standards
IRR	Internal Rate of Return
IRU	Indefeasible Right of Use
ISA	International Standards on Auditing
KYC	Know Your Customer
LEA	Law Enforcement Agency
M&E	Monitoring and Evaluation
MDAs	Ministries, Departments, and Agencies
MEF	Monitoring and Evaluation Framework
MFD	Maximizing Finance for Development
MFI	Microfinance Institution
MIS	Management Information System
MNO	Mobile Network Operator
MoCI	Ministry of Commerce and Industry
MoF	Ministry of Finance
MoIFAR	Ministry of Interior, Federal Affairs, and Reconciliation
MOU	Memorandum of Understanding
MPF	Multi-Partner Fund
MPTT	Ministry of Posts, Telecommunications, and Technology
MSMEs	Micro, Small, and Medium Enterprises
MTB	Money Transfer Business
MTO	Money Transfer Operator
NADRA	National Database and Registration Authority
NCA	National Communications Authority
NDP	National Development Plan
NGO	Nongovernmental Organization
NPL	Nonperforming Loan
NPS	National Payment Systems
NPV	Net Present Value

NRA	National Risk Assessment
OSS	One-Stop Shop
PACG	Pre-Arrears Clearance Grant
PAFS	Project Annual Financial Statement
PDO	Project Development Objective
PFI	Participating Financial Institution
PFM	Public Financial Management
PIU	Project Implementation Unit
POM	Project Operations Manual
PP	Procurement Plan
PPA	Public Procurement, Concessions, and Disposal Act
PPD	Public-Private Dialogue
PPSD	Project Procurement Strategy for Development
PSC	Project Steering Committee
QPR	Quarterly Progress Report
RA	Reflows Account
RegTech	Regulatory Technology
SBCF	Somali Business Catalytic Fund
SCALED-UP	Somalia Capacity Advancement, Livelihoods and Entrepreneurship, through Digital Uplift Project
SCoA	Standard Chart of Accounts
SCORE	Somali Core Economic Institutions and Opportunities Project
SEAP	Somali Electricity Access Project
SMEs	Small and Medium Enterprises
SMEF	SME Facility
SMP	Staff Monitored Program
SMPF	Somalia Multi-Partner Fund
SOE	Statement of Expenditure
SomaliREN	Somalia Research and Education Network
STEP	Systematic Tracking of Exchanges in Procurement
TA	Technical Assistance
TOR	Terms of Reference
TTL	Task Team Leader
TTWG	Tripartite Technical Working Group
UNDB	United Nations Development Business
UNDP	United Nations Development Programme
WFP	World Food Programme

Regional Vice President:	Hafez M. H. Ghanem
Country Director:	Bella Bird
Senior Global Practice Director:	Sebastian Molineus
Practice Manager:	Niraj Verma
Task Team Leader(s):	Thilasoni Benjamin Musuku, Axel Rifon Perez

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DATASHEET

BASIC INFORMATION

Country(ies)	Project Name
Somalia	Somalia Capacity Advancement, Livelihoods and Entrepreneurship, through Digital Uplift Project (SCALED-UP)

Project ID	Financing Instrument	Environmental Assessment Category	Process
P168115	Investment Project Financing	B-Partial Assessment	Urgent Need or Capacity Constraints (FCC)

Financing & Implementation Modalities

[ ] Multiphase Programmatic Approach (MPA)	[ ] Contingent Emergency Response Component (CERC)
[ ] Series of Projects (SOP)	[✓] Fragile State(s)
[ ] Disbursement-linked Indicators (DLIs)	[ ] Small State(s)
[✓] Financial Intermediaries (FI)	[ ] Fragile within a non-fragile Country
[ ] Project-Based Guarantee	[✓] Conflict
[ ] Deferred Drawdown	[ ] Responding to Natural or Man-made Disaster
[ ] Alternate Procurement Arrangements (APA)	

Expected Approval Date	Expected Closing Date
07-Mar-2019	30-Jun-2023
Bank/IFC Collaboration	Joint Level
Yes	Complementary or Interdependent project requiring active coordination

Proposed Development Objective(s)

The Project Development Objective (PDO) is to support progress towards increased access to basic digital financial and government services targeting entrepreneurship and employment, particularly for women.

Components

Component Name	Cost (US$, millions)
Strengthening Institutions	7,000,000.00
Enabling Financial and Digital Services	20,000,000.00
Project Management and Coordination	4,000,000.00

Organizations

Borrower:	Ministry of Finance, Federal Republic of Somalia
Implementing Agency:	Ministry of Finance, Federal Republic of Somalia

PROJECT FINANCING DATA (US$, Millions)

SUMMARY

Total Project Cost	31.00
Total Financing	31.00
of which IBRD/IDA	18.00
Financing Gap	0.00

DETAILS

World Bank Group Financing

International Development Association (IDA)	18.00
IDA Grant	18.00

Non-World Bank Group Financing

Trust Funds	13.00
Somalia Multi-Partner Fund	13.00

IDA Resources (in US$, Millions)

	Credit Amount	Grant Amount	Guarantee Amount	Total Amount

National PBA	0.00	18.00	0.00	18.00
Total	**0.00**	**18.00**	**0.00**	**18.00**

Expected Disbursements (in US$, Millions)

WB Fiscal Year	2019	2020	2021	2022	2023
Annual	0.50	3.66	3.93	4.41	5.50
Cumulative	0.50	4.16	8.09	12.50	18.00

INSTITUTIONAL DATA

Practice Area (Lead)

Finance, Competitiveness and Innovation

Contributing Practice Areas

Transport

Climate Change and Disaster Screening

This operation has been screened for short and long-term climate change and disaster risks

Gender Tag

Does the project plan to undertake any of the following?	
a. Analysis to identify Project-relevant gaps between males and females, especially in light of country gaps identified through SCD and CPF	Yes
b. Specific action(s) to address the gender gaps identified in (a) and/or to improve women or men's empowerment	Yes
c. Include Indicators in results framework to monitor outcomes from actions identified in (b)	Yes

SYSTEMATIC OPERATIONS RISK-RATING TOOL (SORT)

Risk Category	Rating
1. Political and Governance	High
2. Macroeconomic	High
3. Sector Strategies and Policies	Moderate
4. Technical Design of Project or Program	Substantial

5. Institutional Capacity for Implementation and Sustainability	● High
6. Fiduciary	● High
7. Environment and Social	● Substantial
8. Stakeholders	● Substantial
9. Other	
10. Overall	● High

COMPLIANCE

Policy

Does the project depart from the CPF in content or in other significant respects?

[ ] Yes [✓] No

Does the project require any waivers of Bank policies?

[ ] Yes [✓] No

Safeguard Policies Triggered by the Project	Yes	No
Environmental Assessment OP/BP 4.01	✓	
Performance Standards for Private Sector Activities OP/BP 4.03		✓
Natural Habitats OP/BP 4.04		✓
Forests OP/BP 4.36		✓
Pest Management OP 4.09		✓
Physical Cultural Resources OP/BP 4.11		✓
Indigenous Peoples OP/BP 4.10		✓
Involuntary Resettlement OP/BP 4.12		✓
Safety of Dams OP/BP 4.37		✓
Projects on International Waterways OP/BP 7.50		✓
Projects in Disputed Areas OP/BP 7.60		✓

Legal Covenants

Sections and Description
The Recipient shall not later than 30 days after the Effective Date, establish and thereafter, maintain throughout the project implementation, the Project Steering Committee with a mandate, resources, terms of reference and functions, satisfactory to the Association.

Sections and Description
The Recipient shall, not later than October 31 of each year prepare and furnish to the Association, a consolidated annual program of activities proposed for implementation under the Project during the following Fiscal Year, together with a proposed budget for the purpose.

Sections and Description
The Recipient shall furnish to the Association each Project Report not later than forty-five (45) days after the end of each calendar semester, covering the calendar semester.

Conditions

Type	Description
Effectiveness	The Recipient shall have (i) established the MSME Financing Facility, in form and substance satisfactory to the World Bank; and (ii) appointed to said MSME Financing Facility a governing board consisting of members drawn from the private and public sector, all with qualifications, terms of reference and functions, acceptable to the Association; and (iii) recruited to said MSME Financing Facility adequate staff in accordance with the provisions of the Procurement Regulations.
Effectiveness	The Subsidiary Agreement, acceptable to the World Bank, shall have been duly executed and delivered on behalf of the Recipient and the MSME Financing Facility and shall have become effective and binding upon such parties in accordance with its respective terms.
Effectiveness	The Recipient has submitted, in form and substance satisfactory to the World Bank, its policy statement regarding its digital identity system, including data protection;
Effectiveness	The Recipient has prepared and adopted, in form and substance satisfactory to the World Bank, the Project Operational Manual.
Effectiveness	Effectiveness of each Agreement: (1) For the Financing Agreement: “the SMPF Grant Agreement has been executed and delivered and all conditions precedent to its effectiveness or to the right of the Recipient to make withdrawals under it have been fulfilled.”; and (2) For the SMPF Grant Agreement: “the Financing Agreement has been executed and delivered and

	all conditions precedent to its effectiveness or to the right of the Recipient to make withdrawals under it have been fulfilled."
Type Disbursement	Description For payments made prior to the date of the Grant Agreement, or payments under the line of credit, no withdrawal shall be made unless: (i) a technical and fiduciary (procurement and financial management) assessment of MSME Financing Facility (as an implementing entity for the financial intermediary), has been carried out, in a manner acceptable to the Association; (ii) a Project Agreement has been executed between the Association and the MSME Financing Facility; and (iii) the MSME Subproject Manual (forming an annex or schedule to the Project Operations Manual) is prepared and submitted, in form and substance satisfactory to the Association.
Type Disbursement	Description For payments under the large loans window for MSMEs no withdrawal shall be made unless the Technical Agreement has been executed between the IFC and the MSME Financing Facility.

I. STRATEGIC CONTEXT

A. Country Context

1. **Somalia remains a fragile country despite the substantial progress made in recent years to lay the foundations for stability and development.** Since 2011, Somalia has had a sustained period of political, economic, and security-related progress. Consequently, the country has a unique opportunity to escape from decades of conflict and fragility, and the Government is demonstrating a strong commitment to wide-ranging institutional and economic reforms. Yet, substantial challenges remain, including access barriers to services enabling economic opportunities, reconciliation, security sector reform, widespread malnutrition, recurrent drought, and poverty. Limited fiscal space constrains service delivery by the Federal Government of Somalia (FGS) leading to low trust in the state. The United Nations Population Fund's Population Estimate Survey in 2014 produced the first population estimates for Somalia in many years. Total population was estimated at 12.4 million—42 percent urban, 26 percent nomadic, 23 percent rural, and 9 percent displaced. In 2017, Somalia's population was about 14 million, and it is estimated that about 69 percent of the population is poor.[1] A poverty gap of 29 percent suggests that the consumption levels of many of the poor are far from the poverty line and they face deprivations in both monetary and non-monetary dimensions.[2]

2. **Somalia's economic development challenges are equally daunting, and growth remains insufficient for reducing vulnerability for a large segment of the population.** With an estimated per capita gross domestic product (GDP) of US$511 in 2017,[3] Somalia remains one of the poorest countries in the world. Despite the perpetual civil conflict, the economy has grown at a moderate pace, averaging 2.5 percent, real GDP growth in 2013–17. Growth is mainly consumption driven, enabled by large remittance and aid inflows (US$1.4 billion[4] and US$1.75 billion,[5] respectively in 2017), while construction, telecommunications, and money transfer services have been the key growth sectors. The diaspora remittances enable household consumption at 132 percent of GDP and represent an important component of income for the bottom 40 percent of households.[6] Low electrification rates, especially in rural areas, are one of the key constraints for economic growth in Somalia.

3. **Unemployment is widespread within Somalia's young population.** With 70 percent of the population below the age of 30,[7] youth unemployment is at 74 percent and 61 percent for women and men, respectively.[8] Similarly, for persons with disabilities, unemployment is widespread. In this setting, remittances and humanitarian aid alone are not sufficient to support the development of sustainable livelihoods that are necessary for poverty reduction and mitigation of political, social, and economic vulnerability. The domestic economy and many local livelihoods are dependent on the livestock sector,

[1] World Bank. 2018. *Somalia High Frequency Survey. December 2017, Wave 2*.
[2] Ibid.
[3] World Bank Group. 2018. *Somalia Economic Update: Rapid Growth in Mobile Money - Stability or Vulnerability?*
[4] IMF (International Monetary Fund). 2017. *2016 IMF Somalia Country Report 17/61*.
[5] Ministry of Planning, Investment and Economic Development, Federal Republic of Somalia. 2018. *Aid Flows in Somalia: Analysis of Aid Flow Data*.
[6] World Bank Group. 2018. *Somalia Economic Update: Rapid Growth in Mobile Money - Stability or Vulnerability?*
[7] World Bank Group. 2015. *Somalia Economic Update: Transition Amid Risks with a Special Focus on Intergovernmental Fiscal Relations*.
[8] World Bank Group Gender Data Portal. http://datatopics.worldbank.org/gender/country/somalia.

which generates trade worth an estimated 40 percent of Somalia's GDP and represents over 50 percent of Somalia's exports, but which is itself highly vulnerable to drought and trade-related shocks.

4. **Poor access to tailored finance to women contributes to limiting female entrepreneurship.** An analysis of gender gaps in Somalia, in relation to financial and digital access, suggests that women face discrimination and considerable socioeconomic barriers to accessing jobs and livelihood opportunities.[9] Traditional gender roles still limit women's employment opportunities, often excluding them from work in formal sectors, generating gender gaps in labor market participation. Gender gaps in education and basic literacy translate into weak digital and financial skills among women, which in turn limits their financial and digital services access. Nevertheless, Somali women are largely responsible for growth in microenterprise activity and yet are not supported to grow and expand their businesses. A recent review of the World Bank's Small and Medium-Size Enterprise Facility (SMEF), which provided business development services (BDS) to small and medium enterprises (SMEs) in Somalia under the Somali Core Economic Institutions and Opportunities Project (SCORE) (P152241), reiterates that women-led businesses struggle to access funding even though there is demand for financing among female-headed SMEs. This is partly because financial service providers do not necessarily offer financial products that target women, nor do they implement a cohesive policy that targets women in a way that removes barriers that currently restrict access. For example, women face discrimination in accessing credit due to existing collateral requirements. Even when women have the required collateral, banks typically ask for a male guarantor, and when women do receive loans, they are typically microcredit, that is, in the range of US$1,000.

5. **Somalia has a vibrant private sector, a networked business community and a desire for international trade and investment.** The agriculture sector, mainly livestock, remains the backbone of the Somali economy. Preliminary gross production estimates for the agriculture sector show that the sector accounts for the largest share of GDP since the pre-war period—62 percent in 1986–88 to an average estimate of about 70 percent in 2013–16 (World Bank and FAO 2018).[10] Somalia's Doing Business ranking is the lowest at 190 out of 190 (Doing Business 2019). Somalia has one of the most expensive electricity rates, at almost US$1 per kilowatt, and correspondingly the lowest rates of electricity usage in the world. Moreover, informality dominates the private sector, making market-based financial intermediation challenging particularly in key sectors of the real economy such as energy and livestock. In addition, regulatory and institutional capacity gaps—in key enabling sectors such as financial and information and communication technology (ICT)—result in an uneven playing field undermining economic growth and potential. The development of the manufacturing sector is limited by the harsh business environment and the high electricity and transport costs. This, combined with barriers that restrict access to services—compounded by fears of money laundering and terrorist financing, as well as poor banking relationships between domestic and international banks—creates unpredictability of remittance channels and connectedness of the country to international capital sources, deterring large-scale private and public investment. These service access barriers may, in turn, exacerbate political tensions and result in the development of parallel underground 'shadow markets'. Thus, to support

[9] See annex 5 for detailed discussion on gender gap analysis in Somalia across labor markets and financials markets and ID ownership.

[10] It is difficult to determine sectoral contribution to GDP in Somalia due to lack of national accounts data. New GDP estimates by World Bank and International Monetary Fund (IMF) staff are used to compute the sector shares post 2013.

livelihoods and inclusive growth, there is a pressing need to stabilize core institutions offering basic services enabling economic opportunities for individuals and businesses.

6. **The lack of a robust and inclusive foundational ID system limits financial access and poses challenges for broader service delivery and economic growth.** Over 77 percent of Somalia's population are estimated to lack an official proof of identity. Although data on ID coverage is scarce, recent surveys indicate that women are more likely than men to lack an ID, with an estimated gender gap of at least 9 percentage points. Existing ID systems are fragmented and designed to meet specific program needs rather than to serve as a foundational, multipurpose identification for the entire population (see box 1). Moreover, there are no reliable and broadly accessible ID verification or authentication mechanisms, further compounding challenges for accessing crucial financial and government services. The lack of a robust and inclusive foundational ID system makes it difficult for financial service providers to fulfill international customer due diligence (CDD) requirements. Failure to adequately comply with international anti-money laundering and countering financing of terrorism (AML/CFT) requirements, due, in part, to a lack of robust 'Know Your Customer (KYC)' verification mechanisms, have resulted in many Somali remittance providers and other financial institutions losing their correspondent banking relationships in recent years, posing a threat to the livelihood of millions of Somalis and further impeding financial access and entrepreneurship.

Box 1. Registration and Identification Approaches in the Humanitarian Sector

A historic lack of a robust foundational identification system has led to a proliferation of disconnected functional registers and, as a result, Somalis must rely on a patchwork of non-interoperable systems and documents to prove their identity, most of which are of low quality, with coverage limited to specific municipalities, states, or program beneficiaries.

International organizations, such as the United Nations World Food Programme (WFP), the United Nations Office for Project Services (UNOPS), as well as the National Commission for Refugees and Internally Displaced Persons (NCRI), collect identity data and issue credentials, often using sophisticated digital and/or biometric identification technologies. For example, WFP's SCOPE system, which is used to register and manage benefit transfers to the beneficiaries of WFP assistance in Somalia, contains information on over 4 million individuals (biometric registration of 2 million individuals, and additional 2 million individuals registered by collecting their biographic data only). Registered beneficiaries are issued electronic transfer cards (e-cards) allowing card holders to purchase food at vetted local shops or to receive food assistance.

While these functional systems can support effective program delivery for the organizations that own and manage the beneficiary registries, they offer only limited utility for broader identification purposes. These functional systems often use proprietary data management solutions and lack interoperability, making it difficult for third parties to reliably verify identities. Because humanitarian organizations often focus on a particular area and only a limited number of people per household are issued a credential for service delivery, existing, functional ID systems tend to also be limited in scope—both demographically and geographically. At the same time, the previous registration experience of humanitarian agencies as well as enrollment strategies and outreach campaigns can provide important lessons for achieving high coverage and ensuring the robustness of the proposed foundational digital ID. Existing registries could also be leveraged in the future as the FGS will begin to deliver its own social protection programs.

7. **Somalia's security situation hampers development initiatives and freedom of movement in the country.** All development initiatives and staff movements within Somalia are continuously analyzed for security threats. If security restrictions are put in place for certain locations, then project activities and

staff movements are limited, potentially excluding those locations from development initiatives. Alternately, initiatives may be redirected when possible to other appropriate locations, delayed, or altogether cancelled. All existing and newly designed World Bank Group operations must be flexible to adapt to the changing security context affecting the whole economy in Somalia.

8. **Somalia has achieved significant progress in laying the foundations for stability and development; however, political and institutional gains must have tangible benefits for people if Somalia's transition is to hold.** The World Bank Group's Country Partnership Framework (CPF) for Somalia for FY19-22 (Report No. 124734-SO) aims to increase citizen's access to services and help restore economic resilience—laying the foundations for longer-term poverty reduction and inclusive growth. The CPF is based on an analytical framework elaborated in the recently concluded Systematic Country Diagnostic as well as the outcome of country level dialogue between the World Bank Group, its Somali partners, and the international community. With debt arrears outstanding, Somalia has been ineligible for assistance from International Development Association (IDA) and other international finance institutions (IFIs)—but the World Bank Group's reengagement in 2012 funded by the Multi Partner-Fund (MPF) has helped stabilize institutions and initiate IFI normalization. With support of eight key donors, the MPF has enabled the World Bank Group to strengthen federal institutions and establish basic economic regulatory foundations. The MPF will remain the core financing vehicle for the CPF—but will be complemented in FY19 by IDA Pre-Arrears Clearance grants of US$140 million targeting the key milestones to reach Decision Point under the Heavily Indebted Poor Country (HIPC) Initiative. Provided its reform momentum continues, Decision Point is feasible within the CPF period, allowing Somalia access to concessional resources from IDA and other IFIs, together with investment of private capital from the International Finance Corporation (IFC).

9. **This project builds on the foundations laid by predecessor projects' early successes that is, SCORE (P152241) and ICT Sector Support (P152358) projects.**[11] With financing from IDA's Pre-Arrears Clearance Grant (PACG) facility as well as the MPF, the project proposes to further support reforms associated with stabilizing core government functions that will help Somali communities overcome restrictions on access to services. The supported government institutions are those considered key to enabling access to basic financial and government services that offer economic opportunities for individuals and businesses. In so doing, the project initiates the development of sustainable mechanisms for delivery of targeted accessible government services, enabling efficient and market-based financial intermediation, and inclusive growth. These basic financial and government services contribute to breaking the cycles of violence and setting Somalia on the path toward economic development. The project is initially designed as a four-year program, which if successful in its first phase, additional financing may be considered.

B. Sectoral and Institutional Context

10. **Somalia's financial sector is limited in size, simple in structure, and extremely isolated from the global financial system.** Access to global banking systems remains uncertain. Over the past three years, banks in international jurisdictions such as Australia, the United Kingdom, and the United States have closed accounts of some Somali remittance companies due to risks related to money laundering, as well as legal and regulatory weaknesses. This makes it essential to enhance the understanding of AML/CFT

[11] See box 2 for further details on the predecessor projects, that is SCORE (P152241) and ICT Sector Support (P152358) projects.

risks of the Financial Reporting Center (FRC), Somalia's financial intelligence unit, and to strengthen its institutional capability and core systems to receive and analyze financial intelligence on AML/CFT and disseminate this intelligence to law enforcement agencies (LEAs), as appropriate. In this setting, the impetus for institutional reform is driven by external pressures on Somali policy makers and financial institutions to improve governance and institutional effectiveness.

11. **Overall, there is meagre intermediation taking place in the Somali credit market, which meets only 7 percent of the current demand.** Lending is heavily concentrated on short-term trade finance, which makes up approximately 85 percent of the total portfolio of financial institutions leaving a large unmet market demand in the real economy. This lack of progress to expand access to finance in underserved economic segments is partly explained by slow progress in elaborating a financial inclusion strategy to underpin public and private sector commitments to address some key institutional and structural challenges. In addition, Somali financial institutions are not experienced in lending outside trade finance, have a weak pipeline of bankable micro, small, and medium enterprises (MSMEs) operating in productive sectors of the economy and limited understanding of what constitutes a well-prepared loan application for MSMEs operating in productive sectors resulting in little to no provision of credit to businesses and/or poor credit quality.

12. **The financial system comprises central banks (including in Somaliland), banks, microfinance institutions (MFIs), money transfer businesses (MTBs), and mobile network operators (MNOs) providing mobile money services.** As of January 2019, eight banks and 11 MTBs were licensed by the Central Bank of Somalia (CBS), but three banks are not yet operational.[12] The total banking industry assets were at US$351 million as of September 2018.[13] Most banks met the minimum capital requirement of US$7 million. There are several MFIs operating in the country. However, as explained in box 2, the MFI industry remains unregulated. In 2015, the mobile phone penetration rate stood at 59 percent, and in 2017, some 70 percent of Somalis with a mobile phone regularly used mobile money services, transacting for approximately US$2.7 billion per month—yet, mobile money remains unregulated.[14] In 2011, the FGS passed the Central Bank of Somalia Act, which reinstated the CBS. In 2012, the FGS passed the Financial Institutions Law (FIL), which created a national framework for financial institution regulation and supervision by the CBS. However, the FIL only covered banks and MTBs, and there are plans currently underway to modernize the FIL.

Box 2. Microfinance Industry in Somalia[a]

- The Somalia microfinance industry is currently unregulated. The 2012 FIL only recognizes commercial banks and MTBs as financial institutions which has left microfinance players in a legal vacuum. The FIL is to be amended and modernized during 2019.
- Six major MFIs operate in Somalia either as affiliated subsidiaries of commercial banks or registered as nongovernmental organizations (NGOs). This includes MicroDahab, IBS Microfinance, Premier Microfinance, AMAL Microfinance, KAABA Microfinance, and Kaah International Microfinance Services (KIMS). Additionally, many local and international NGOs provide heavily subsidized microfinance products. Women are overrepresented as clients within the microfinance industry. MFIs lend both for business and private purposes.

[12] For more detailed information regarding Somali financial institutions kindly refer to annex 3.
[13] Central Bank of Somalia Quarterly Report, 2018.
[14] World Bank. 2017. Mobile Money Ecosystem in Somalia: Household Survey and Market Analysis. Washington, DC.

- Microfinance regional coverages differs by institution. Microfinance operators affiliated with commercial banks generally operate in the same regions as their parent institutions while NGO-based MFIs are usually concentrated in major urban centers such as Mogadishu, Hargeisa, Garowe, and Kismayo.
- Asset sizes of MFI players in Somalia range from US$0.3 million to US$3 million.
- MFIs provide services using Islamic financing instruments. The two most utilized financial instruments within the industry are Qardu Hassan (charity-based and often subsidized with donor money) and Murabaha (cost-plus).
- Average microfinance loans currently stand at around US$1,000. Tenors are short, often less than a year.

Note: a. Limited data are available on the financial condition of MFIs in Somalia. The data are based on World Bank. 2017. *Mobile Money Ecosystem in Somalia: Household Survey and Market Analysis*. Washington, DC, and interviews by the task team with financial sector stakeholders in Somalia conducted in September 2018.

13. **An emerging trend in the sector is the consolidation of financial service operators into a few large companies, which deters competition from prospective entrants.** Somali money transfer and MNOs have always been intertwined, but the rapid growth of mobile money has forced key players in the strategic sectors of banking and money transfer services to not only protect their market niche but also occupy new ones as well. They do so largely through mergers and alliances. There is also a growing trend of partnerships to facilitate international remittances directly to customers, resulting in large conglomerates and the crowding out of smaller MTBs. As a result, there is overlapping business interest ownership in the financial sector covering banking, microfinance, and mobile money.

14. **Limitations exist in financial, technical, and managerial capacity to implement targeted interventions to enhance provision of and access to basic financial and government services by individuals and businesses.** Capacity improvements will take time to overcome, while the urgency of expanding access to basic services is increasing. Missing financial infrastructure and rules affecting the coverage, scope, and accessibility of credit information such as credit referencing or moveable collateral registries limit expansion of financial access.

15. **Providing a robust and verifiable government-recognized ID is among the most pressing priorities in Somalia at this time**. A unique identifier linked to each transaction account, will help ensure that financial transactions can be more accurately tracked. This will enable scale-up of access to finance and other basic services for Somalis, including for women and vulnerable people in rural areas, and promote safe and orderly migration within and across Somalia's borders. A robust digital ID system is also instrumental for improving the robustness of business registration and access to finance for MSMEs as implementation of a central registry for companies offers access to information ensuring transparency around who really owns and controls Somali companies which is useful in tackling AML/CFT risks.

16. **The FGS has already taken steps to enable the implementation of a digital ID system, although large gaps remain in the enabling environment and several risks will need to be addressed**. A Memorandum of Understanding (MOU) dated May 23, 2018, was signed between the FGS Ministry of Interior, Federal Affairs, and Reconciliation (MoIFAR) acting through the Office of the President and National Database and Registration Authority (NADRA)[15] of Pakistan for the development of a digital ID system, including the design and installation of data management systems for multiple foundational and functional IDs, skills, and knowledge transfer, and maintenance and support for one year. However, for

[15] https://www.nadra.gov.pk/.

the digital ID system to achieve its full potential, risks associated with, among others, exclusion, vendor lock-in, and potential misuse of the system will need to be appropriately addressed. In addition, Somalia currently lacks a robust legislative and regulatory framework to govern the implementation of a robust, inclusive, and responsible foundational ID system and has not yet set up a dedicated entity to oversee and manage the proposed digital ID system. Ensuring that the ID system rests on solid legal and institutional foundations will be critical for its ability to ensure that IDs are accessible for all, to protect users' data and privacy, to build and maintain trust in the system, and to ensure its long-term sustainability.

17. **Addressing the multifaceted challenges of lack of access to basic services enabling economic opportunities for individuals and businesses requires approaches that are both innovative and flexible**. First, lack of reliable identity documents and identity verification mechanisms, compounded by a lack of connectivity are important barriers to the efficient delivery of basic services by the Government and private sector service providers. The design and implementation strategy of the ID system will draw on, and adapt to the Somali context as needed, the latest international good practices and lessons learned from digital ID systems all around the globe. For example, to enable rapid take-up of the ID credentials and to make registration accessible for members of vulnerable populations, the project proposes to follow an 'ecosystem' approach for enrollment, leveraging private sector entities and local NGOs as enrollment agents. Second, there are spatial and gender disparities in access to basic financial and government services making credible demand assessments from final beneficiaries essential to ensure appropriateness of products or services and sustainability of investments. Addressing these specificities, as well as the challenges posed by the operating environment and all-round capacity weaknesses, the project proposes to set up dedicated entities to operate on a sustainable basis to expand access to services. Based on the Government's policy commitments, these entities will be highly agile and use private sector governance principles in constructing sustainable and effective service delivery mechanisms supported by appropriate fiscal plans, financing instruments, and performance reporting tools.

18. **Digital technologies will remain critical in Somalia for the foreseeable future to help curb economic isolation and rapidly transform the way people, businesses, and the FGS communicates, transacts, and accesses information and services.** The World Bank, in partnership with public and private digital stakeholders, launched the Digital Economy for Africa (DE4A) Initiative in April 2018.[16] DE4A recognizes that traditional economic sectors of Africa are paving the way to new growth models with rising mobile phone penetration, improving broadband Internet, and growing use of mobile money—unleashing new opportunities for people, businesses, and governments. As such, the project aims to build on the DE4A codified pillars for the development of an inclusive digital economy in Africa[17] by making steady and incremental improvements on accomplishments delivered under the SCORE (P152241) and ICT Sector Support in Somalia (P152358) projects. The project achieves this by enhancing the linkage and synergy between digital developments and digitization of finance to support entrepreneurship and livelihoods. While the preceding projects set up the foundational infrastructure and platforms to kick-start the process of enabling economic opportunities and expanding access to basic financial and government services to support entrepreneurship and sustainable jobs (see box 3), this project leverages technology

[16] http://live.worldbank.org/digital-economy-africa.
[17] The DE4A conceptual framework includes the basic elements of the digital economy as a whole (a) a highly efficient digital infrastructure, (b) public digital platforms, (c) digital finance services, (d) digital and innovative entrepreneurship, and (e) digital skills. Progress must be made in each of these elements to develop relevant digital services for the growth of various sectors of the economy.

as an enabler and anchor to build and strengthen key institutions and financial market infrastructure and support efficient financial intermediation.

Box 3. Building on the Accomplishments of Preceding Projects

The SCORE (P152241) and ICT Sector Support (P152358) projects involve strengthening legal and regulatory foundations, institutional capacity, and financial and private sector development. This project makes a strategic shift from the two predecessor projects, as the Somalia Capacity Advancement, Livelihoods, and Entrepreneurship, Through Digital Uplift Project (SCALED-UP) is supporting the FGS to deliver on its commitments to improve robustness and expand coverage of key services enabling entrepreneurship and supporting livelihoods (digital ID, transaction accounts, KYC e-verification services, e-registration services for businesses, and interoperable retail payment services). Figure 2.1 in annex 2 provides additional details on the phased and iterative approach of implementing activities under the two predecessor projects.

SCORE Project. This is a US$28.5 million investment lending operation running from May 2016 to June 2020. Under SCORE, the World Bank is helping build core financial and private sector foundations, concretely, the legal and regulatory framework, financial sector infrastructure, and institutional and enforcement capacity—all of which have effectively been absent. This has involved developing foundational legislation and priority functions of the CBS and the Ministry of Commerce and Industry (MoCI) as follows:

- Improving Somalia's business climate through modernization of the 2012 FIL, passage of a modern Company Law, and a new Payment Systems and Insurance Act utilizing the IFC Public-Private Dialogue (PPD) platform as an instrument to hold constructive dialogue among the relevant stakeholders regarding the development and passage of these legislations.
- Delivering a core banking and accounting system at the CBS to strengthen the operating environment from a fiscal agency point of view.
- Supporting examination of the MTBs and providing on-the-job training for CBS staff in support of safe and low-cost remittance flows to Somalia and establishment of mobile money regulations.
- Building a platform for engagement between the CBS and the financial services industry to drive national payment systems (NPS) developments to allow humanitarian assistance to be transferred more securely, improve FGS service delivery, and deepen financial sector intermediation.
- For the FRC, a National Risk Assessment (NRA) has been initiated and once concluded will inform both a capacity-building program for the FRC and a national strategy to manage AML/CFT risks.

SCORE Project is also contributing to the development of entrepreneurship and SMEs in support of the jobs agenda, by launching a US$5.5 million BDS program for entrepreneurs through the SMEF and mobilizing SME financing through the Somali Business Catalytic Fund (SBCF), which as of June 2018 has reached 82 firms, committed to disburse US$6.5 million (to be matched by the recipients) to SMEs in the agriculture, manufacturing, and fisheries sectors, and catalyzed the mobilization of further US$1.06 million in private financing from financial institutions. The SBCF was closed in January 2019, and SMEF will be phased out in April 2019. There is no overlap between the two MSME financing mechanisms under the SCORE and SCALED-UP largely because the SBCF bypassed financial intermediaries as it was operated as an SME matching grants scheme.

ICT Sector Support project. This is a combined US$14 million investment lending operation running from 2015 to 2020. Under the ICT Sector Support project, the World Bank has supported the passage of the Communications Act of 2017 and subsequent creation of the National Communications Authority (NCA). Other key accomplishments include the following:

- Supported infrastructure such as a fiber-optic loop around Mogadishu which boosted Internet capacity for 26 FGS ministries in 15 different locations and establishing the first Internet Exchange Point.

- Supported the adoption of the National Numbering Plan and schedule of spectrum and licensing fees that will contribute to the National Treasury and are benchmarks linked to the Recurrent Cost and Reform Financing (RCRF) project (P167224).
- Internet capacity was also acquired, and doubled recently, for the higher education sector, connecting 10 Somali universities, for the higher education sector through the Somalia Research and Education Network (known as 'SomaliREN'). This was done under a 20-year and 10-year pre-purchase of Internet bandwidth from the optical fiber operators in the form of an indefeasible right of use (IRU)[18] contract. The IRU refers to the right to use a specific amount of capacity on the cable for the duration of the contract.
- Supported the creation of around 40 communications rooms across the country.
- Supported public/private dialogue between the operators, Internet service providers, and the FGS. This has stimulated investment in the information and communications technology (ICT) sector both from the private sector and from donor partners.
- Provided support to a youth-owned and youth-led tech hub called 'IRise'. It is one of the first tech hubs in Somalia aiming to promote innovation and increase access for support to local innovative entrepreneurs.

Additionally, under the second phase of the ICT Sector Support project, an operational pilot is underway for making salary payments to civil servants, and for making humanitarian payments in areas affected by drought and flood, using mobile money bulk payments.

19. **To respond to the development challenges, effective coordination mechanisms among institutions are needed to improve performance and delivery of the most crucial services to overcome economic isolation and expand economic opportunities for individuals and businesses.** Several institutions and stakeholders are to be involved if a harmonized policy framework and agenda to offer economic opportunities and enhance access to basic financial and government services is to be pursued. However, unclear mandates and structures, overlap of responsibilities, and lack of a shared strategy remain as key challenges, creating tensions, and delaying the decision-making process**.** In this regard, the project proposes to update and fill gaps in existing government policy frameworks and strategies pertaining to the financial and digital developments, particularly addressing gender gaps in sectoral strategies as well as those related to direct project interventions on digital ID enrollment, access to financial services, and operation of the MSME Financing Facility.[19] This will include development of eligibility criteria for participation in the MSME Financing Facility by bank and nonbank financial institutions involving holistic assessments of factors ranging from fitness and propriety of owners, controllers, and managers of PFIs and final beneficiaries to assessing the capability of PFIs to credibly serve underfunded and underserved market segments and sectors including women and female-owned MSMEs.

C. Relevance to Higher Level Objectives

20. **Alignment to the CPF (FY19–22).** The project is anchored under the Somalia CPF for FY19–22 (discussed by the Board in September 2018, Report No. 124734-SO), specifically Focus Area 2 (Restoring Economic Resilience and Opportunities). The CPF's objective on increasing financial and digital access

[18] Indefeasible right of use (IRU) is a permanent contractual agreement, that cannot be undone, between the owners of a communications system and a customer of that system.
[19] The MSME Financing Facility refers to the entity to be set up by the FGS and mandated to manage the line of credit under the project.

directly relates to Somalia's National Development Plan (NDP) which sets out the country's priorities for national recovery and development for 2017–2019, particularly on actions to address constraints faced by MSMEs. The NDP specifically highlights the importance of enhancing capacity building for the private sector, especially the MSMEs as one of the prerequisites for inclusive growth and employment creation.

21. **The project is also aligned with the 2018–2020 Financial Sector Roadmap developed by the CBS, in partnership with the International Monetary Fund (IMF) and World Bank.** The broad structure of financial sector reforms supported by the Financial Sector Roadmap is a key element of the ongoing IMF's Staff Monitored Program (SMP). The roadmap integrates the process of defining and sequencing supported reforms along four pillars:[20]

(a) Improving CBS capacity for core functions and organization in banking operations, and the licensing and supervision departments, as well as internal audit, and financial reporting and accounting.

(b) Developing a payments system by establishing a national switch and Automated Transfer System (ATS) that will integrate a Real Time Gross Settlement System and Automated Clearing House (functionality onto a single platform with seamless links between the CBS, commercial banks, and mobile money. Other aspects relate to stabilizing MTB foreign banking relationships and minimizing risks in the mobile money sector.

(c) Strengthening legal and regulatory frameworks by modernizing the FIL and other laws to improve the legal basis for provision of financial services as well as CBS regulation and supervision of the financial system that is consistent with internationally accepted practice.

(d) Developing the financial infrastructure to support efficient intermediation and to support collateralized lending and mitigate credit risk.

22. Division of labor between the World Bank and IMF around the 2018–2020 Financial Sector Roadmap is such that IMF takes the lead on aspects related to Pillar (a) above while the World Bank takes the lead in Pillars (b), (c), and (d) with some of the support already in progress under the SCORE Project (P152241). In Pillar (a), the World Bank has supported the implementation of the core banking and accounting system and helped to kick-start MTB onsite and offsite examinations. Moreover, the project is being implemented in close partnership with other key development partners supporting the Government's wide-ranging reform agenda which relates to the broader objective of IFI normalization through the HIPC framework.

23. **The project also supports the Maximizing Finance for Development (MFD) agenda by creating and expanding markets for private sector investment to maximize development results.** The project supports the setting up of a digital ID system using the ID4D principles and targets entrepreneurship and MSME access to financial services with a new apex institution set up to leverage private capital, when it is ready and forthcoming. To crowd-in investment capital from private sector sources, the new apex

[20] Figure 2.2 in annex 2 provides additional details on the broad structure of the financial sector road map and the connections across the four key pillars. The road map and its four key pillars acting as the coordinating vehicle between the World Bank, IMF and other development partners in supporting CBS and other key institutions to financial sector development in a joined-up manner that takes into account the comparative advantages of each supporting institution.

institution is structured on private sector principles and will benefit from a range of blending tools consisting of supporting instruments that enable channeling of core equity and/or subordinated/mezzanine debt to help attain far greater leverage of public funds (relative to more typical approaches to MSME financing), in line with the MFD approach. The project also will support the FGS to stabilize core government institutions that are key to the provision of services enabling economic opportunities for individuals and businesses, and to create legislative and institutional framework enabling financial and digital development. All these activities are essential preconditions or critical enablers for leveraging private capital.

II. PROJECT DESCRIPTION

A. Project Development Objective

24. **The Project Development Objective (PDO) is to support progress towards increased access to basic digital financial and government services targeting entrepreneurship and employment, particularly for women.** The Theory of Change is depicted in the Results Chain in section II.D.

25. **Achievement of PDO will be measured by the following indicators:**

- Number of people who have received their unique ID number, of which (%) are female
- Number of people accessing financial services using their digital ID, of which (%) are female
- Number of firms that benefit from reformed business registration requirements, of which (%) are female-owned
- Value of MSME loans from the MSME Financing Facility (US$), of which (%) are female-owned
- Jobs created by firms that access the MSME Financing Facility, of which (%) are for females, and of which (%) sustainable jobs[21]

B. Project Components

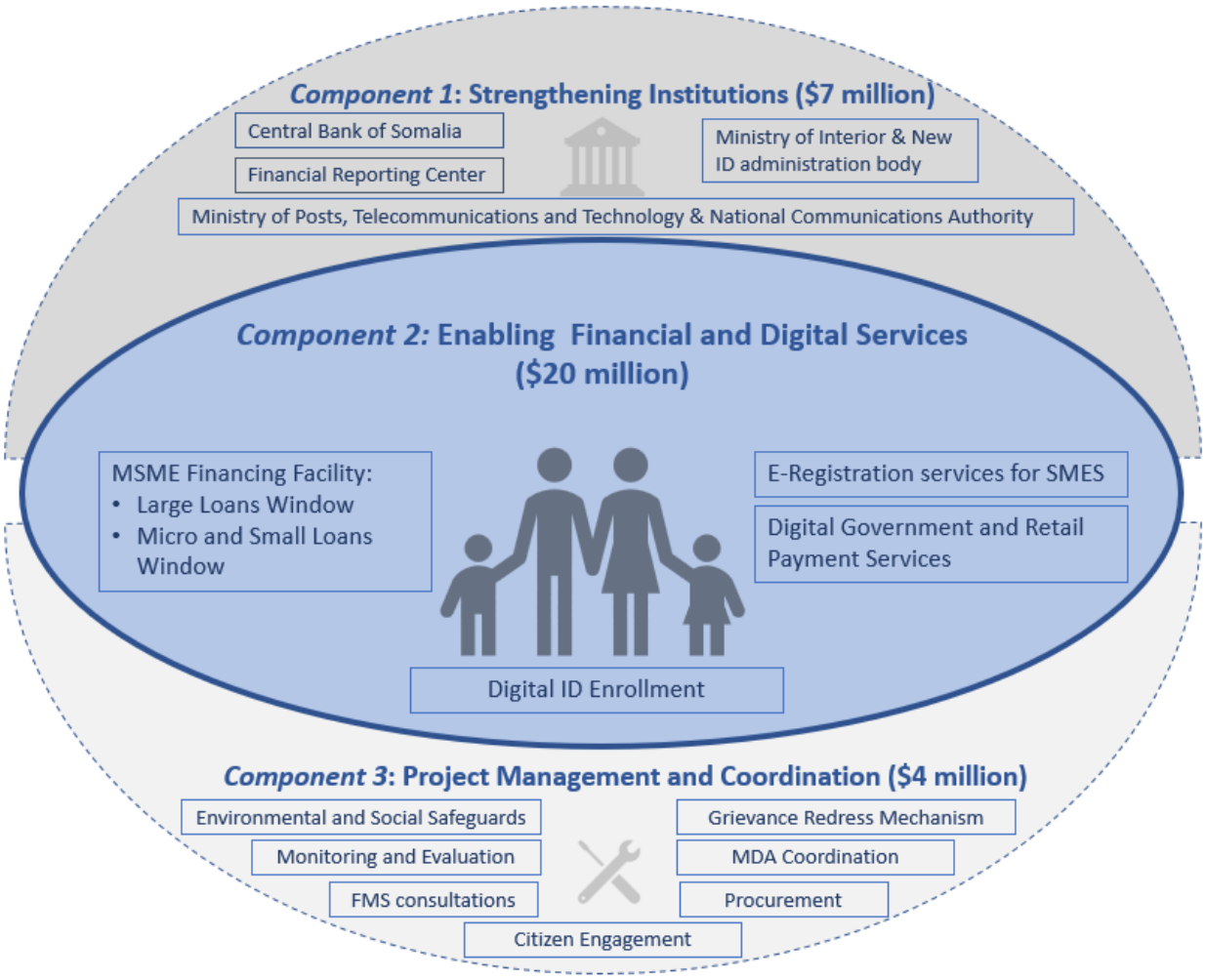
26. **The project has three components, which are summarized in this section (see annex 2 for detailed description).** The project adopts a highly graduated and integrated approach that is well-adapted to the country context. Initially, the project focuses on establishing an enabling legal and regulatory

[21] Sustainable jobs are referred to as paid direct full-time equivalent (FTE) lasting a minimum of six months created by SMEs who have accessed the line of credit (microloans are assumed to support livelihoods of final beneficiaries and not generate new jobs). Jobs lasting less than one month (or less than 20 days excluding weekends) are not counted to emphasize those jobs that provide more stability through length. Jobs should be converted to FTE. One FTE equals 260 days (excluding weekends) or 12 months. Thus, a job that lasts 4 months should be counted as 1/3 FTE and a job that lasts for 130 days (excluding weekends) should be counted as 1/2 FTE. Number of hours worked per day or per week is not restricted as work hours may vary greatly. Furthermore, Jobs must be formalized with a written employment contract. Lastly, relevance is not placed on remuneration scale for jobs created as there is no regulated minimum wage in Somalia. (For the definition of sustainable jobs, SCALED-UP has chosen to employ a tested model utilized by USAID for its ongoing Growth, Enterprise, Employment, and Livelihoods [GEEL] project in Somalia).

environment for financial and digital development. The project then focuses on stabilizing core institutions and their governance as preconditions for enabling access to basic inclusive financial and government services that offer economic opportunities and expand provision of sustainable jobs. Subsequently, project focus shifts to expanding the coverage and number of service users.

27. **At the core of the project is the establishment of two specialized Somali entities.** The first entity will administer a digital ID system and the second will be an apex MSME Financing Facility to manage a line of credit that the project will make available to eligible financial institutions. The project will provide initial funding to the two institutions with IDA and donor financing. In the case of the MSME Financing Facility, it would be subsequently opened to sequential private sector investing and shareholding through follow-on fund-raising. In this way, the MSME Financing Facility represents the first step in creating a Somali entity with a commercial orientation that can act as a platform to crowd-in additional investments of private capital from international sources, including development finance institutions (DFIs), thereby fostering financial sector development, financial inclusion while sustaining the most dynamic MSMEs and provision of jobs, in a capital-constrained environment.

Figure 1. Components of the Project



Component 1: Strengthening Institutions (SDR 5 million, US$7 million equivalent)

28. **This component is focused on stabilizing core government functions enabling access to services for individuals and businesses.** This is a reform area requiring progress across multiple ministries, departments, and agencies (MDAs) in several areas. This is intended to strengthen governance and institutional effectiveness thereby contributing to building state legitimacy and improving citizens' trust in institutions. The key areas covered by this component are as follows: (a) support to the CBS on improving financial institutions regulations and supervision, promoting efficient financial intermediation and strengthening policies and strategies for digital financial services and expanding financial access; (b) support to the FRC on enhancing its understanding of Somalia's AML/CFT risks, analyzing financial intelligence, and disseminating reports to LEAs as appropriate; (c) support to the Ministry of Posts, Telecommunications, and Technology (MPTT)/NCA to strengthen policy development and effective

regulation of the ICT sector; and (d) support to the MoIFAR to create the legislative and institutional enabling environment for the digital ID system, including the setup and operationalization of a new dedicated ID Authority.

29. **The project proposes to support regulatory technology (RegTech) solutions for financial reporting by financial institutions and communications service providers to regulatory agencies and rigorous data analysis thereby improving the effectiveness of institutions.** The objective is to use RegTech to drive improved and timely regulatory reporting by regulated entities to ensure that they are accurately reporting their financial condition and performance, combined with strengthened management information systems (MIS) used by the regulators for collecting, managing, and analyzing financial data from regulated entities. This will help regulators rigorously assess risks and build robust cases for possible follow up actions. As such, the RegTech solutions will be aligned with principles around data privacy and confidentiality. Other important considerations in the implementation of RegTech solutions will include (a) business modelling to ensure financial sustainability and affordability; (b) operations and technology governance to guarantee convenience and security for data collection, transfer, exchange, and storage; (c) interoperability and interconnection considerations, including a review of application programing interface or web services to be created to provide the interface for reporting entities and how this is to be secured; and (d) the policies, standards, guidelines, and frameworks needed to guarantee a resilient, open and flexible technology solution offering rigorous analytical capability, protection of data privacy, and control of regulatory processes. Alongside support to the MDAs, the Attorney General's Office will be critical to the development of legal and regulatory reform packages. As such, incidental capacity-building support will be provided to the Attorney General's Office on technical drafting of laws and regulations related to this project.

30. **This component includes a focus on support for building a robust ID enabling environment, including the adoption of comprehensive policy and legislative frameworks and the establishment of a competent and well-governed digital ID Authority** (for a detailed sequence of activities refer to table 2.1 in annex 2). Although under the MOU signed by the FGS and NADRA in 2018, NADRA is expected to provide the technical components—for example, software and hardware—for the digital ID system, critical legislative and institutional gaps will need to be addressed to ensure the system's successful implementation. Building a robust legislative and institutional foundation for the digital ID system is critical for mitigating the risk of misuse, building the trust needed in the new system to achieve high coverage and use, and ensuring long-term sustainability. The support for a comprehensive legal framework will help the FGS to, among others, define the basic purposes of the ID system, establish and specifying the mandate, governance arrangements, and functions of the ID Authority, and lay out key system features and principles, such as those related to registration processes, credential issuance, system interoperability, and the use of identity verification and authentication mechanisms for financial service providers and beyond. It will also facilitate the adoption of appropriate policies related to data protection, the rights of data subjects over their data, and cybersecurity, among others. This component will also support the setup of a dedicated and competent ID Authority—operating with legal, institutional, and financial independence—to provide identification services. To ensure that it operates in an inclusive manner and that it remains responsive to a broad set of user needs, the ID Authority's governance structures will aim to include representatives of users and a wide range of stakeholders, including from both the private and public sectors.

31. **Activities to be financed will include provision of goods, consultancy services, capacity building, training, and workshops for carrying out implementation activities supporting policy makers, regulators, and supervisors, and other beneficiaries and stakeholders.** These activities will enable the FGS to (a) develop and implement effective sector policies and strategies and legal and regulatory frameworks; (b) strengthen regulatory reporting, compliance, and transaction monitoring through the use of regulatory technology (RegTech) tools; (c) implement shared IT systems and related utility services for identification verification as well as fraud detection and control; and (d) improve business processes and streamline workflows.

Component 2: Enabling Financial and Digital Services (SDR 14.3 million, US$20 million equivalent)

32. **This component focuses on increasing individuals' and businesses' access to services that expand economic opportunities and help restore resilience in a gender-sensitive manner.** Under this component, the project will support sustainable mechanisms for service delivery. In addition, the project will encourage a gender-sensitive approach to the delivery of targeted services and promote the development of gender-sensitive sector policies and strategies to help address the gender gaps identified. Areas covered by the component are as follows:

(a) Setting up the MSME Financing Facility as a dedicated apex institution providing financing to bank and nonbank financial institutions, with implementation support from the World Bank. Discussions have also been held with IFC to engage in supporting implementation of the facility (see annex 2). The entity will follow private sector management and governance principles, as well as embed AML/CFT controls in accordance with the Financial Action Task Force (FATF) standards. Eligible financial institutions will be those which are appraised by the MSME Financing Facility and meet World Bank Group policies as well as other risk considerations (including environmental and social [E&S] safeguards and AML/CFT risk controls).

(b) Digital ID enrollment for at least the first one million registrants, including dedicated support for outreach to the poorer and marginalized groups, and support for the use of the digital ID for increased financial access through more accurate identity verification and authentication mechanisms available to, among others, mobile money companies, banks, and MTBs.

(c) Government digital payments, construction of interoperable retail payments services, and integrated Government digital services thereby contributing to strengthened systems for revenue mobilization and expenditure management in an increasingly coherent federal government structure for service delivery.

(d) e-business registration services for SMEs through operationalization of one-stop shop (OSS), thereby enabling access to a centralized information service to verify the identity of the beneficial owners of all legal entities operating in Somalia. The digital business registration services would also enable CDD as a pillar of an effective AML/CFT program by financial service providers operating in Somalia as well as the MSME Financing Facility set up under the project.

33. **The MSME Financing Facility will be set up as a dedicated and autonomous Somali body to ensure long-term sustainability.** The entity will be initially publicly funded using IDA financing but would be structured to operate through private sector management and governance principles and with the provision to allow transition toward private sector majority shareholding over time. To avoid crowding-out private sector financing, any subsidy component in the pricing will be explicit and transparent and will be gradually phased out to build a commercial market segment for lending to MSMEs in underserved market segments.

34. **The MSME Financing Facility will be supported by the World Bank Group to build its operational capacity and establish credibility in the market.** The project will also help protect the integrity of the institution by requiring the MSME Financing Facility to operate in accordance with World Bank-reviewed appraisal procedures and standards as a condition of the IDA Grant Agreement and the World Bank project agreement. The World Bank Group implementation support to the MSME Financing Facility will indirectly help build capacity to improve the quality of subproject loan applications prepared by the participating financial institutions (PFIs). This is because the MSME Financing Facility will adopt an MSME Subproject Manual developed with World Bank Group assistance. The key design elements of the MSME Subproject Manual will ensure (a) access to finance by MSMEs in underserved economic segments, especially women and female-owned businesses and (b) clarity, transparency, and administrative efficiency in MSME Financing Facility appraisal operations under a single institution using a single MSME Subproject Manual.

35. **The project will support the MSME Financing Facility to develop the institutional capacity to screen, appraise, and supervise funded subprojects.** This will involve supporting the MSME Financing Facility to manage its operations on a sustainable basis; building capacity in PFIs and other relevant parties; developing standardized documents and procedures for PFIs to use in preparing subproject loan applications and requiring the use of such documents and procedures for subprojects to receive funding from the MSME Financing Facility; and supporting on-demand sub-loan preparation activities, including feasibility studies, transaction advisory support, and other activities that PFIs consider complex. The MSME Financing Facility will operate through two separate financing windows addressing different customer-facing channels and lines of business emphasizing the need to tailor the framework to an individual bank's line of business structure, products, and priorities as follows:

- **A 'large loans' window to cover large loans to SMEs (large businesses).** The eligibility criteria for borrowers would be flexible. However, informal companies would not be accepted. All advances will be in U.S. dollars and all types of credit would be eligible (working capital and investment loans), except trade finance.

- **A 'micro and small loans' window that would be open to SMEs, individuals, and groups**. This will include informal small and microenterprises and groups with a commitment to formalize during the loan repayment period. All advances will be in U.S. dollars and all types of credit would be eligible (working capital and investment loans) except trade finance.

36. **The project will also support enrollment in the digital ID system of at least the first one million registrants.** The project proposes to use an ecosystem approach to rapidly reach high volume and ensure the inclusion of vulnerable and marginalized populations such as women, internally displaced persons (IDPs), and persons living with disabilities. Under such an approach, public and private sector service

providers, local NGOs, and entrepreneurs would also serve as registration agents and/or ID service partners. These stakeholders could also be engaged to raise awareness about the importance of obtaining an ID and could play an active role in designing key features of the ID system itself. To develop an inclusive and collaborative enrollment strategy, the project will build on early analytical work[22] delivered advising the Somali authorities on good practices and will facilitate consultations with the private sector, civil society, and humanitarian agencies. The FGS can draw on lessons from previous biometric registration efforts by WFP and other humanitarian organizations and should explore ways to leverage their existing network of registration partners for enrollment and ID service provision related to the new digital ID system. The planned project activities also include the preparation of a social management plan to address risks of exclusion as well as a comprehensive outreach and communications strategy to be completed before the rollout of the digital ID system to ensure the ID system's accessibility for women and other vulnerable populations, such as persons with disabilities. Collaboration with humanitarian organizations can also be valuable in this context, because they have considerable experience of serving vulnerable communities across the country and can provide guidance on outreach strategies as well as the implementation of an effective project-level grievance redress mechanism (GRM).

37. Activities to be financed will include provision of goods, capacity building, training, workshops, and consultancy services to support stocktaking exercises; implementation of interoperability measures including data exchange protocols, and scheme regulations and rules; procedural reforms, process reengineering, simplified forms and documentation, and digital ID enrollment services; and citizen engagement, consultation, and communication campaigns on delivery of robust and sustainable financial and digital services.

Component 3: Project Management and Coordination (SDR 2.9 million, US$4 million equivalent)

38. **The component will fund project management and coordination activities.** The project will be implemented by the FGS using a single Project Implementation Unit (PIU) anchored in the Ministry of Finance (MoF) in Mogadishu, with a multilayer implementation and oversight structure. The PIU will be responsible for day-to-day project management and will coordinate closely with MDAs covering the project target areas. The PIU will also coordinate activities across the FGS including Federal Member States (FMS). Project focal persons will be appointed and embedded within MDAs covering project target areas. The project will set up a single Project Steering Committee (PSC) comprising the key MDAs to coordinate and oversee the implementation of activities, with attention to sequencing and timing issues, as well as ensuring effective stakeholder consultations and engagements. The project will also fund an independent monitoring agent to provide an added layer of physically monitoring the flow and use of project funds, including the MSME Financing Facility. In addition, funding will be allocated to establish a project-level GRM. Activities to be financed by this component will include provision of goods, consulting services, training, and operating costs of the PIU to support project coordination, implementation, monitoring and evaluation (M&E), and management.

[22] See: World Bank. 2018. *Toward a Robust, Inclusive and Responsible Digital ID System in Somalia*. Washington, DC: The World Bank Group; World Bank. 2016. *Toward a Somali Identification System: ID4D Diagnostic*. Washington, DC: The World Bank.

C. Project Beneficiaries

39. **Direct beneficiaries of the project will be the residents of Somalia, especially women and female owners of MSMEs, who will benefit from more formalization and growth in economic participation.** Women and female owners of MSMEs will derive direct benefit from improved access to financial services through ownership of transaction accounts enabled by the digital ID system and from the MSME Financing Facility. In addition, all those enrolled in the digital ID system and issued a unique ID number will benefit from greater access to financial services by having a robust and verifiable official proof of identity. ID holders, of which 50 percent are expected to be women, will also be more able to participate in the formal economy more broadly and capitalize on economic opportunities arising, for example, from greater freedom of movement, as facilitated by the digital ID system.

40. **Other beneficiaries of this project will be FGS institutions that are key to delivery of targeted financial and digital services.** These include the MoF, MoIFAR, MoCI, MPTT, CBS, FRC, NCA, a new dedicated ID Authority, and the newly created MSME Financing Facility. Banks and nonbank financial institutions participating in the MSME Financing Facility will also directly benefit from the strengthened capacity to provide MSME banking and conduct E&S assessments. The project would enable delivery of support across FMS depending on the readiness of the states.

41. **More broadly, a more robust and inclusive financial and digital ecosystem will benefit the entire Somali population including the economic empowerment of women.** This is accomplished by helping the FGS with clear policies and specific strategies, plans, and road maps to help 'leapfrog' a few development steps and effectively respond to the demands of the domestic economy for robust and inclusive financial and Government services enabled by highly efficient digital infrastructure and an enabling institutional, legal, and regulatory framework.

42. **In addition, the MSME Financing Facility will benefit financial institutions and the market at large through possible links with DFIs attracting additional capital overtime**. The MSME Financing Facility is expected to result in (a) the upstream benefit of raising the standards of subproject preparation by PFIs and (b) the downstream benefit of providing financing to MSMEs based on transparent appraisal of subproject risks and viability as well as eligibility criteria and realization of the Government's commitment to financial inclusion targeting access to marginalized groups including women and female-owned MSMEs.

43. **Over time, once a track record is established, the MSME Financing Facility may raise funds from private investors and DFIs.** To crowd-in investment capital from private sector sources, the MSME Financing Facility is expected to benefit from a range of blending tools consisting of core equity (with the FGS accepting a high-risk for a relatively low return) and/or subordinated/mezzanine debt (with the FGS accepting first losses ahead of private creditors/investors). In this way, private investors (such as DFIs when they can invest further down the line) will be afforded the opportunity to achieve better returns at lower risk than other core equity shareholders such as the FGS, to the extent that they can provide finance and achieve additionality. Equity and subordinate instruments will also help attain leverage of public funds, in line with the MFD approach.

D. Results Chain

Note: The list of activities, outputs, and outcomes are not all inclusive. Component 3 (Project Management and Coordination) is excluded because it primarily relates to administrative activities and does not directly contribute to the PDO and intermediate indicators.

E. Rationale for World Bank Group Involvement and Role of Partners

44. **The World Bank Group brings extensive international experiences in all components of the project.** This includes World Bank-supported interventions establishing digital ID systems, establishing dedicated entities to manage lines of credit, strengthening central banks, Financial Intelligence Units (FIUs), ICT regulators, and promoting access to finance for MSMEs around the world. The World Bank Group also brings strong analytical expertise underpinning reforms and informing decisions and investments. Rigorous diagnostics and studies will continuously feed the project implementation. The proposed M&E Results Framework will generate evidence-based findings that will inform future interventions and adjustments to support financial sector and digital developments in Somalia and beyond.

45. **The MSME Financing Facility is designed to support initial stages of mobilizing investments of private capital in underserved economic sectors in Somalia.** The strategic rationale for the World Bank and proposed IFC supporting the setup of the MSME Financing Facility is two-fold:

(a) By helping the MSME Financing Facility establish credible appraisal standards and other operational and institutional procedures and codifying them in the MSME Subproject Manual (which includes the E&S safeguards assessments), the World Bank and IFC can help the facility demonstrate that its appraisal standards are of a high standard and its institutional integrity is protected by the FGS-World Bank agreements under the project.

(b) World Bank and the proposed IFC support to the MSME Financing Facility can contribute to improved quality of loans provided to MSMEs by PFIs. This is because PFIs will use the IFC implementation TA[23] to inform improvements in credit risk policies used in the evaluation of loan applications seeking funding support from the MSME Financing Facility. Leveraging IFC experience in this regard will be critical for the MSME Financing Facility as it will signal to the market that the quality of its appraisal standards, governance and other internal controls are high.

46. **The World Bank has the convening power to bring to Somalia technical expertise, best practices, and lessons learned from around the world.** The World Bank Group has unique advantages to convene both public and private stakeholders and local, national, and global levels of expertise at all the stages of the project. In 2014, the World Bank established the Identification for Development (ID4D) program, which provides dedicated support on the design and implementation of digital identification systems, building on a growing body of evidence and good practices from across the globe. ID4D will provide specialized expertise for strengthening the enabling environment and mass registration for the digital ID system, including through providing practical advice from members of ID4D's Technical Expert Group.

47. **The project builds upon experiences and accomplishments of SCORE (P152241) and ICT Sector Support in Somalia Phase II (P152358) projects.** These operations involve strengthening legal and regulatory foundations, institutional capacity, and financial and telecommunications infrastructure.

[23] See annex 4, box 4.1 for a description of IFC's Financial Institutions Development Program (FIDEP) (ID: 602159) currently under preparation.

Several proposed activities are incremental improvements that scale up past accomplishments (see box 2).

48. **The project is closely linked to the World Bank's project - Somali Electricity Access Project (SEAP, P165497, approved by the Board in December 2018).** SEAP's objective is to expand electricity access in targeted urban, peri-urban, and rural communities in Somalia. SEAP is expected to increase access to affordable and reliable renewable energy services for households and small businesses by incentivizing private companies in the off-grid solar photovoltaic sector to enhance their business operations and reach currently untargeted populations. SEAP will leverage the MSME Financing Facility under the project to support MSMEs within the renewable energy value chain as one of its target sectors. It is expected that MSMEs supported under SEAP will also be strong candidates for commercial financing under the MSME Financing Facility.

49. **The project complements other development partner programs addressing access to financial and digital services in Somalia.** The MSME Financing Facility will act as a vehicle through which the FGS, DFIs, and other donors could channel additional funds to build up market-based financial intermediation at the lower end of the financial sector. In this way, the MSME Financing Facility helps the FGS (a) coordinate donor funding to the poorest segment of financial services customers, thereby avoiding possible duplication of efforts and distortion of markets; (b) kick-start MSME banking in key underserved service and productive sectors by supporting the PFIs to scale up rapidly and become sustainable; and (c) build sustainable mechanisms for advancing market-based financial intermediation by instilling a commercial orientation to MSME banking by PFIs supporting the lower end of the financial sector. On the financial intermediation front, there are two main donor programs in operation that the project will closely coordinate with: (a) Swedish International Development Cooperation Agency Partial Guarantee, and; (b) Nordic Horn of Africa Fund. On the TA side, USAID's Growth, Enterprise, Employment, and Livelihoods (GEEL) Project is working to develop a few selected agricultural product value chains by providing specialized technical support. The MSME Financing Facility introduces private sector orientation and MFD-enabling dimensions to the financial intermediation interventions. This is very much part of the institution building agenda and value addition envisaged with possible involvement of IFC in provision of implementation support. On the energy side, the World Bank developed a study in cooperation with Lighting Africa on 'Market Assessment of the Off-grid Solar Lighting Sector in Somalia' that was completed in March 2018 and helps to uncover the market demand for off-grid systems.

50. **On the digital ID side, the project is supporting the FGS to set up a foundational digital ID together with the institutional and legal framework.** This provides an opportunity for the FGS to leverage the lessons learned from previous registration experience of humanitarian agencies such as the WFP for achieving high coverage and ensuring the robustness of the foundational digital ID. The World Bank has developed two studies in cooperation with the United Nations Development Programme (UNDP) which suggests pathways to building robust digital ID system in Somalia. The first of these ('Toward a Somali Identification System: ID4D Diagnostic') had been completed in 2016, and the second ('Toward a Robust, Inclusive and Responsible Digital ID System in Somalia') was completed in June 2018.

51. **On enhancing the integrity of financial markets, the project builds on the NRA delivered under the SCORE Project (P152241) and supplements support provided by other developing partners.** The U.S. State Department has been providing some support to the FRC and CBS in the form of AML/CFT mentors and capacity building as well as improving physical security of FRC premises, while the IMF has been

engaged in the financial sector, through a legal review of CFT laws and regulations, and with the CBS mainly through the SMP. The European Union has been channeling support jointly with UNDP to the justice sector through the Joint Justice Program which is being implemented by UNDP. The program foresees capacity building to the Attorney General's Office, including the possible establishment of specialized units to deal with cases relating to juveniles, gender-based violence (GBV), or corruption.

F. Lessons Learned and Reflected in the Project Design

52. **The following lessons learned from similar projects in Somalia as well as from other international experiences were considered in the design of the project:**

- **Fragile security situation.** Operating in a fragile and conflict-affected country and all-around capacity weaknesses affects the project both in terms of the safety of staff and contractors, as well as implementation time lines of project activities and budgets due to high costs of client hand-holding efforts and challenging logistics within the country. Client absorptive capacity will be continually assessed and interventions carefully calibrated. Similarly, the security situation will continually be assessed. 'Duty of Care' responsibilities will be upheld always to ensure the health, safety, security, and well-being of all staff and contractors. The project will maintain high level of planning and coordination of activities on an ongoing basis and adjust as needed to achieve successful project activities and outcomes.

- **Fiscal sustainability.** Somalia is highly fiscally constrained meaning the adoption of new budgetary units should be treated with caution and managed carefully in coordination with the MoF. The project adopts the following measures: (a) Government financing: to ensure sustainability, solution selection will be based on confirmation of adequate sources of funds needed to meet operations and maintenance costs of completed service facilities, and; (b) stakeholder participation: stakeholder participation is crucial in solution identification and preparation and in securing stakeholder contributions in cash or kind. Local ownership of completed service facilities would also provide additional assurance of subsequent sustainability of operations and maintenance. Moreover, while the structure of the MSME Financing Facility is initially publicly financed, the intent is to transition to majority private sector shareholding over time and use public capital to private leverage funding which contributes to fiscal sustainability in the medium term.

- **Autonomous project management and staff competency.** There is a need for highly efficient project management capacity that can cope with many beneficiary MDAs and management of the MSME Financing Facility. The management of the MSME Financing Facility will use private sector governance principles covering an independent board of directors, an outside advisory panel, and recruitment of competent management staff through open competition.

- **Risk mitigation through a phased and iterative approach to project implementation and institutional reform, based on technical assessments.** The first phase of the project will support the building of the enabling policy, legal, and regulatory frameworks and the setting up of the specialized entities. This will be followed by efforts to scale up access to the basic services targeted by the project. Iterative technical assessments will be essential to ensure

healthy and sustained delivery of services beyond the life cycle of the project through the provision of technical experts and more complete and relevant analytical work on sustainable business models. In all cases, project support will ensure transparency and accountability on all procurements and financial governance issues. This will be aimed at affording the FGS the opportunity to generate a complete evidence base and information needed to renegotiate unfavorable contract terms and/or correct technical weaknesses or gaps in service facilities or business model sustainability including addressing cybersecurity risks.

- **E&S safeguards mitigation.** During the selection of subprojects, strict screening of E&S safeguards is necessary, which will also determine investment needs to provide appropriate mitigation measures.

53. **The design of the MSME Financing Facility is based on lessons learned from across similar financial sector development projects offering lines of credit.** The MSME Financing Facility is intended to serve as a stepping stone that facilitates the adoption of traditional lending by Somali financial institutions and create sufficient scale of market-based funding to MSMEs in nontraditional sectors which generally have difficulties accessing finance. The MSME Financing Facility target sectors include energy and livestock. Lessons were drawn from previous World Bank projects in Afghanistan (ARTF-Microfinance [P091264]), Indonesia (Indonesia Infrastructure Guarantee Fund Project [P118916]), Yemen (Yemen Emergency Electricity Access Project [P163777]), Rwanda (Rwanda Housing Finance Project [P165649]), Kenya (Kenya Affordable Housing Finance Project [P165034]) and Pakistan (Pakistan Housing Financing Project [P162095]) whereby public funding created the market opportunities while operations were on private sector principles and in some cases, with an enabling provision to allow private sector participation and majority shareholding over time. This was confirmed in the Letter of Policy Commitments from the Prime Minister, dated January 22, 2019 (see annex 6). As such, the charter for the MSME Financing Facility will create a domestic Somali entity with a commercial orientation that can act as a platform and benefit from blending tools to crowd-in additional private and public financing from other sources including DFIs. It also creates a revolving fund able to create sufficient scale through multiple financing rounds. This will help to gain trust and reduce the risk perceived by lenders in MSMEs sectors and by private investors in Somali financial institutions.

54. **The project also draws on lessons learned from other ID projects and on the wealth of analytical and global convening work on identification by the World Bank's ID4D program.** The 10 Principles on Identification for Sustainable Development, which have been endorsed by over 24 development partners, United Nations agencies, and private sector organizations, synthesize lessons learned from around the globe about maximizing the benefits of identification systems for development while mitigating important risks. The proposed digital ID system's design and implementation strategy will be aligned with the Principles, including with regard to the accessibility of the system, the adoption of robust, secure, responsive, and sustainable system features and technologies, and governance arrangements that facilitate trust and help protect privacy and user rights. This was confirmed in the Letter of Policy Commitments from the Prime Minister, dated January 22, 2019 (see annex 6). To this end, the ID Authority will include representatives of users and a wide range of stakeholders, including from both the private and public sectors within its governance structures such as its board. A public entity with a dedicated mandate for ID service provision and with legal, institutional, and financial independence will be more likely to operate in an inclusive and efficient manner, to be responsive to user needs, and build up public

trust due to its greater perceived political neutrality. To be able to effectively implement the digital ID system, the ID Authority will also need to have sufficient capacity, including capable and dedicated staff, to manage large-scale registration efforts, safeguard the integrity of identity data, and ensure integration of the ID into service delivery.

III. IMPLEMENTATION ARRANGEMENTS

A. Institutional and Implementation Arrangements

55. **The project will adopt a layered and inclusive project oversight structure to ensure coordination among different participating government stakeholders.** The MoF will be the executing agency of the project. The project will set up a single Project Steering Committee (PSC). The PSC, headed by the MoF with representatives from the MoCI, MPTT, MoIFAR, CBS, FRC, NCA, and the new ID Authority, will provide policy guidance and monitor the progress through the Secretariat, represented by the Director General in the MoF. The FGS can make changes in the membership composition of the PSC or its terms of reference (TOR) in consultation with IDA. Furthermore, the MoF will appoint an independent board of directors in accordance with the charter of the MSME Financing Facility. In turn, the board of directors will appoint a competent management and investment committee selected through a clearly defined TORs and criterion which are set out on the Project Operations Manual (POM) including an annex MSME Subproject Manual. The FGS will submit to IDA for review and clearance the proposed charter of the MSME Financing Facility, TORs for the board of directors and management, job descriptions for directors/staff proposed to be recruited, and MSME Subproject Manual.

56. **The existing SCORE Project (P152241) PIU in the MoF, created in 2016, will implement the project.** An effective management structure is in place, and the PIU had demonstrated its capacity to deliver results efficiently. It has established a strong track record of performance, has familiarity with the World Bank's fiduciary guidelines, as well as functional MIS and M&E systems. Lessons learned from the implementation arrangements for the predecessor SCORE and ICT Sector Support projects have been considered when designing implementation arrangements for this project.

57. **The PIU will coordinate activities across the FGS where necessary at the FMS level, making it unnecessary to establish subsidiary implementation arrangements with the FMS.** The PIU will include focal persons from MDAs to coordinate and oversee the implementation of activities at sponsoring MDAs, with attention to sequencing and timing issues, as well as ensuring effective stakeholder consultations and engagements. As such, the project would enable delivery of support across the FMS depending on the readiness of the states.

58. **The duties and functions of the PIU will include** (a) providing assistance to MDAs (including the FMS depending on the readiness of the states) and initial support to the MSME Financing Facility in preparing priority investment programs; (b) appointing consultants and stakeholders for specific assignments, including participation in the supervision of technical solutions requiring stakeholder participation; (c) monitoring quality and costs of executed assignments; (d) validating results on the ground through stakeholders and third parties, as needed; (e) establishing proactive communications and consultations with project stakeholders; (f) coordinating with MDAs, the MSME Financing Facility, and the private sector; and (g) revising and updating documents governing PIU staffing hiring. To facilitate early project readiness, the PIU will support the MSME Financing Facility in the initial setting-up period. As a

condition of project effectiveness, the authorities will submit to IDA a satisfactory POM that the PIU would follow in helping MDAs and others to prepare and implement project activities. The POM would specify the managerial, financial, administrative, procurement, environmental, and social safeguard policies and procedures for the execution of the project as well as operating the GRM, and the eligibility criteria for the selection of PFIs and final beneficiaries of the MSME Financing Facility. Similarly, as a condition of disbursement under the MSME Financing Facility, the authorities will prepare and submit to IDA a satisfactory MSME Subproject Manual (forming an annex or schedule to the POM).

59. **The MoF will establish the MSME Financing Facility to provide funding and capacity building to PFIs.** For the dedicated entity to have credibility in the market, the newly established institution must quickly demonstrate that it has the capacity to appraise projects on technical and financial merits, and that it will be allowed to operate as an independent institution with the mandate for appraisal of all PFIs requiring access to the MSME Financing Facility. It will take some time for the entity to develop full in-house capacity to appraise projects. As such, there is a need for investment advisory support for the entity to demonstrate early on that its appraisal standards are not only sound, but that they will also stand the test of time and occasional pressure when the institution is forced to reject popular projects which are not financially or technically viable.

60. **The MSME Financing Facility will be managed by a board of directors and a competent management team.** The independent board of directors (majority private sector) will be assigned oversight responsibility for the MSME Financing Facility and hiring of a professional management team which will include competency in environment and social safeguards assessment and other technical areas to support effective operations. The MSME Financing Facility setup will include an external advisory board to provide specialists' advice on specific topics to the board of directors and management.

61. **Under the project, the selection of PFIs will be done by the MSME Financing Facility without undue outside interference.** The participation of banks and nonbank financial institutions in the MSME Financing Facility will be based on criteria that will ensure their capacity to implement as well as embed World Bank Directive on Investment Policy Financing and draw on the IFC investment standards. The E&S management consultant will be involved in the identification exercises undertaken by this entity. The selection criteria related to the World Bank Directive focuses on adherence to prudential regulatory ratios, minimum capital and operational standards, appropriate governance, policies, and risk management functions. PFIs will be subjected to fit and proper tests, AML/CFT controls, and reporting obligations to the FRC and will fall under the supervision of the CBS, according to FATF standards and the Somali AML/CFT legal framework, based on their risk. Additional requirements may be set out in the MSME Subproject Manual. Segregation of duties and responsibilities will ensure that all MSME funding requests are assessed by PFIs and not the MSME Financing Facility. The MSME Financing Facility will assess PFIs' eligibility to participate against well-established selection criteria set out in the MSME Subproject Manual to avoid possible undue political interference. The MSME Financing Facility will submit, once each quarter, 'MSME Financing Facility Quarterly Progress Reports (QPRs)', no later than one month after the end of that quarter, to its board of directors and IDA for review and clearance.

62. **The QPRs are to be provided to the Board of Directors, World Bank Group, and other stakeholders.** These reports will be reviewed by World Bank and commented upon, as neccessary. Biannual reviews based on quarterly reports prepared by the MSME Financing Facility will form the basis of at least two implementation support reviews per year. An independent monitoring agent hired under

the project will provide an added layer of physically monitoring the flow and use of the MSME Financing Facility by PFIs and final beneficiary verifications and reporting cases of fraud and corruption complaints by submitting periodic inspection reports covering standard audits of PFIs and sample checks of compliance in line with the accountability framework set out in the MSME Subproject Manual. These reports will be submitted to the board of directors, the MoF, and other participating investors and the World Bank Group for review and clearance. The monitoring agent will complement the safeguards responsibility of the MSME Financing Facility and will also act as an 'early warning' whistleblower in case governance issues are detected. The QPRs and monitoring agent periodic inspection reports will inform, among other issues, (a) perfomance indicators, (b) compliance with remedial actions to be taken for E&S safeguards and GRM, (c) implementation progress of activities, and (d) status of funds. At the end of the second year, the FGS and World Bank will carry out a joint midterm review of progress made in carrying out the project.

B. Results Monitoring and Evaluation Arrangements

63. **Results M&E will involve both the PIU measuring and monitoring results and a World Bank review.** The PIU will be responsible for monitoring and reporting results. The newly established M&E Unit in the PIU will systematically gather and enter data from different sources into an MIS, thereby constantly keeping it updated. The M&E function is expected to develop an M&E plan and socialize with the PIU and other stakeholders highlighting the theory of change, data collection methodology with time line and definitions of indicators. For specific monitoring activities on the MSME Financing Facility and digital ID services, the FGS will establish autonomous management bodies that will be assigned oversight and M&E responsibilties. The MSME Financing Facility may procure a technology-based solution that will allow PFIs to report efficiently. An external M&E specialist may also be hired to conduct MSME beneficiary surveys to measure satisfaction with quality of on-lending processes and services provided by PFIs. As part of the ID services subcomponent, the autonomous entity will be responsible for measuring key enrollment statistics, as well as conducting surveys of registrants and spot checks to measure service delivery and satisfaction of the planning and enrollment process of the digital ID system. All other PDO and intermediate-level monitoring activities will be monitored and reported on by the M&E Unit in the PIU. Strategic alliances will be established with communities, final beneficiaries, and PFIs to support M&E efforts. The PIU will ensure that the M&E specialist is equipped with the tools and capacity to undertake their duties effectively and will capacitate the rest of the PIU to understand their role in contributing to project results in addition to implementing project activities.

C. Sustainability

64. **Somalia is fiscally constrained, meaning that the adoption of new budgetary units under the project will be treated with caution and managed carefully in coordination with the MoF to ensure fiscal sustainability.** The selection of solutions will be based on confirmation of adequate sources of funds needed to meet operations and maintenance costs of completed service facilities, including confirmation of stakeholder contributions in cash or kind which contributes to fiscal sustainability. In this regard, fiscal sustainability of service delivery from project interventions will be ensured by (a) requiring full stakeholder involvement in solution selection; (b) requiring the subsidy component, if any, in pricing by the MSME Financing Facility to be explicit and transparent and gradually phased out as a commercial market segment

is established for lending to MSMEs in underserved key sectors such as energy and livestock[24]; and (c) reviewing responsibility for operations and maintenance costs as an explicit feature of project validation/confirmation at the time of design of specific solutions and rejecting solutions with inadequate or no provisions for sustainability. For digital Government services, the responsibility for sustainability of completed service delivery facilities resides with the MDAs in consultations with the MoF to ring-fence annual operation and maintenance budgets. The project-supported MDAs will be given training in accounting, setting user fees, banking, and technical aspects of managing operational and maintenance costs. Beneficiaries will be given awareness training on sustainability of service delivery as well as E&S safeguards and GRM aspects of the project.

65. **The MSME Financing Facility will be a dedicated Somali institution set up to operate a revolving fund offering a line of credit to PFIs on market terms.** To ensure sustainability, the MSME Financing Facility will use market tools and target improved risk appetite and capacity of Somali financial institutions and MSMEs. PFIs will assume the credit risk for on-lending to final beneficiaries and follow their respective pricing policies considering prevailing market conditions, thereby supporting sustainable enterprise financing, growth, and employment. The lending rates charged by the MSME Financing Facility will mirror current market terms. Research by Batra and Mahmood (2003) showed that "credit programs may produce good results if credit is provided at market rates."[25] As such, loans to final borrowers will be priced to cover costs to ensure efficient use of resources. PFIs will be required to comply with established eligibility criteria which will include compliance to central bank regulations particularly on asset clarification as well as risk and internal controls (as and when they are developed by the CBS). For noncompliant PFIs, the project is proposing offering conditional eligibility which will link the level of access to the MSME Financing Facility to performance of the affected PFI on a Financial Institutions Development Plan (FIDP). Conditional eligibility will only apply to marginal cases of noncompliance that are unlikely to threaten the financial integrity or sustainability of the MSME Financing Facility. Conditional eligibility will be subject to satisfactory performance on the FIDP with potential for phasing out PFIs in cases of unsatisfactory performance on the FIDP. The financing under conditional eligibility will be capped to a certain percentage of the MSME Financing Facility at a point in time to manage and mitigate risks of moral hazard by PFIs. PFI eligibility criteria will be elaborated upon in the MSME Subproject Manual.

IV. PROJECT APPRAISAL SUMMARY

A. Technical, Economic, and Financial Analysis

66. **Economic and financial analysis.** The nature of project activities (that is, largely technical advisory services, diagnostic, capacity building, and institutional strengthening) under Component 1 makes direct attribution of economic and financial benefits resulting from supporting economic institutions challenging. However, the results chain illustrates how activities related to improved institutional capacity

[24] List of the relevant costs—cost of funds—include operational costs, loan loss expenses, and a small profit margin. See table 4.1 in annex 4 (Financial Intermediary Financing) for a detailed discussion on components of the costs of funds. The project proposes to adjust annually the apex pricing to recalibrate lending rates to market developments including potential inflationary pressures.

[25] Batra, Geeta, and Syed Mahmood. 2003. "Direct Support to Private Firms: Evidence on Effectiveness." World Bank Policy Research Working Paper No. 3170. Available at SSRN: https://ssrn.com/abstract=636589.

contribute to the objectives of increased access to financial and digital services and sustainable employment.

67. In the case of Component 2, at least 1 million people will be enrolled in the digital ID system, or which technical components will be provided NADRA, enabling financial access and ownership of at least 900,000 transaction accounts covering mobile money, bank and nonbank financial institutions, and MTBs. The project is expected to finance 200 small enterprises and 30 large enterprises, supporting sustainable employment by these beneficiaries, and initially 1,600 microloans to microenterprises and individuals will be financed during the first lending cycle in support of livelihoods and economic empowerment of individuals especially women and female-owned microenterprises. As such, significant economic benefit is expected to be derived from Component 2 activities.

68. Broadly speaking, the project is expected to increase efficiency in financial intermediation and support robust delivery of basic Government services. This will enable broad-based economic empowerment and effective participation in the economy. The project will contribute to sustainable employment and economic empowerment of women through the increase and diversification of financing for MSMEs. The project will do so by easing financial access constraints, catalyzing the mobilization of additional private capital by financial institutions, and rolling out a foundational digital ID system enabled for use in the financial sector.

69. The project will also promote demand for the digital ID and its use for financial services in support of safe and low-cost access to retail payment services for remittance and Government payments. Robust digital IDs can help reduce AML/CTF risks by enabling financial institutions to reliably verify the identities of their customers, including through e-KYC and other biometrically supported authentication processes, and to monitor transactions more effectively. Digital IDs and interoperable payment systems can also help lower the cost and increase the efficiency for the delivery of government to person (G2P) and social protection payments.

70. The expected economic benefits by project subcomponent are as follows:

- **MSME Financing Facility/line of credit.** The project will promote gains in productivity and sustainable employment in MSMEs. This is because access to finance could lead to creation and/or expansion of enterprises and products. The MSME Financing Facility is also expected to have positive spillover effects, including creating additional business, and increasing productivity and competitiveness. This subcomponent will help improve efficiency of the MSME credit market and expand the availability of funding to MSMEs. The benefits for PFIs include access to new clients, enhanced credit policies, and portfolio diversification. This could enhance profitable MSME banking to viable enterprises and reduce PFIs' nonperforming loans (NPLs). The MSME Financing Facility will target women and female-owned MSMEs.

- **Digital ID rollout.** A digital identification system has the potential to generate significant economic benefits and savings for the FGS and the Somali private sector. Examples from across the world demonstrate that robust, inclusive, and responsible foundational ID

systems can act as powerful drivers of sustainable development.[26] Digital ID systems have demonstrated particularly strong potential for boosting financial inclusion and promoting equitable access to economic resources, including for the most vulnerable segments of the population such as persons with disabilities.[27]

- **Government and retail payment services.** This project will also help support efficient services by easing the transactional burden of paying taxes, business registration, and promoting the digitization of Government payments and reduce leakages by leveraging the digital economy and technology to enhance financial management (FM) and control. Potential fiscal savings through the reduction of error, fraud, and corruption and duplication of costs could exceed the initial investment and recurrent operating costs of the digital ID system and NPS in Somalia. Economic benefits to the public sector could also be accrued through increasing tax collection. Additional revenues may be generated by charging fees for various Government digital services, but the revenue-seeking activities should not compromise the accessibility of the system to all. The increase in the digitization of Government payments will also likely result in cost-savings to the Government. The combined benefits to individuals, to the overall economy, and to the fiscal situation suggest a high rate of return; however, those benefits are inherently difficult to measure due to data limitations.

71. Of the project's subcomponents, only the MSME Financing Facility is susceptible to a meaningful net present value (NPV) analysis. The beneficiaries of the MSME Financing Facility are the PFIs and final beneficiary MSMEs. It is expected that during the project duration, MSME financing would reach approximately 230 SMEs, out of which 200 are small loans (US$5,001–US$50,000) and 30 SMEs will receive large loans (large loans are classified as US$50,001–US$150,000) and 2,900 microloans (microloans are classified as US$1,001–US$5,000). Unlike the large and small SME loans which have longer repayment periods, the microloans are intended to have a maximum tenor of 18 months. This entails that microloans will be recycled once during the project lifetime. The first lending cycle is expected to disburse 1,600 microloans and the second cycle will disburse 1,300 microloans bringing the total microloans disbursed during the project lifetime to 2,900 microloans.

72. Evidence from the existing literature and analysis on the impact of interventions to facilitate access to finance for MSMEs is mixed. Initial studies found that MSME financing is expected to result in direct and indirect[28] job creation. For example, based on the Independent Evaluation Group evaluation of World Bank credits to SMEs in Sri Lanka, the 'average beneficiary' expanded employment by 22 to 56 employees. Other studies also find the association between finance and job growth to be stronger among MSMEs (Ayyagari, Demirgüç-Kunt, and Maksimovic 2011).[29] The IFC study (2013) finds that improving access to finance for SMEs can create jobs by establishing new businesses and by expanding existing

[26] See, for example: Gelb, A., and A. Diofasi Metz. 2018. *Identification Revolution: Can Digital ID Be Harnessed for Development?* Washington, DC: Center for Global Development.
[27] World Bank. 2018. *G20 Digital Identity Onboarding*. Washington, DC: World Bank. Available from: https://www.gpfi.org/sites/default/files/documents/G20_Digital_Identity_Onboarding_WBG_OECD.pdf.
[28] This project will not be counting indirect jobs.
[29] Ayyagari, M., A. Demirgüç-Kunt, and V. Maksimovic. 2011. "Small vs. Young Firms Across the World - Contribution to Employment, Job Creation, and Growth." Policy Research Working Paper 5631 (The World Bank Development Research Group).

ones.[30] More recent studies report that the impacts of providing access to finance on employment are very modest. For example, Cho and Honorati (2013) reviewed more than 100 evaluations of programs that provided support to SMEs and Grimm and Paffhausen (2014) reviewed 139 studies that evaluated SMEs interventions in providing access to finance.[31] Study findings underscore that finance and training interventions to promote MSME development are more effective in changing intermediate outcomes like business knowledge than in increasing jobs. For microenterprises, some studies find evidence of creation of new jobs.[32] Nevertheless, a recent paper shows that larger, individual-liability loans offered to growth-oriented women entrepreneurs in Ethiopia had an impact on accelerating growth in the business incomes and employment levels of women-owned enterprises (Alibhal, Buehren, and Papineni 2018).[33]

73. While there is a large amount of empirical evidence on the effects of MSME growth on jobs, there is limited evidence of SME financing interventions on the impact of productivity, profits, and sales. Overall, SME support has a positive impact on firm performance and labor productivity (Cravo and Piza 2018).[34] Cho and Honorati (2013) [35] reviewed more than 100 evaluations of programs that provided support to SMEs. The findings show that finance and training interventions to promote MSME development are more effective in changing intermediate outcomes like business knowledge than in increasing jobs. Several studies find that the SME credit line program does not have an impact on profits (Angelucci, Karlan, and Zinman 2013;[36] Augsburg et al. 2012[37]). Of the studies focusing on revenues and business expenditures, most do not detect any effects either (Banerjee et al. 2013;[38] Karlan et al. 2011[39]). Results from several evaluations suggest that it takes time for SME finance to influence productivity.

[30] IFC Jobs Study: 'Assessing Private Sector Contributions to Job Creation and Poverty Reduction', January 2013.
[31] Grimm, Michael, and Anna Luisa Paffhausen. 2014. "Do Interventions Targeted at Micro-Entrepreneurs and Small and Medium-Sized Firms Create Jobs? A Systematic Review of the Evidence for Low and Middle Income Countries." IZA Discussion Papers 8193, Institute for the Study of Labor (IZA).
[32] Grimm, Michael, and Anna Luisa Paffhausen. 2015. "Do Interventions Targeted at Micro-Entrepreneurs and Small and Medium-Sized Firms Create Jobs? A Systematic Review of the Evidence for Low and Middle-Income Countries." *Labour Economics* Volume 32.
[33] Alibhal, S., N. Buehren, and S. Papineni. *Better Loans or Better Borrowers? Impact of Meso-Credit on Female-Owned Enterprises in Ethiopia.*
[34] Cravo, Tulio A., and Caio Piza. 2016. "The Impact of Business Support Services for Small and Medium Enterprises on Firm Performance in Low- and Middle-Income Countries: A Meta-Analysis." Policy Research Working Paper No. 7664, World Bank, Washington, DC. https://openknowledge.worldbank.org/handle/10986/24501 License: CC BY 3.0 IGO.
[35] Cho, Yoonyoung, and Maddalena Honorati. 2013. "Entrepreneurship Programs in Developing Countries: A Meta Regression Analysis." Social Protection and Labor Discussion Paper No. 1302, World Bank, Washington, DC. https://openknowledge.worldbank.org/handle/10986/13568 License: CC BY 3.0 IGO.
[36] Angelucci, Manuela, Dean Karlan, and Jonathan Zinman. 2015. "Microcredit Impacts: Evidence from a Randomized Microcredit Program Placement Experiment by Compartamos Banco: Dataset." American Economic Journal: Applied Economics. http://dx.doi.org/10.1257/app.20130537.
[37] Augsburg, Britta, Ralph De Haas, Heike Harmgart, and Costas Meghir. 2012. "Microfinance at the Margin: Experimental Evidence from Bosnia and Herzegovina." Available at SSRN: https://ssrn.com/abstract=2021005 or http://dx.doi.org/10.2139/ssrn.2021005.
[38] Banerjee, Abhijit, Esther Duflo, Rachel Glennerster, and Cynthia Kinnan. 2013. "The Miracle of Microfinance? Evidence from a Randomized Evaluation." https://www.poverty-action.org/sites/default/files/44-_june_2010-_miracle_of_microfinance.pdf.
[39]Karlan, Dean, and Jonathan Zinman. 2011. "Microcredit in Theory and Practice: Using Randomized Credit Scoring for Impact Evaluation." *Science* 332 (6035): 1278–1284.

74. Impacts of SME finance on capital investment as well as firm performance. Firms have seen an increase in sales and revenues after accessing SME finance.[40] A systematic review of the SME finance literature suggest that SME finance programs should target SMEs that are credit constrained. Banerjee et al. (2014) report that Indian SMEs benefiting from a priority lending report an increase in sales and profits.[41]

75. For fragility, conflict, and violence (FCV) affected countries, there is no readily available study on the MSME finance multiplier effect. The SCORE Project (P152241) applied a multiplier of 4x on output on the support provided. The supported firms would yield an increase in output ('benefits multiplier') at a multiple of 4 times (4x) the support provided with a lag of two years. However, this was a grant scheme. In the following scenario analysis, under base-case scenario, benefits multipliers of 2x for SME large loans, small loans and microenterprises have been used. Due to difficulty in accurately estimating job creation, the secondary impacts in terms of increased employment income have not been included in the calculation of economic NPV and internal rate of return (IRR). Because of increased efficiency and capacity utilization, the supported firms would yield an increase in output ('benefits multiplier') at a multiple of two times (2x) for SMEs with small, large loans, and micro loans with a lag of two years. The multiplier will have an effect for one year only. After that, the multiplier will become stagnant if no new investment is made.

76. Base-case and low-case results. For a 12 percent discount rate and 3x output for SMEs with large loans, 2x output for SME with small loans and for microenterprises, the economic NPV for the line of credit is estimated at US$ 3.8 million. The IRR is estimated at 19 percent. Sensitivity analysis reveals that the most important input variable is the benefits multiplier. Even with a lower multiplier for micro loans as shown in the low scenario, the project remains viable. However, at a discount rate of 16 percent, the NPV could become negative. These assumptions are very conservative. These results are also robust at various discount rates. See table 1.

77. Because no data are available, the project will collect data from every firm that gets a loan on basic variables such as sales, output, revenues, costs, profits, and employment as a baseline. After two years, or at the midterm review, a new estimation of the model will be conducted.

Table 1. Sensitivity Analysis of the MSME Financing Facility (NPV in US$, millions)

Benefits Multiplier	**Low Scenario** **3x (SME large loans)** **2x (SME small loans)** **1.5x (micro loans)**	**Base Scenario** **3x (SME large loans)** **2x (SME small loans)** **2x (micro loans)**
Discount rate		
Low 8%	4.22	6.73
Base 12%	1.66	3.78
High 16%	−0.35	1.45
IRR (%)	15	19

[40] Kersten, Renate, J. Harms, K. Liket, and K. Maas. 2017. *Small Firms, Large Impact?* World Development Report. Volume 97.
[41] Banerjee, Abhijit V., and Esther Duflo. 2014. "Do Firms Want to Borrow More? Testing Credit Constraints Using a Directed Lending Program." The *Review of Economic Studies* 81(2): 572–607, https://doi.org/10.1093/restud/rdt046

B. Fiduciary

(i) Financial Management

78. The External Assistance Fiduciary Section (EAFS) Unit established within the office of the Accountant General in the FGS' MoF will have FM responsibility. With guidance from the Accountant General, the EAFS Unit in consultation with the respective PIU and beneficiary institutions, will provide day-to-day FM. For the revolving fund, the FM arrangements, controls, and oversight procedures will be extended to cover the FM aspects as shall be detailed in the POM. The effectiveness of the EAFS Unit alongside other key functional units will be monitored while key areas of capacity strengthening will be identified and supported through the project. The existing organizational and functional structure of the EAFS Unit will be maintained and further strengthened to provide effective FM for the project. All project FM transactions will be reported through the Government financial management information systems (FMIS). The EAFS Unit, with the support of the Accountant General's Office, will ensure that (a) important business and financial processes are adhered to; (b) internal controls and procedures are in place and adequately enforced; (c) unaudited interim financial reports (IFRs) are prepared on a timely basis; (d) project financial statements are prepared on a timely basis and in accordance with International Public Sector Accounting Standards (IPSAS) cash-basis; and (e) external audit is completed on time and audit findings and recommendations/issues raised in the management letter are implemented expeditiously.

(ii) Procurement

79. Procurement will be carried out in accordance with the requirements in the World Bank Procurement Regulations for IPF Borrowers: Goods, Works, Non-Consulting Services and Consulting Services, dated July 1, 2016 (revised November 2017 and August 2018); Guidelines on Preventing and Combating Fraud and Corruption in Projects Financed by IBRD Loans and IDA Credits and Grants (revised as of July 1, 2016); and provisions stipulated in the Financing Agreement. Given Somalia's FCV country status, procurement will be processed under the special procurement arrangements referred to in paragraph 12 of the World Bank Policy on Investment Project Financing, dated November 10, 2017.

80. **Project Procurement Strategy for Development (PPSD) and Procurement Plan (PP).** The World Bank's New Procurement Framework will apply to this project. In this regard, the task team together with the borrower have prepared the PPSD, based on which the PP for the first 18 months has been prepared. The PP sets out the selection methods to be followed by the recipient during the project implementation in the procurement of goods, works, and consulting services. The PP also include the cost estimates, time schedules, the World Bank's review requirements, brief description of the activities/contracts, and so on. The PP will be updated at least once in 12 months or as required to reflect the actual project implementation needs, but each update shall require World Bank Group approval. All PPs will be publicly disclosed in accordance with the World Bank Group's disclosure policy.

81. **Systematic Tracking of Exchanges in Procurement (STEP).** The World Bank Group's STEP system will be used to prepare, clear, and update PPs and conduct all procurement transactions for the project.

C. Safeguards

(i) Environmental Safeguards

82. **The World Bank Group has screened the project components and has determined that this project is Category B.** OP 4.01 (Environmental Assessment) is the relevant World Bank Operations Policy for environmental safeguards. The client has prepared an Environmental and Social Management Framework (ESMF) to guide implementation of the financial intermediary activities, which are expected to be limited to the livestock and off-grid renewable energy sub-sectors. Therefore, livestock production, small-scale animal husbandry, slaughterhouses, and credit lines to solar home system providers (SHS) are likely to be financed. The ESMF has been prepared in compliance with OP 4.01 (Environmental Assessment) and includes relevant stakeholder consultations. The ESMF has been disclosed on the World Bank external website on January 24, 2019, and in-country on January 25, 2019.

83. **Each potential financial intermediary will be required to undertake an Environmental and Social Screening process which allows SCALED-UP activities to be classified according to their potential impacts and appropriate mitigation/rehabilitation measures required, according to the Somalia Environmental Law and OP 4.01.** Subproject screening will identify and exclude any transactions which merit the application of any other OP relevant to E&S safeguards and will also limit financing to subprojects classified as Environmental Category B or C.

84. **The PIU will ensure that implementation of this ESMF becomes a standard investment review procedure within potential financial intermediaries.** Elements of the ESMF will form part of the Participation Agreement signed between the MSME Financing Facility and every PFI. It is expected that most of the beneficiary MSMEs will not have the adequate capacity in managing even minor environmental or social impacts. Therefore, an E&S management consultant will be recruited by the PIU to implement project safeguard compliance activities, MSME application screening, due diligence, capacity building and technical support, and safeguards monitoring and reporting. The Consultant will ensure that beneficiary MSMEs with subprojects classified as environmental category 'B' have an environmental and social management system (ESMS) that focuses on key risks and mitigation measures.

85. **Climate and disaster risk screening was conducted for this project.** With high exposure to multiple climatic risks, notably drought and flooding, the overall risk exposure rating is considered High. These risks are amplified by the local country context, which tend to aggravate local risk to climate hazards, but are mitigated by the present performance of the financial and ICT sectors, which are already helping strengthen the resilience of local communities. By implementing targeted activities that strengthen these sectors further and boost access to financial and digital services, this project will thus help moderate the risks associated with climatic hazards. Risk exposure has also been factored into the project design and will be mitigated through the adoption of relevant contingency planning for service delivery.

(ii) Social Safeguards

86. **Gender gap analysis.** As noted above, an analysis of gender gaps in Somalia, in relation to financial and digital access, suggests that women face discrimination and considerable socioeconomic barriers to accessing jobs and livelihood opportunities (see annex 5). Nevertheless, Somali women are largely responsible for growth in microenterprise activity and yet are not supported to grow and expand their businesses. Yet few existing financial and Government service delivery arrangements, Government policy frameworks, or business strategies take existing gender gaps into consideration.

87. **Planned project activities to address identified gender gap.** The program will encourage a gender-sensitive approach to the development of strategies for delivery of targeted services and formulation of sector policies and strategies to help address the gender gaps identified. The creation of a new foundational digital ID and progressive movement toward universal coverage will help bridge the ID gender gap by actively boosting female enrollment and facilitate women's access to financial services and economic opportunities more broadly. The project will support the CBS to convene a gender-themed workshop, targeting financial service providers, with the view of enhancing their advisory services, product range, and outreach strategies for increasing their female client base. PFIs will also be required to submit their outreach strategy, for targeting women, as part of the eligibility criteria for participation in the MSME Financing Facility. Finally, the project will ensure that all feedback and grievance mechanisms in place are accessible to women.

88. **GBV risks.** GBV risks under the project are anticipated to be low. The project supports women's economic empowerment and increased access to financial services, which can contribute to improved voice and agency, improved ability to navigate gendered power dynamics and to help the project against forms of GBV. At the same time, increasing women's financial autonomy can also disrupt social and/or domestic power dynamics and contribute to increases in violence, particularly in the home. Given these risks and given the challenging country context of instability and existing high rates of GBV, the project will identify and integrate into the POM key measures to monitor and address GBV risks during project implementation. This includes training and sensitization of PIU staff, as well as of targeted communities, of potential GBV risks and available options for reporting and response. This should also include identification of GBV service providers in the project area of influence and articulation of key steps for appropriate response by PIU staff should allegations arise. This should further include integration of GBV-sensitive channels for reporting of GBV incidence in the GRM and key measures to manage GBV cases reported in the GRM. Additional measures to manage GBV risks may be identified and integrated into relevant project documentation, including the POM.

89. **Citizen engagement.** Project activities will include citizen engagement surveys and information, education, and communication campaigns related to all project activities, specifically the digital ID program/enrollment; ownership of transaction accounts covering mobile money, banks, and remittances; and e-registration services for SMEs under the OSS and the MSME Financing Facility. This will involve annual citizen engagement surveys covering project activities, including access to financial and Government services supported by the project, with a view to raising public awareness, usage, and increasing satisfaction. Coverage of the citizen engagement will include persons with disabilities.

(iii) Grievance Redress Mechanisms

90. **Communities and individuals who believe that they are adversely affected by a World Bank (WB) supported project may submit complaints to existing project-level grievance redress mechanisms or the WB's Grievance Redress Service (GRS).** The GRS ensures that complaints received are promptly reviewed in order to address Project-related concerns. Project affected communities and individuals may submit their complaint to the WB's independent Inspection Panel which determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate Grievance Redress Service (GRS), please visit

http://www.worldbank.org/en/projects-operations/products-and-services/grievance-redress-service. For information on how to submit complaints to the World Bank Inspection Panel, please visit www.inspectionpanel.org.

V. KEY RISKS

91. **Overall risk (High).** Somalia remains a high-risk context for institution building and development financing, but the mitigation and the prospects of benefits outweigh the risks thereby providing a basis for engagement**.** The risks include political contestation among key political and economic actors (resulting in conflict) and fiscal pressure on the budget from a wide array of needs across the country and recurring external shocks. The novelty of the MSME Financing Facility, and the introduction of the digital ID system poses high project implementation risks, exacerbated by cybersecurity risks occasioned by use of digital technologies and low capacity of key stakeholder institutions. The project is managing this risk through multiple layers of monitoring and implementation support that has enabled the task team to implement and expand predecessor financial and ICT sector projects over the last two years and will be applied for the project as well. Important lessons will be incorporated in the MSME Subproject Manual for the project and MSME Financing Facility. See annex 6 for a detailed discussion on risks and mitigation pertaining to the MSME Financing Facility and digital ID subcomponents. Additional risks over the next four years include the upcoming elections at the state level, potentially slowing down the reform processes and introducing fragility in the existing political compacts. A slowing reform trajectory can have a significant impact on the IMF's SMP, minimizing the likelihood of achieving full normalization of IFI relations within the project duration.

92. **Political and Governance (High).** Risk of political instability remains high and could slow or derail project implementation over the course of the project, especially the support to the digital ID activities. Political economy risk will be heightened over the course of the project as consequential and high-level decisions will occupy the FGS' agenda**.** The constitutional review process, the African Union Mission in Somalia (AMISOM) transition and security sector reform, federal elections in 2020, and state-level elections each year toward and beyond 2020, as well as increased regulatory activity at the federal level will have an impact on the emerging formal institutional framework and the informal networks currently providing space for reform. Federally, defining the project activities and implementation plans may prove challenging given the current political tensions between the FGS and FMS. An example of such challenges includes division of licensing revenues and other fees accrued from telecommunications among the FMS which will be a task for the NCA. Political and governance risks are being managed through a range of activities supported by the World Bank and other development partners. This includes additional financing for the Recurrent Cost and Reform Financing Project (P167224) (approved in September 2018), which is investing in intergovernmental institutional frameworks aimed at providing a conducive environment for constructive intergovernmental relations. To manage this risk, the project is proposing leveraging policy dialogue and client engagement through activities provided in other World Bank-financed operations that continue to engage with the FGS within structures promoting an inclusive policy dialogue and consultation among key actors. Additional activities planned that reduce this level of risk are the project's own support to capacity-building activities to help stabilize core government functions, strengthening governance and accountability frameworks for supported entities.

93. **Macroeconomic (High).** The macroeconomic risk remains high due to limited, yet increasing, ability of the FGS to react to external shocks on the nascent formal economy. The state remains

constrained to increase legitimacy, capacity, and authority across Somalia. Despite important and widespread reforms, the FGS' fiscal position remains weak due to the limited ability to generate domestic revenues, security sector expenditures dominating the budget, and only limited fiscal transfers between the FGS and FMS. Consequently, the authorities are at risk of structural over-reliance on grant financing. Somalia's growth prospects are also dependent on external remittances, and on export revenues from only a few commodities (mainly livestock), which make them vulnerable, for example, to disease or trade bans. Principally, the mitigation of macro-fiscal risk is the ongoing work—jointly with other development partners, including the IMF—to support increased domestic resource mobilization. The proposed European Union budget support operation will further provide fiscal space to mitigate against shocks and provide a more predictable fiscal basis over the coming years. Additional mitigation that helps reduce this level of risk is the project's own support to formalization of businesses, the MSME Financing Facility to fund expansion and growth of MSMEs operating in productive sectors, including energy and livestock, combined with TA to support efficient financial intermediation and improved capability of banks. Furthermore, the project proposes to adjust annually the MSME Financing Facility pricing to re-calibrate lending rates to market developments including potential inflationary pressures. See table 4.1 in annex 4 (Financial Intermediary Financing) for a list of the relevant costs and a detailed discussion on components of the costs of funds.

94. **Implementation and Sustainability (High).** The FGS has embarked on important reforms and has been able to attract domestic and diaspora talent to drive key reforms, yet overall level of capacity in the public sector and its core institutions remains inadequate. Strengthening country systems and investing in talent across Somalia will require longer-term investments in human capital of the country. In the short-term, mitigation measures that reduce this level of risk is the project's own additional capacity building efforts targeting MDAs enabling access to basic services for individuals and businesses, as well as augmenting existing capacity with external support provided by other development partners. In addition, an independent monitoring agent will provide an added layer of supervision capacity and help identify or anticipate key gaps on the client side. The majority of the institutions supported by the project are either new (FRC, NCA) or yet to be set up (that is the dedicated entities to manage the digital ID system and the MSME Financing Facility). To mitigate the risks related to delays in setting up these entities or changes in the operating environment, the task team has already engaged in policy dialogue with the client and has received a number of policy commitments that the client intends to tackle in the context of stabilizing the policy and operating environment. This was confirmed in the Letter of Policy Commitments from the Prime Minister, dated January 22, 2019 (see annex 6). This action by the client provides the needed policy stability and predictability during the duration of the project thereby enabling the project's own activities to further build important capacity on the client side.[42]

[42] The Somali authorities have delivered policy commitments in the form of a 'policy letter' from the Prime Minister, dated January 22, 2019, on setting up of the MSME Financing Facility and digital ID system. The authorities will follow up the policy commitments with elaboration of a charter for the MSME Financing Facility and formally establish the organization. With respect to the digital ID system, the authorities will develop a detailed policy statement as the first step toward elaboration of the legislation as one of the conditions of effectiveness. As of September 2018, the task team has drafted a navigation tool in the form of a report titled 'Options and Recommendations for the Design and Implementation Strategy of Somalia's Digital ID System.' The report helps the FGS define the scope and the overall architecture of the digital ID system. As such, the FGS has taken the initial steps in strategic direction-setting decisions on several key topics, which are grouped under four main themes: (a) governance, (b) system architecture, (c) registration, and (d) credentials and authentication.

95. **Fiduciary (High).** The overall combined FM and procurement fiduciary risk rating for the project is High. The FM risk is rated High, while the overall procurement assessment risk is substantial. The country public financial management (PFM) legal framework is weak and fragmented. The PFM accountability systems, supporting processes and intergovernmental fiscal transfers mechanisms between the FGS and FMS in the country are evolving. The project banking and funds flow risks are high, given the need to utilize exceptional arrangements and channels in the absence of a solid domestic banking system. Principally, the mitigation of FM risk is the ongoing work, jointly with other development partners including the IMF, fostering PFM transparency and accountability as well as the support of the monitoring agent as an added layer of supervision capacity. Additional mitigation that reduces this level of risk is the project's own support promoting government digital payments and reduced fiscal leakages by leveraging the digital economy and technology to enhance FM and control. An increase in the digitization of government payments is likely to result in cost-savings to the FGS. Furthermore, control and oversight of the dedicated entities set up with support of the project will include arrangements prescribed by the mandated government PFM institutions—Office of the Accountant General and the Auditor General.

96. **Technical design (Substantial).** Key technical design risk is associated with the technical components of the digital ID system being delivered and deployed by NADRA before a detailed policy and legal framework for the ID system had been designed. At present, the deployment of the technical components is not supported by a clear, comprehensive policy or legislative framework to define the ID system's objectives, overall design, implementation arrangements, and mitigate risks. This creates the risk for potentially unsuitable and unfavorable features to be coded into the system delivered by NADRA. To mitigate this risk, the project proposes the setup of a Tripartite Technical Working Group (TTWG) to bring together the FGS, NADRA, and the World Bank Group to provide ongoing technical advice and review of the ID system's technical components. There is also an added risk that the promised technical components will not materialize if the Government of Pakistan does not continue to finance NADRA's activities. If the agreement with NADRA were to fall through, the FGS would need substantial additional financing to proceed with the implementation of the digital ID system (for example, to procure the necessary software and hardware). In addition to the risk mitigation measures, the phased approach of the project's support for the digital ID will provide it with more time and flexibility to fine-tune the implementation of technical components and consider additional financing options, if needed. It is expected that the setup of a robust enabling environment for digital ID implementation under the first phase of the project could help catalyze further donor financing for the project, if this was needed, and the World Bank could play a convening role to secure additional financing commitments for the digital ID system, should this become necessary, given the clear rationale and great demand for the system by individuals and businesses.

97. **Stakeholders (Substantial).** Some telecommunications companies have recently complained about the early implementation of the 2016 Communications Act, citing lack of consultation. It is also understood that there is a fear that the regulation will affect their profits. In addition, the rollout of the digital ID and expansion of OSS business registration services will create additional stakeholder risks. For instance, issuance of ID and registration of SIM cards may encounter social resistance among communities that have not used registration or identification services provided by a Government authority for more than a generation. Security is also a concern, both for the mass registration activities and later on, where holding a Government issued ID could be considered by extremist groups to indicate collaboration with the authorities. To manage this risk, the project is proposing leveraging policy dialogue and client engagement through activities provided under the project's own activities as well as other World Bank operations that continue to engage in inclusive dialogue and consultation among key actors. Additional

activities planned that reduce this level of risk are the project's own support, depoliticizing of the digital ID initiative, and incorporating continuous citizen engagement activities through outreach, including with the most vulnerable groups of society.

98. **Environmental and Social (Substantial).** The environmental risk rating is Substantial due to the following factors: potential adverse environmental impacts associated with the livestock sector, existing safeguards capacity of the client and beneficiaries, mixed safeguards implementation performance of the predecessor SCORE Project (P152241), and the lack of ability to directly supervise environmental impacts of project activities and compliance with the ESMF. The project social risk rating is Substantial given the fragile context of the country, the low capacity of the borrower, particularly on safeguards, and the potential social risks that might result from weak labor practices (child and forced labor) and occupational health and safety risks. Considering Somalia's politically fragile context, there is the potential risk of microcredits exacerbating marginalization of poor customers from vulnerable groups, vulnerable households, female-headed households, and IDPs who have no ability to access credits. There are additional risks that improved access to finance may negatively alter social and household dynamics, thereby exacerbating risks of GBV, in particular, intimate partner violence. The combined environmental and social risk rating is Substantial. The Substantial risk is expected to be mitigated by a focus on two distinct subsectors (livestock and off-grid renewable energy), a competent E&S management consultant hired as part of the PIU, and close safeguards supervision of subproject screening documentation and resultant ESMS by the World Bank environmental safeguards team member. In addition, the project design requires the participation agreements with PFIs on the MSME Financing Facility to include a clause requiring PFIs to not discriminate against gender, physical ability, language, place of residency, and so on. PFIs will use World Bank E&S screening criteria, which will be included in the agreements between the MSME Financing Facility and PFIs. PFIs will be required to appoint a designated staff member who is accountable for implementing the PFI E&S requirements (although responsibilities may be assigned to a qualified, external consultant). Furthermore, because women in Somalia are disproportionally disadvantaged when it comes to financial services, the project will have a focus on increasing opportunities for women to access finance. This in turn is expected to result in increased availability of financial services, greater income opportunity, improved financial literacy, and inclusive growth. The project will further identify and integrate key measures to manage GBV risks, including strengthening GBV reporting mechanisms and options for ethical, safe, and survivor-centered response.

VI. RESULTS FRAMEWORK AND MONITORING

Results Framework

COUNTRY: Somalia

Somalia Capacity Advancement, Livelihoods and Entrepreneurship, through Digital Uplift Project (SCALED-UP)

Project Development Objectives(s)

The Project Development Objective (PDO) is to support progress towards increased access to basic digital financial and government services targeting entrepreneurship and employment, particularly for women.

Project Development Objective Indicators

Indicator Name	DLI	Baseline	Intermediate Targets			End Target
			1	2	3	
• Number of people who have received their unique ID number, of which (%) are female						
• Number of people who have received their unique ID number (Number)		0.00	0.00	0.00	500,000.00	1,000,000.00
Of which (%) are female (Percentage)		0.00			50.00	50.00
Number of people accessing financial services using their digital ID						
Number of people accessing financial services using their digital ID (Number)		0.00	0.00	0.00	450,000.00	900,000.00
of which % are female (Percentage)		0.00			45.00	45.00
Number of firms that benefit from reformed business registration requirements						
Number of firms that benefit from reformed business registration requirements (Number)		0.00	0.00	500.00	1,000.00	1,500.00

Indicator Name	DLI	Baseline	Intermediate Targets			End Target
			1	2	3	
of which % are female (Percentage)		0.00		30.00	30.00	30.00
Value of MSME loans outstanding from MSME Financing Facility (USD)						
Value of MSME loans from the MSME Financing Facility (USD) (Amount(USD))		0.00	0.00	8,000,000.00	12,000,000.00	16,200,000.00
Of which % are female owned (Percentage)		0.00		30.00	30.00	30.00
Jobs created by firms that access the MSME Financing Facility						
Jobs created by firms that access the MSME Financing Facility (Number)		0.00	0.00	650.00	1,100.00	1,400.00
Of which % are for females (Percentage)		0.00	0.00	30.00	30.00	30.00
Of which % sustainable jobs (Percentage)		0.00	0.00	30.00	30.00	30.00

Intermediate Results Indicators by Components

Indicator Name	DLI	Baseline	Intermediate Targets			End Target
			1	2	3	
Component 1						
Digital ID Authority established & operational (Yes/No)		No	No	No	Yes	Yes
Semi-annual reports produced by NCA on a number of license		No	Yes	Yes	Yes	Yes

Indicator Name	DLI	Baseline	Intermediate Targets			End Target
			1	2	3	
applications processed for communications service providers (Yes/No)						
FRC publishes quarterly statistics in their website on STRs received and reports disseminated to LEAs (Yes/No)		No	Yes	Yes	Yes	Yes
Semi-annual reports produced by CBS on number of financial institution examinations and cases of supervisory actions using regulatory technology solution. (Yes/No)		No	No	Yes	Yes	Yes
Inter-agency coordination body established for coordination between CBS, FRC, and NCA, under an MOU (Yes/No)		No	Yes	Yes	Yes	Yes
Financial sustainability plans prepared and submitted to MoF by each of the project supported institutions (Yes/No)		No	No	Yes	Yes	Yes
Component 2						
Total number of MSME loans outstanding from the MSME Financing Facility (Number)		0.00	0.00	1,700.00	2,100.00	3,130.00
Of which (%) are Micro loans (Percentage)		0.00	0.00	90.00	90.00	90.00
Target quotas for lending to women introduced by the PFIs of the MSME Financing Facility (Yes/No)		No	No	Yes	Yes	Yes
Percentage of MSME beneficiaries that are satisfied with PFI lending		0.00	0.00	0.00	50.00	85.00

Indicator Name	DLI	Baseline	Intermediate Targets			End Target
			1	2	3	
processes (Percentage)						
% of female owned MSMEs that are satisfied with services provided by PFIs. (Percentage)		0.00	0.00	0.00	70.00	90.00
Additional private capital mobilized by PFIs (USD) (Amount(USD))		0.00	0.00	4,000,000.00	6,000,000.00	8,000,000.00
Percent of FGS payments that are executed via interoperable inter-bank payment mechanism rather than cash. (Percentage)		0.00	0.00	25.00	75.00	100.00
Percent of Somali citizens satisfied with quality of service on digital ID enrollment (Percentage)		0.00	0.00	0.00	0.00	85.00
Percentage of Non-Performing Loans among PFIs (Percentage)		25.00	20.00	15.00	10.00	10.00
Percentage of grievances for the MSME Financing Facility addressed by the Project (Percentage)		0.00	0.00	100.00	100.00	100.00

Monitoring & Evaluation Plan: PDO Indicators

Indicator Name	Definition/Description	Frequency	Datasource	Methodology for Data Collection	Responsibility for Data Collection
• Number of people who have received their unique ID number	• Number of people who have received their unique ID number or ID card	Semi-annually	Compilation of enrollment statistics, disaggregate	Compilation of enrollment statistics, disaggregated by gender, provided from digital ID enrollment	PIU

			d by gender, provided from digital ID enrollment reports	reports	
Of which (%) are female					
Number of people accessing financial services using their digital ID	Total number of people accessing financial services, including transaction accounts, using their digital ID.	Semi-annually	Compilation of statistics on the number of transaction accounts opened with and/or linked with the digital ID, provided by financial service providers (banks, MTBs, mobile money, etc.) Surveys about the use of IDs for financial services Compilation of data about	Compilation of statistics on the number of transaction accounts opened with and/or linked with the digital ID, provided by financial service providers (banks, MTBs, mobile money, etc.) Surveys about the use of IDs for financial services Compilation of data about the cumulative number of successful identity verification request and/or authentications performed against the digital ID registry by financial service providers	CBS/Financial Service providers

			the cumulative number of successful identity verification request and/or authenticatio ns performed against the digital ID registry by financial service providers		
of which % are female					
Number of firms that benefit from reformed business registration requirements	Total number of businesses registered with the e-registration services at MOCI	Semi-annually	Compilation of business registry data provided from MOCI business registration system	Compilation of business registry data provided from MOCI business registration system	MOCI
of which % are female					
Value of MSME loans from the MSME Financing Facility (USD)	Value of MSME loans (cumulative) from the MSME Financing Facility. Includes re-flows from	Quarterly	Compilation of data from MSME Financing	Compilation of data from MSME Financing Facility beneficiaries	PIU/MSME Financing Facility/PFIs

	microloans window.		Facility beneficiaries		
Of which % are female owned					
Jobs created by firms that access the MSME Financing Facility	Cumulative number of jobs created, assuming 6 jobs per SME. Definition for sustainable jobs included in the PAD.	Semi-annually	Compilation of data from MSME Financing Facility beneficiaries, and surveys of MSMEs.		PIU/MSME Financing Facility/PFIs
Of which % are for females					
Of which % sustainable jobs	Sustainable jobs are referred to as paid direct full-time equivalent (FTE) lasting a minimum of six months created by SMEs who have accessed the credit line (microloans are assumed to support livelihoods of final beneficiaries and not generate new jobs). Jobs lasting less than one month (or less than 20 days excluding weekends) are not counted in order to emphasize those jobs that provide more stability through length. Jobs should				

	be converted to full-time equivalents (FTE). One FTE equals 260 days (excluding weekends) or 12 months. Thus, a job that lasts 4 months should be counted as 1/3 FTE and a job that lasts for 130 days (excluding weekends) should be counted as 1/2 FTE. Number of hours worked per day or per week is not restricted as work hours may vary greatly. Furthermore, Jobs must be formalized with a written employment contract. Lastly, relevance is not placed on remuneration scale for jobs created as there is no regulated minimum wage in Somalia. (For the definition of sustainable jobs, SCALED-UP has chosen to employ a tested model utilized by USAID for its ongoing GEEL project in Somalia).				

Monitoring & Evaluation Plan: Intermediate Results Indicators					
Indicator Name	**Definition/Description**	**Frequency**	**Datasource**	**Methodology for Data Collection**	**Responsibility for Data Collection**
Digital ID Authority established & operational	Legal framework governing the implementation of the digital ID body/system is passed by Parliament, assented to by the President, and effective.	Semi-annually	Project Implementation reports		PIU
Semi-annual reports produced by NCA on a number of license applications processed for communications service providers	Semi-annual reports produced by NCA on number of license applications processed for communications service operator (including ISPs, MNOs, broadcasting service providers).	Semi-annually	Project implementation reports		PIU/NCA
FRC publishes quarterly statistics in their website on STRs received and reports disseminated to LEAs	FRC publishes quarterly statistics in their website on Suspicious transaction reports (STRs) received and reports disseminated to law enforcement agencies (LEAs).	Quaterly	Project implementation reports		PIU/FRC
Semi-annual reports produced by CBS on number of financial institution examinations and cases of supervisory actions using regulatory technology solution.	Semi-annual reports produced by CBS on number of financial institution examinations and cases of supervisory actions using regulatory technology solution.	Semi-annually	Project implementation reports		PIU/CBS

Inter-agency coordination body established for coordination between CBS, FRC, and NCA, under an MOU	Inter-agency coordination body established for coordination between CBS, FRC, and NCA, under an MOU covering policy formation and harmonization of policies.	Annually	Project implementation reports		PIU
Financial sustainability plans prepared and submitted to MoF by each of the project supported institutions	Financial sustainability plans prepared by each of the project supported institutions (CBS, FRC, MPTT/NCA, MoIFAR/new ID Authority) and submitted to MoF.The sustainability plan will assist the concerned agency and MoF with comprehensive fiscal planning for the long-term management of the assets associated with the project, including foreseen reinvestment when improvements are past their useful life or in need of routine replacement and/or maintenance.	Annually	Compilation of date from the project-supported institutions.	Compilation of date from the project-supported institutions.	PIU
Total number of MSME loans outstanding from the MSME Financing Facility	Total number of SME and Micro loans that are financed by MSME Financing Facility via the PFIs (cumulative).	Quarterly			MSME Financing Facility/PFIs
Of which (%) are Micro loans	Percent of loans extended to Micro Enterprises				

Target quotas for lending to women introduced by the PFIs of the MSME Financing Facility	PFIs of the MSME Financing Facility will introduce target quotas for women to increase women's access to finance.	Annually	PIU/MSME Financing Facility		PIU/MSME Financing Facility
Percentage of MSME beneficiaries that are satisfied with PFI lending processes	These indicators capture MSME satisfaction with quality of on-lending processes and services provided by PFIs.	Annually			PIU
% of female owned MSMEs that are satisfied with services provided by PFIs.					
Additional private capital mobilized by PFIs (USD)	This indicator captures how the MSME Financing Facility incentivizes PFIs to voluntarily strengthen their capital position, as the terms of agreement for PFIs to access funds includes a clause that borrowing from the MSME Financing Facility cannot exceed 20% of current capital.	Annually	Survey of PFIs	Survey of PFIs	PIU/MSME Financing Facility/PFIs
Percent of FGS payments that are executed via interoperable inter-bank payment mechanism rather than cash.	This indicator captures the change in the use of cash as settlement instrument towards interoperable inter-bank payment mechanism.	Semi-annually		Reports with baseline and subsequent change in the use of cash as settlement instrument.	PIU/CBS/MOF/FIs
Percent of Somali citizens satisfied with quality of service on digital ID enrollment	This indicator will be captured through a survey which measures satisfaction on planning and enrollment	Annually	Citizen engagement surveys of beneficiaries.	Citizen engagement surveys of beneficiaries.	PIU

	process of digital ID				
Percentage of Non-Performing Loans among PFIs	The asset quality of PFIs verified through the sum of impaired assets and those past due items that are overdue 90 days or more	Semi-annually	CBS, PFIs, and MSME Financing Facility.	Compilation of NPL data by CBS, PFIs, and MSME Financing Facility	CBS and PIU
Percentage of grievances for the MSME Financing Facility addressed by the Project	Percentage of grievances received through GRM for the MSME Financing Facility addressed by the Project	Annually	PIU/MSME Financing Facility	PIU/MSME Financing Facility	PIU/MSME Financing Facility

ANNEX 1: IMPLEMENTATION SUPPORT PLAN AND FIDUCIARY ARRANGEMENTS

COUNTRY: Somalia
Somalia Capacity Advancement, Livelihoods and Entrepreneurship, through Digital Uplift Project (SCALED-UP)

1. **This implementation support plan describes how the World Bank will support the risk mitigation measures and provide the technical advice necessary to help the FGS achieve the PDO.** The plan also identified the minimum requirements to meet the World Bank fiduciary obligations. This has been developed based on the project's nature and risk profile. Formal implementation support visits and field visits will be carried out at least semiannually, complemented by ongoing dialogue through audio conferences and email, and focus on the areas detailed in this annex.

2. **There will be strong coordination between the World Bank and the PIU, the party responsible for day-to-day administrative project management.** The World Bank task team will bring a comprehensive set of instruments and expertise to advice on project activities. It will work closely with the PIU to ensure project success.

3. **In addition to implementation support visits and ongoing engagements, the World Bank task team will carefully monitor progress of project implementation and achievement of results through formal and informal reporting channels.** Formal reporting channels include Implementation Status and Results Reports and results monitoring reports supplied by the PIU. Informal channels include interactions with direct beneficiaries of the project, reports from local media, and country economic analysis.

4. The project team will take a flexible approach to ensure that it meets clients' needs as circumstances evolve.

Implementation Support Plan

Table 1.1. Implementation Support Plan - Year 1

Focus	Skills Needed	Resource Estimate	Partner Role
Project/task management	TTLs/Senior Financial Sector and Digital Development Specialists (Nairobi and Washington, DC)	20 weeks	PIU: Project Coordinator
Procurement supervision	Senior Procurement Specialist (Nairobi)	2 weeks	PIU: Procurement Officer
FM supervision	Senior Financial Management Specialist (Nairobi)	2 weeks	PIU: Financial Management Officer
Technical support	Technical Specialists (Nairobi/Washington, DC)	10 weeks	Project beneficiaries

Note: TTL = Task Team Leader.

Table 1.2. Implementation Support Plan - Years 2 to 4

Focus	Skills Needed	Resource Estimate	Partner Role
Project/task management	TTLs/Senior Financial Sector and Digital Development Specialists (Nairobi and Washington, DC)	35 weeks	PIU: Project Coordinator

Focus	Skills Needed	Resource Estimate	Partner Role
Procurement supervision	Senior Procurement Specialist (Nairobi)	10 weeks	PIU: Procurement Officer
FM supervision	Senior Financial Management Specialist (Nairobi)	10 weeks	PIU: Financial Management Officer
Technical support	Technical Specialists (Nairobi/Washington, DC)	20 weeks	Project beneficiaries

Detailed FM Arrangements

5. **Project FM system.** The EAFS Unit established within the Office of the Accountant General in the FGS will be charged with overall FM responsibility for all the Somalia Multi-Partner Fund (SMPF)/IDA-funded projects at the FGS and FMS and their performance has been satisfactory. With overall guidance from the Accountant General, the EAFS Unit, in consultation with the respective PIU, will continue to provide day-to-day FM of the project. The effectiveness of the EAFS Unit alongside other key functional units will be continuously monitored while key areas of capacity strengthening will be identified and supported through the project. The existing organizational and functional structure of the EAFS Unit is expected to be maintained and further strengthened to provide effective FM support to the project. All project FM transactions will be recognized, captured, recorded, analyzed, summarized, and reported through the FGS FMIS. The EAFS Unit, with support of the Accountant General, will ensure that

- All important business and financial processes are adhered to;
- Adequate internal controls and procedures are in place and adequately enforced;
- Unaudited IFRs are prepared on a timely basis;
- Project financial statements are prepared on a timely basis and in accordance with IPSAS cash-basis; and
- External audit is completed on time and audit findings and recommendations/issues raised in the Management Letter are implemented expeditiously.

6. **Budgeting arrangements.** The EAFS Unit, working closely with the PIU at the MoF, will prepare the project annual work plan, budget, and cash flow forecast for each component. Not later than two months to the end of the preceding financial year (October 31), these will be submitted to World Bank Group project TTL for necessary review and approvals. The work plans, cash flow projections, and budget include the project activities, amounts according to the FGS financial year analyzed by month and quarter delineated by funding source (SMPF and IDA PACG). The World Bank Group-approved budget and projected annual disbursements at the FGS and FMSs will be 'on-budget' and will be incorporated into the annual Appropriation Bills (Acts). The analyzed budget will be posted into the respective FMIS according to the approved Standard Chart of Accounts (SCoA). The SMPF and IDA share of project financing will be posted by appropriate SCoA funding source to facilitate generation of project periodic reports by funding source (SMPF and IDA). The project's budget utilization reports shall be prepared from the FGS FMIS as a subset of the FGS Treasury Single Account fiscal reports. As necessary, the project will take necessary steps to ensure the anticipated recoveries and disbursements under the revolving fund subprojects are appropriated through the Government budget using the defined SCoA.

7. **Flow of funds and banking arrangements.** The project proceeds from the SMPF and IDA will be channeled through two Designated Accounts (DAs) managed directly by the FGS:

- **DA-AA.** This will be used to manage the funds for Component 1 (Institutional Strengthening); Component 2 (that is, Subcomponent 2.2 on digital ID services and enablement of financial access; Subcomponent 2.3 on government and retail payment services, and Subcomponent 2.4 on e-registration services for businesses under the OSS); and Component 3 (Project Management and Coordination).

- **DA-BB.** This will be used to manage the funds earmarked for Component 2 (that is, Subcomponent 2.1 on financial intermediary financing for MSMEs). The proceeds from IDA will be channeled through DA-BB. Funds will be made available to qualifying PFIs from this DA-BB. The repayment of loans by the PFIs will be deposited in the Reflows Account to be opened at the CBS. As part of regular reporting, the Government will provide an activity statement of the Reflows Account to be submitted to the World Bank together with the project IFRs, 45 days after the end of each quarter.

8. Financing by funding source (SMPF and IDA) will be tracked and reported through the FMIS. All the expenditures incurred through the DAs as well as those submitted to the World Bank Group through client connection for direct payments will be justified, supported, and eligible as defined in the Project Appraisal Document and the Grant Agreements. Expenditures will be recognized at the point disbursements are effectuated from DA-BB to specific subprojects' beneficiaries in line with the prescribed eligibility criteria. All project withdrawal applications to the World Bank Group will be made in U.S. dollars and will be submitted online through the client connection portal. Replenishment and reimbursement Withdrawal Applications will be accompanied by Statements of Expenditures (SOEs) in accordance with the procedures established in the Disbursement Letter and the World Bank Group's Disbursement Guidelines.

9. Detailed disbursement arrangements will be documented in the Disbursement Letters. The EAFS Unit, in consultation with the respective Offices of Accountant General, Director General, and alternate signatories, will institute adequate controls in the management of the DAs. The signatories to the DAs (Treasury check/payment instructions/electronic funds transfer) and Withdrawal Applications will include at least two bank accounts signatories' categories (either from each panel must sign) in each of the following panels at the FGS and the fund managers for the MSME Financing Facility.

Signatories

FGS: DA-AA

- Panel A: Director General of the MoF or equivalent (with Director of Administration as alternate)

- Panel B: Accountant General (with Deputy Accountant General as alternate)

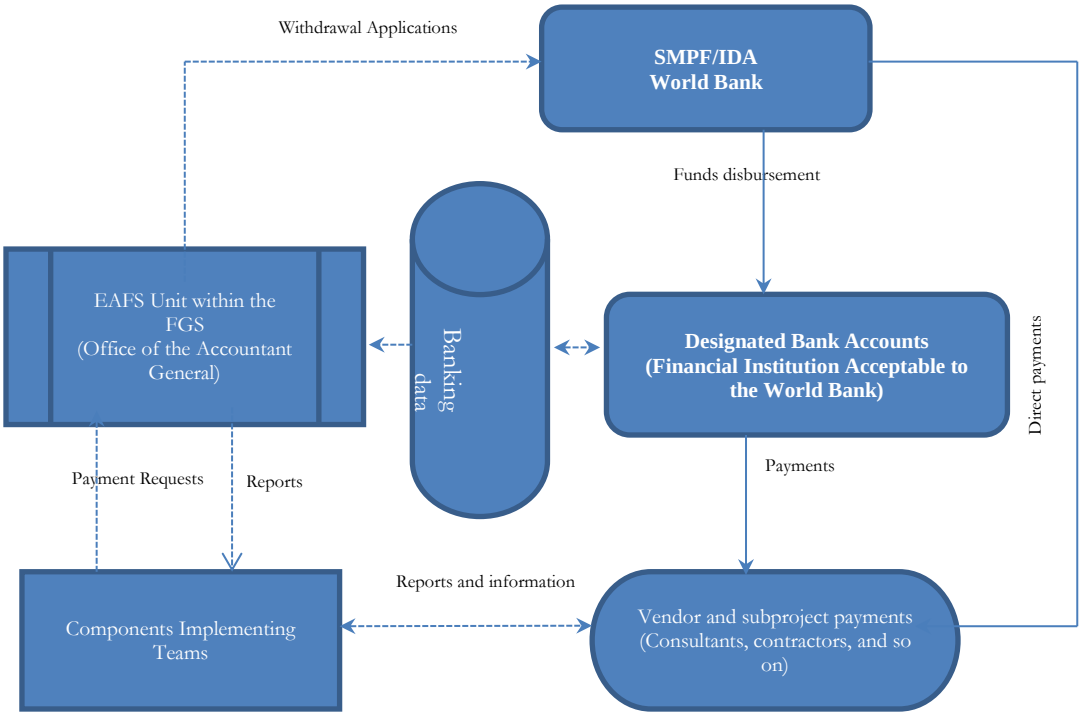
MSME Financing Facility: DA-BB

- Panel A: Director General of the MoF or equivalent (with Director Administration alternate)
- Panel B: Accountant General (with Deputy Accountant General as alternate)

10. The EAFS Unit will ensure that

- The two DAs are maintained in U.S. dollars for the project components in a financial institution acceptable to the World Bank Group. The ceiling of the DA will be based on calculated cash forecasts to ensure adequate working capital cash resources are maintained in the DAs. Funds drawdown will continue to be disbursed based on SOEs. Options in migration to report-based disbursements shall be explored;
- The project component funds are transferred into the DA against an approved withdrawal application prepared by the EAFS. Subsequent withdrawals will be based on the SOE and after the change to report-based disbursement, based on the actual amount expended with a forecast of expenditure and cash flow needs; and
- Detailed disbursement arrangements are documented in the Disbursement Letter. Typical funds flow arrangements are highlighted in figure 1.1.

Figure 1.1. Funds Flow Arrangements



11. With respect to the flow of funds for Subcomponent 2.1 (financial intermediary financing for MSMEs), a subsidiary financing agreement will be signed between the MSME Financing Facility and the

MoF, a project management agreement between the World Bank and the MSME Financing Facility, and a participation agreement will be signed between the MSME Financing Facility and PFIs. The participation agreements will have outlined subprojects' eligibility criteria, repayments/recovery procedures, and schedules. A revolving fund or Reflows Account for the MSME Financing Facility will be held at the CBS and will be managed in line with the Government procedures and overseen by an independent and autonomous board of directors mandated to manage the MSME Financing Facility. The CBS will make disbursements from the DA based on agreed documentation prepared by the MSME Financing Facility. With respect to the loans between the PFIs and the MSME Financing Facility, a loan agreement will be prepared and signed among the two parties. The agreement will outline the terms of the loan that will be extended to the borrower and the responsibilities of the two parties. On that basis, the MSME Financing Facility will provide individual sub-loans (in the case of 'large' and 'small' loans) or programmatic funding (in the case of 'micro' loans), against which the PFI will extend the loan(s) to the SME, microentrepreneur, group, or individual as the case maybe. PFIs will make regular loan repayments to the MSME Financing Facility according to the PFI loan portfolio amortization schedule. The loan repayment by the PFI to the MSME Financing Facility will be deposited into a special revolving fund or Reflows Account at the CBS. The funds collected on the Reflows Account will be available for on-lending by the MSME Financing Facility and applied to support other core operational business related to the extension of MSME banking in Somalia. It is expected that the board of directors of the MSME Financing Facility in consultation with the CBS will make use of the PFI reserve currency holding at the CBS to effect timely loan repayment by the PFI. This will be clearly spelled out in the participating agreement and supported by regular instructions being promptly delivered to the CBS by the PFIs by the 15th and 30th of each month. Upon full repayment of a sub-loan, the final beneficiary(ies) have the option to apply through the PFI to the MSME Financing Facility for a new loan. Detailed financial management procedures for the revolving fund, sub-projects eligibility criteria, and oversight arrangements will be detailed in the POM (including the MSME Subproject Manual as an annex or schedule).

12. Both case-by-case large or small loans and block microloans would be disbursed directly into the DA-BB and directly to subproject beneficiaries bank accounts at PFIs (from the reservice currency holding account at CBS). For purposes of replenishing the DA-BB and documentation of expenditures, withdrawal applications will be supported by a copy of the participation agreement with the PFI and a statement of disbursement of funds to the beneficiaries under (a) 'large loans' window, and (b) 'micro and small loans' window. As part of the monitoring arrangements, disbursements under the 'large' and 'small' loans will provide summaries and supporting evidence on the date of the sub-loan agreements with each selected beneficiary, duly certified by the PFI and acceptable to the MSME Financing Facility. In the case of 'micro' loans, the PFI monitoring arrangements will certify that the subsequent use of funds will be for eligible final beneficiaries or eligible loans and the balances outstanding through the project implementation period would be reported by the PFI to the MSME Financing Facility and be subject to Government internal and external audit requirements. Any balances remaining outstanding and unspent on the DA-BB at the end of the project period would be refundable to the World Bank by the MoF.

13. **Accounting and internal control arrangements.** The project finances will be accounted for on cash basis. These will be supported with appropriate records and documentation to track commitments and to safeguard assets. The project budgets and expenditure will be classified to facilitate the preparation of relevant reports and financial statements, including information on total project expenditures, total expenditure on each project component/activity, and analysis of that total expenditure into various categories of goods, training, consultants, and other procurement and

disbursement categories. The generic project FM arrangements will be spelled out in the Comprehensive Operations and Accounting Procedures Manuals, while specific detailed FM arrangements for the project will be outlined in the POM. In addition, the SCoA will be updated to accommodate the IDA funding source and consolidation of the project components as shall be detailed in the POM as part of implementation. The accounting records will be maintained in U.S. dollars. The project activities (SMPF and IDA) will be mapped to the FMIS using the SCoA to facilitate recording and reporting of all the project financial information, including information on total project expenditures, total expenditure on each project component/activity, and analysis of that total expenditure into various categories and funding sources. All the project FM records will be maintained in hard copies at the EAFS Unit as well as in electronic format (archived) in the FMIS.

14. **The EAFS Unit will continue to monitor and report on the utilization of project funds, including the fiduciary standards complied with and the reliability of the FM system.** The EAFS, in consultation with the PIU, will maintain project fixed assets register within the FMIS fixed assets module. The register will be regularly updated and physical verification/count of assets carried out periodically (at least once every six months). The fixed assets registers reflect details of suppliers, description, and location of goods, original cost, disposal of assets, asset reference (identification) number, serial or registration number, date of purchase and price (cost) and/or valuation, additions to the asset, condition of asset, useful life and residual value, and disposal. Contracts' registers will also be maintained with respect to all contracts with consultants, contractors, and suppliers. The EAFS Units will prepare Contract Status Reports as part of the periodic IFRs. Control procedures over fixed assets and contracts management will be the responsibility of the EAFS in consultation with the PIU. An internal audit function, once established and operational in the MoF, will be mainstreamed into the project activities. The internal auditors are expected to undertake project risk-based systems audits. The audit reports together with the findings and systems strengthening recommendations will be shared with the project PIU, CBS, the managers of the MSME Financing Facility, and the World Bank Group FM team.

15. **Financial reporting arrangements.** The project's financial and physical progress reports will be submitted to the World Bank in periodicity agreed between the Government and the World Bank. All project financial reports will be generated directly from single integrated window through the Government's FMIS and as a subset of the various authorities Treasury Single Account fiscal summary reports. Periodic[43] IFRs will be prepared by the EAFS in consultation with the PIU and will cover all project funds (SMPF and IDA). Reporting on specific MSME Financing Facility operations will be submitted as part of the project physical performance reporting. For purposes of monitoring, the reports shall be submitted to the PIU, CBS, MSME Financing Facility, and the World Bank Group. The IFRs and physical progress reports will cover all funds received under the project (the SMPF and IDA) as well as counterpart or Government funds received under the project, if any. The formats and contents of the financial progress reports are designed into the FMIS. The systems will be reconfigured to reflect desegregated reporting by funding source (SMPF and IDA). The EAFS will be responsible for providing overall consolidated financial reports for the two DAs as defined in the relevant covenants. The EAFS Unit will also prepare Project Annual Financial Statements (PAFSs) for the entire project. PAFSs will be prepared in accordance with cash-basis IPSAS. The PAFSs will include adequate notes and disclosures consistent with the cash basis of financial reporting under IPSAS.

[43] Quarterly or any other periodicity as shall be agreed between the World Bank and the authorities.

16. **External auditing.** The Office of the Auditor General at the FGS has the constitutional responsibility to carry out independent audit of project components implemented by the FGS. The project will support the engagement of an external audit technical assistance (TA) to work with the staff of the Office of the Auditor General to undertake the project audit alongside other SMPF/SPF/IDA-funded projects implemented through country systems. Given the high country risks, specific attention will be focused on the International Standards on Auditing (ISA 800)—Auditor's Report on Special Purpose Audit Engagements, as necessary. The detailed external audit approach and procedures will be outlined in the terms of reference (TOR) for the external audit including twinning knowledge transfer arrangements. The TOR will be extended to cover the auditing and expression of an audit opinion on the Reflows Account for the MSME Financing Facility. The audited PAFSs and Management Letters, together with any additional information required, will be submitted to the World Bank within six months after the end of the financial year. The audits shall be in conformity with the World Bank's audit requirements and in accordance with internationally recognized auditing standards. The respective Office of the Auditor General will express an opinion on the financial statements in compliance with International Standards of Supreme Audit Institutions and prepare a Management Letter giving observations and comments, providing recommendations for improvements in accounting records, systems, controls, and compliance with financial covenants in the Grant Agreement(s).

17. **Fraud and corruption.** Possibility of circumventing the internal control system with colluding practices such as bribes, abuse of administrative positions, misprocurement, and so on is a critical issue and may include (a) late submission of supporting documents; (b) poor filing and records; (c) lack of system integration; (d) lack of budget discipline; (e) unauthorized commitment to suppliers, bypassing budget and expenses vetting procedures; (f) unsecured safekeeping and transportation of funds; (g) uncertainty over the banking arrangements supporting the project; (h) potential exposure to money laundering; and (i) insecurity and political instability. These are mitigated as follows: (a) specific aspects on corruption auditing would be included in the external audit and monitoring arrangements TOR; (b) FM procedures (as part of FM manuals) are approved and in operation for the project; (c) strong FM arrangements are in place, including qualified project accountants in the EAFS Unit; (d) periodic IFRs will include budget execution and monitoring; (e) measures to improve social accountability and transparency are built into the project design by ensuring that project reports are available to the public; (f) annual PFM forums will be held; and (g) portfolio-wide periodic preliminary audits will feed into the annual audits. The external audit will pay special attention to the risks of material misstatement of the financial statements due to fraud, in line with ISA 240: "The auditor's responsibilities relating to fraud in an audit of financial statements."

Detailed Procurement Arrangements

18. **Procurement will be carried out in accordance with the requirements in the World Bank Procurement Regulations for IPF Borrowers**: Goods, Works, Non-Consulting Services and Consulting Services, dated July 1, 2016 (revised November 2017 and August 2018); Guidelines on Preventing and Combating Fraud and Corruption in Projects Financed by IBRD Loans and IDA Credits and Grants (revised as of July 1, 2016); and provisions stipulated in the Financing Agreement. Given Somalia's FCV country status, procurement will be processed under the special procurement arrangements referred to in paragraph 12 of the World Bank Policy on Investment Project Financing dated November 10, 2017.

19. **PPSD and PP.** The World Bank's New Procurement Framework will apply to this project. In this regard, the task team together with the borrower have prepared the PPSD, based on which the PP for the first 18 months has been prepared. The PP will be updated at least once in 12 months or as required to reflect the actual project implementation needs, but each update shall require World Bank Group approval. All PPs will be publicly disclosed in accordance with the World Bank Group's disclosure policy.

20. **PPSD Summary:**

(a) **Works.** There are no works contracts expected in this project.

(b) **Goods and non-consulting services.** The contracts under goods include ICT equipment, vehicles, office furniture, and office supplies. The contracts under non-consulting services include activities such as hiring of conference facilities, transport, or IT services. The type and budget for such activities will be defined and agreed between the borrower and the World Bank during the project implementation period.

(c) **Consulting services.** This includes recruitment of individual consultants and consultant's firms as the need arises for technical support and assistance.

21. **Operating context**:

(a) **Governance aspects.** The FGS is faced with the challenge of rebuilding state institutions in the midst of recurrent and protracted conflict. Since the collapse of the Siad Barre Government in 1991, Somalia has experienced cycles of conflict that fragmented the country, destroyed legitimate institutions, and created widespread vulnerability. Past transitional governments were undermined by warlords' mismanagement and external interference, giving rise to militia-based opposition and the Al Shabaab insurgency. The fragile governance context is further exacerbated by competition over key economic resources by groups with an active interest in sustaining conflict primarily to gain access to the economic and financial resources.

New Federal Member States (FMS) have emerged in the past five years, but the federation process is complex. State formation is both a significant development opportunity and a contentious process. Urban areas in Southern Somalia formerly under Al Shabaab control are now the capitals of newly formed FMS and are responsible for subnational administration. Powerful local actors emerged as leaders of the five FMS. While state formation has set a course for Somalia's governance and service delivery, it has also opened new uncertainties over representation and sharing of power and resources. Risk of political instability remains high and could slow or derail project implementation, especially the support to the digital ID activities. Political economy risk will be heightened over the course of the project as consequential and high-level decisions will occupy the FGS' agenda**.** The constitutional review process, the AMISOM transition and security sector reform, federal elections in 2020, and state-level elections each year towards and beyond 2020, as well as increased regulatory activity at the federal level will have an impact on the emerging formal institutional framework and the informal networks currently providing space for reform.

(b) **Economic aspects.** Somalia is classified by the United Nations as one of the least developed countries. Despite experiencing two decades of civil war, the country has maintained an informal economy, based mainly on livestock, remittance/money transfers from abroad, and telecommunications. Somalia's GDP per capita makes it one of the poorest country in the world. In addition, remittances from the diaspora remain an important source of household income and a buffer against shocks.

(c) **Sustainability aspects.** Because of the protracted war and persistent drought conditions in many parts of Somalia, the country faces uncertainty regarding the sustainability of the projects intended to support the growth of the economy and thus support sustainable programming. It is hoped that with the steps that the country has been able to take since 2011, and with the new Government in place, the country will be able to develop more long-term sustainable development.

(d) **Technological aspects.** Besides the devastating impact of Somalia's civil war, an aspirational technology sector has been growing in the country for years. Somalia has one of the most active mobile money markets in the world, with millions of people subscribed to mobile money services. Young people, with increased access to the Internet and mobile phones, have shown interest in launching technology-driven businesses and crowdfunding entities—even innovating around famine relief efforts.

(e) **Market research and analysis:**

(i) **Consultancy services.** The procurement activities under consultancy services for this project will be hiring of consultants. These will include both individual consultants and consultant firms as needed from local and international markets, as appropriate. There are qualified consulting firms and individuals available in Somalia, many of whom have participated in previous similar assignments funded by the World Bank.

(ii) **Procurement of non-consulting services.** Contracts under non-consulting services include activities such as hiring of conference facilities, transport, or IT services. Given the nature and size of the non-consulting services to be procured, most of the potential bidders are available locally. Such items will be procured through National Open Competitive market approach and Request for Quotations.

(iii) **Office equipment, IT equipment, vehicles, and supplies.** Somalia has local traders for ICT equipment, scientific equipment, motor vehicles, and furniture and other office supplies. These items are available either locally or internationally. Such items will be procured using either Open National/International or Request for Quotation methods, as appropriate.

22. **STEP.** The World Bank's STEP system will be used to prepare, clear, and update PPs and conduct all procurement transactions for the project. The PIUs under the ongoing SCORE Project have been trained and are using STEP and the World Bank STEP champion and the Procurement Specialist will continue working closely with PIUs for smooth use of STEP, including the training of new staff.

23. **Procurement templates.** The World Bank's Standard Procurement Documents (SPDs) shall be used for procurement of goods, works, and consulting and non-consulting services under International Competitive Procurement. As there are no National Bidding documents, the SPDs may be used under National Procurement Procedures. Similarly, selection of consultant firms shall use the World Bank's SPDs, in line with procedures described in the Procurement Regulations.

24. **Publication (Advertising).** The borrower is required to prepare and submit to the World Bank a General Procurement Notice. The World Bank will arrange for its publication in United Nations Development Business online (UNDB online) and on the World Bank's external website. Specific Procurement Notices for all procurement under International Competitive Bidding and Requests for Expressions of Interest for all consultancies shall be published in at least one newspaper of national circulation in the borrower's country, in the official gazette, or on a widely used website or electronic portal with free national and international access and in UNDB online.

25. **National Public Procurement Law.** The Public Procurement, Concessions, and Disposal Act, 2015 (PPA) for The Federal Republic of Somalia (FGS) is the relevant public procurement legal framework. The new Act foresees a decentralized system of procurement. The Act further provides for an independent oversight body that will foster the regulatory and the policy framework of public procurement in the country. The PPA has been reviewed by the World Bank and found to be satisfactory and consistent with the National Procurement Procedure requirements prescribed in paragraph 5.4 of the Procurement Regulations to a large extent. However, institutions are not yet in place in accordance with the Act. Similarly, regulations and other procurement guidance documents, including Standard Bidding Documents, are yet to be prepared. The private sector and civil society have limited capacity or functionality. Currently, the process of operationalizing the PPA is under way, through a consultancy assignment. Until such time that the PPA is operationalized and the documents are reviewed and found satisfactory by the World Bank, the project shall use the World Bank's SPDs. It is anticipated that, when the PPA is operationalized, for the national procedures to be used in accordance with the PPA, the following shall be observed: (a) the request for bids/request for proposals document shall require that bidders/proposers submitting bids/proposals present a signed acceptance at the time of bidding, to be incorporated in any resulting contracts, confirming application of, and compliance with, the World Bank's Anti-Corruption Guidelines, including without limitation the World Bank's right to sanction and the World Bank's inspection and audit rights; and (b) the World Bank will have the rights to review the borrower's procurement documentation and activities.

26. **Training and workshops.** The project will finance training and workshops. These costs should not be on the PP. If required, the costs will be based on an annual training plan and budget which shall be submitted to the World Bank for its prior review and approval. The annual training plan will identify, among other things, (a) the training envisaged, (b) the justification for the training, (c) the personnel to be trained, (d) the duration for such training, and (e) the estimated cost of the training. At the time of the actual training, the request shall be submitted to the World Bank for review and approval. Upon completion of the training, the trainees shall be required to prepare and submit a report on the training received.

27. **Procurement implementation arrangements.** The project will be implemented by the FGS using a single PIU anchored in the MoF in Mogadishu with project focal persons appointed and embedded within MDAs covering SCALED-UP priority areas (MoF, MoCI, MoIFAR, MPTT, CBS, FRC, NCA, and new ID

Authority). The PIU will be responsible for day-to-day project management and will coordinate closely with MDAs covering the project's priority areas. It is also proposed that the PIU coordinates activities across the FGS including the FMS, making it unnecessary to establish subsidiary implementation arrangements with the FMS. The project proposes to set up a single PSC comprising the key MDAs to coordinate and oversee the implementation of activities, with attention to sequencing and timing issues, as well as ensuring effective stakeholder consultations and engagements.

28. A PSC, headed by the MoF with representatives from the MoCI, MoIFAR, MPTT, CBS, FRC, NCA and new ID Authority, will provide policy guidance and monitor the progress through its Secretariat, represented by the Director General in the MoF. FGS can make changes in the membership composition of the PSC or its terms of reference in consultation with IDA.

29. The PIU in the MoF, created more than two years ago, will implement the project. An effective management structure is in place and the PIU had demonstrated its capacity to deliver results efficiently. It has established a strong track record of performance, has familiarity with the World Bank's fiduciary guidelines, as well as functional MIS and M&E systems. However, given the high number of subprojects to be managed under the MSME Financing Facility, the PIU will be further staffed and specific actions implemented to strengthen MSME Financing Facility management capacities of the PIU, that is (a) initially setting up of a financial sector sub-committee of the PSC to support operationalize the MSME Financing Facility, (b) hiring of an E&S safeguards adviser to support operationalization of the MSME Financing Facility, and (c) hiring of professional staff to manage the MSME Financing Facility. Currently, PIU staff have been selected on a transparent and competitive basis and any new PIU staff will be selected on a competitive basis in accordance with TOR agreed with IDA. The FGS will maintain lean but adequate staffing and competency in the PIU and consult with IDA before making any appointments or replacements.

30. **Procurement assessment.** A procurement capacity assessment of the PIUs in the MoF to implement the project procurement was conducted in December 2018. The objectives of the assessment were (a) to evaluate the capability of the PIUs to undertake procurement and the adequacy of the systems that are in place to administer procurement; (b) to assess the ability of the PIUs to effectively carry out the procurement processes; (c) to develop an action plan to be implemented as part of the project to address the deficiencies detected by the assessment, aimed at minimizing the risks identified; and (d) to propose procurement supervision plans for the World Bank considering the relative strengths and weaknesses and risks revealed by the assessment.

31. The assessment revealed that the implementing agency has procurement experience but lacks adequate capacity and experience in the World Bank Procurement procedures (World Bank New Procurement Framework) and hence will require support to undertake the necessary procurements satisfactorily according to World Bank procedures.

32. The PIU had been established in the MoF under the ongoing SCORE Project (P152241) in Mogadishu. The same PIU will be maintained and strengthened for the implementation of the SCALED-UP and will be responsible for the implementation of the procurement activities. The Procurement Specialist has adequate academic qualification/experience and his performance has been satisfactory. However, the Procurement Specialist has not undergone substantive procurement training on the World Bank New Procurement Framework since the ongoing SCORE Project is being implemented under the old World

Bank Procurement Guidelines. Major procurement challenges of the PIU include (a) inadequate experience in undertaking procurement in accordance with the requirements in the Procurement Regulations, (b) inadequate experience in contract management, and (c) a weak record keeping system.

33. **Risk assessment.** In view of the challenges outlined above, the risk for procurement was considered High. The risk is reduced to a residual rating of Substantial in view of the mitigation measures proposed in table 1.1.

Table 1.1. Procurement Risks and Mitigation Measures

Sl. No.	Risk Description	Mitigation Measures	Timeframe	Responsibility
1.	Inadequate knowledge and experience of World Bank Procurement Regulations for IPF Borrowers: Goods, Works, Non-Consulting Services and Consulting Services dated July 1, 2016 (revised November 2017 and August 2018)	• Conduct training for client on the Procurement Regulations • Prior review of all contracts regardless of the value	During project implementation	MoF (FGS)/World Bank
2.	Inadequate knowledge and skills in contract management by the implementing agencies	• Conduct training tailored toward addressing weakness in contract management for PIU staff and technical departments	During project Implementation	MoF (FGS)
3.	Inadequate skills by the end users in developing specifications and TOR	• Need for TAs/consultants in the respective technical areas to extend hands-on expanded implementation support (HEIS)	During project Implementation	MoF (FGS)
4.	Need for systematic filing system to have complete records of the procurement processes	• Establishment of a satisfactory filing system	During project Implementation	MoF (FGS)
5.	Due to security challenges and weak public sector functionality, the private sector participation and efficiency would be limited, and this affects the supply market functionality.	• All bidding opportunities will be advertised on the available websites and posted in widely circulated national gazette.	During project implementation	MoF (FGS)
6.	Fraud and corruption risks (including collusion and outside interference in contracting process)	• Disclosure of Procurement Plan, disclosure of contract awards, and creating of awareness on effects of fraud and corruption	During project implementation	MoF (FGS)
7.	Use of unqualified and	• Use of qualified and	During project	MoF (FGS)/World

Sl. No.	Risk Description	Mitigation Measures	Timeframe	Responsibility
	inexperienced evaluation members and varying of the evaluation criteria through elimination or skewed subcriteria	experienced sector-relevant evaluation panel members who have the time to undertake the evaluation within the shortest possible time and ensure confidentiality. • Use of clearly defined evaluation criteria established in the bidding documents without skewing. • Training of the evaluation members on carrying out bid evaluations. • Recruitment of short-term procurement consultants to support the Government particularly in drafting the bidding documents and during the bid evaluation.	implementation	Bank

34. **Procurement oversight and monitoring arrangements.** The World Bank exercises its procurement oversight through a risk-based approach comprising prior and post reviews, as appropriate. The World Bank sets mandatory thresholds for prior review based on the procurement risk rating of the project. Based on the risk rating of the project, the World Bank and borrower will agree on procurement above the applicable thresholds, as provided in table 1.2, which shall be subjected to prior or post review. The requirement for a prior or post review shall be specified in the PP. During project implementation, the World Bank will monitor and reassess the risk and risk mitigation measures and, if determined by the World Bank to be necessary and appropriate, the World Bank may require the borrower to revise the prior and/or post review requirements in the PP. The World Bank will carry out post reviews of procurement activities undertaken by the borrower to determine whether they comply with the requirements of the Financing Agreement.

Table 1.2. Thresholds for Procurement Approaches and Methods (US$, millions)

Goods, Works, and Non-Consulting Services				
Category	**Prior Review**	**Open International**	**Open National**	**Request for Quotation (RfQ)**
Goods, IT, and non-consulting services	≥0.1	≥0.5	<0.5	≤0.1
Consulting Services				
Category	**Prior Review**	**Short List of National Consultants**		
		Consulting Services	**Engineering and Construction Supervision**	
Consultants (Firms)	≥0.1	≤0.1	≤0.2	

Individual Consultants	≥0.05	n.a.	n.a.

35. **Selection method.** For goods and non-consulting services, Request for Bids and Request for Quotations will be used as appropriate. Where there is justification, Direct Selection maybe used. For consulting services, the preferred method would be Quality- and Cost-Based Selection. However, other methods including Selection Based on the Consultants' Qualifications (CQS) and Direct Selection would be used, as stipulated in the PP.

36. **Contract strategy.** Goods and services will be packaged in economical packages to attract bidders who are qualified and can offer good prices and complete contracts within the stipulated period, resulting in value for money.

ANNEX 2: DESCRIPTION OF COMPONENTS

1. **The project proposes to finance activities to expand financial and digital access over a four-year period for US$31 million.** The project will consist of three components.

Component 1: **Strengthening Institutions (US$7 million)**

1.1 Support to CBS (US$1.5 million)

1.2 Support to FRC (US$1.5 million)

1.3 Support to MPTT and NCA (US$2 million)

1.4 Support to new ID Authority (US$2 million)

Component 2: **Enabling Financial and Digital Services (US$20 million)**

2.1. Financial intermediary financing for MSMEs (US$15 million)

2.2. Digital ID services (US$3 million)

2.3 Government and retail payment services (US$1 million)

2.4 e-Registration Services for SMEs (US$1 million)

Component 3: Project Management and Coordination (US$4 million)

Component 1: Strengthening Institutions (US$7 million equivalent)

2. **The project proposes to support FGS to enhance the environment for digital transactions and services.** As such, the project would provide TA to strengthen institutions that are key to ensuring healthy provision of targeted financial and government services that is, CBS, FRC, MTPP/ NCA, and the new ID Authority to be established with project support. With clear policies and specific strategies, plans, and road maps, these policy makers and regulators will help increase contestability of markets, and support reconfiguration of the financial and digital communications sector to improve service delivery while mitigating AML/CFT risks. These institutions represent the key public sector agencies enabling robust delivery of targeted financial and digital services in Somalia.

Subcomponent 1.1: Support to CBS (US$1.5 million equivalent)

3. **The subcomponent will provide technical and financial support to the CBS to strengthen critical systems for financial institutions regulations and supervision; and promoting efficient financial intermediation**. This includes improved and timely regulatory reporting by financial institutions to ensure they are accurately reporting their financial condition and performance, combined with a strengthened MIS used by the CBS for collecting, managing, and analyzing data from financial institutions. To achieve these objectives, this subcomponent will directly support the following activities:

- Enhance project implementation through the hiring of one focal person (financial sector consultant) to support implementation of project activities located at the CBS focusing mainly on financial institutions regulations, secured transactions infrastructure, credit referencing, and digital financial services (fintech).

- Strengthen policy and strategy for digital financial services and expanding financial access. The project will encourage a gender-sensitive approach to the development of strategies for delivery of targeted services and formulation of sector policies and strategies to help address the gender gaps identified. The project will support the CBS to convene a series of gender-themed workshops, targeting financial service providers, with the view of enhancing their advisory services, product range, and outreach strategies for increasing their female client-base.

- Draft regulations under a modern FIL, National Payments Law, and Insurance Law, as well as data protection utilizing the IFC PPD platform to hold constructive dialogue among relevant stakeholders in the drafting and passage of these legislations.

- Prepare detailed functional specifications for CBS ICT systems that meet the identified data and analytical requirements and identify, select, and procure a suitable software platform to meet the CBS ICT system needs (RegTech).

- Develop costed workplans for selected elements under the 2018-2020 Financial sector Roadmap in strengthening CBS operations and provide implementation support aimed at CBS reorganization. This will be in consultation with the World Bank and IMF.

- Provide capacity building, staff training, coaching, and mentorship to learn about the new RegTech-system, new payment systems, new regulations and analytical techniques, data collection tools, and analysis.

- Investment in technology platforms and draft laws and regulations relating to secured transaction and credit referencing enabling efficient intermediation.

- Provide transportation, accommodation, per diems, coordination, validation workshops, stationery, printing, dissemination, and other similar costs.

Subcomponent 1.2: Support to FRC (US$1.5 million equivalent)

4. **This subcomponent will provide technical and financial support to the FRC to strengthen its operational capability and core systems needed for effective analysis and investigation of suspected cases of money laundering or financing of terrorism (AML/CTF).** This will cover improving systems used for collecting financial information related to transactions suspected of AML/CTF and implementation of an integrated technology solution for analyzing of transaction data. The support is expected to enhance investigation of cases and result in dissemination of evidence-based findings to the appropriate law enforcement agencies or regulatory bodies for prosecution. This will involve the purchase of necessary systems and equipment.

5. **The FRC is shifting focus toward improving effectiveness of implementation of laws and regulations.** Following the conclusion of the NRA, which is being supported under the SCORE Project (P152241), it is expected that the FRC will begin to take increasingly strong enforcement actions, supported by industry outreach, compliance to AML/CFT international standards, and their effective

implementation. To achieve these objectives, this subcomponent will directly support the following activities:

- Strengthening of institutional capability of the FRC to perform rigorous AML/CFT risk investigations within the financial services sector and conduct AML/CTF risk analysis economy wide
- Development of costed capacity-building program and implementation support covering a few key areas such as understanding of AML/CFT risks, improvement of the legal and regulatory framework, AML/CFT supervision, financial analysis, professional skills development and qualifications, and strategic communication and stakeholder engagement
- Hiring of one consultant with experience managing an FIU to support implementation of project activities at the FRC, focusing mainly on the planned 2021 mutual evaluation[44] and FRC's organizational development
- Strengthening of policy and strategy for AML/CTF risk management including drafting of regulations under a strengthened AML/CFT law
- Capacity building and TA for the FRC staff and facilitation of stakeholder consultation and debate on AML/CTF issues including training events/workshops for the FRC staff including certification of staff
- Harmonization of regulatory framework relating to AML/CFT requirements with the CBS and NCA
- Review of FRC ICT systems, including Disaster Recovery/Business Continuity Planning. Development of costed workplans and implementation support for strengthening the FRC operations and implementation of improved business processes and regulatory reporting requirements

Subcomponent 1.3: Support to MPTT and NCA (US$2 million equivalent)

6. **For the MPTT/NCA, the project proposes to support activities that directly contribute to enhancing citizens' access to digital services and maximizing the development impact of ICT,** including improving affordability and service quality, as well as enabling efficient, secure, and reliable digital transactions and innovation.

7. The project proposes to support activities that would include strengthening of collaboration among NCA, CBS, and FRC regarding implementation of the Communications Act on aspects related to the MNO provision of mobile money services, SIM-card registration, and KYC/CDD requirements for AML/CFT

[44] The FATF conducts peer reviews of each member on an ongoing basis to assess levels of implementation of the FATF Recommendations, providing an in-depth description and analysis of each country's system for preventing criminal abuse of the financial system. Somalia is expected to undergo a mutual evaluation following the completion of the National Risk Assessment supported under the SCORE Project (P152241).

regulations. To achieve these objectives, this subcomponent will directly support activities and convenings related to

- Policy development of an ICT sector strategy (covering e-government, cyber security, and digital skills development;
- Development of regulations, guidelines, and data collection and analysis tools needed to fully abide by the Communications Act;
- Procurement of regulatory equipment and building staff capacity around using this equipment;
- Procurement of short-term consultancies for highly specialized technical tasks that are not currently available within the NCA or MPTT (covering spectrum licensing, product pricing, cyber security, and interconnectivity);
- Development of a comprehensive fiscal and business plan focusing on the establishment of minimum operations to ensure effectiveness and sustainability of services delivered by the NCA; and
- Capacity building for NCA core staff on identified priority areas under the financial sustainability plan.

Subcomponent 1.4: Support to new ID Authority (US$2 million equivalent)

8. **The project will support the creation of a robust enabling environment and institutional framework for a digital ID system,** which is expected to provide at least 1 million people with a biometrically supported unique ID number and will serve as a platform for financial access, digital payments, and delivery of Government, humanitarian, and private sector services.

9. The project will help align the FGS efforts to establish a foundational digital ID system with the 'Principles on Identification for Sustainable Development',[45] thereby helping mitigate risks and maximize opportunities for development. The project will support the FGS with the establishment of a comprehensive legal framework, which will set out, among others, to define the basic purposes of the ID system, establish and specify the mandate, governance arrangements, and functions of the ID Authority, and lay out key system features and principles, such as those related to registration processes, credential issuance, system interoperability, and the use of identity verification and authentication mechanisms for financial service providers and beyond. The support provided to enroll at least 1 million people is expected to be linked with financial service users such as mobile money users, transaction account holders, and remittance recipients, thereby creating strong incentives to enroll. The Somali authorities are finalizing the digital ID policy framework outlining the key features (such as the technical and data protection approaches). To mitigate risks associated with the slow pace of adoption of legislation, the FGS authorities have delivered policy commitments through a letter from the Prime Minister, dated January 22, 2019. The

[45] World Bank. 2017. *Principles on Identification for Sustainable Development: Toward the Digital Age.* Washington, DC: World Bank. http://documents.worldbank.org/curated/en/213581486378184357/pdf/112614-REVISED-English-ID4D-IdentificationPrinciples-Folder-web-English-ID4D-IdentificationPrinciples.pdf.

policy letter is the first step in the process of elaboration of detailed policy statement regarding the digital ID system, including data protection, which is expected to be finalized ahead of effectiveness. Project activities related to strengthening institutional capacity and the enabling environment for the digital ID system include the following:

- Support for the development of a comprehensive implementation strategy for the digital ID policy statement including support for the development of a robust, inclusive, and privacy-conscious legal and regulatory framework for the proposed digital ID system

- Completion of in-depth assessment of the technical components of the ID system being implemented by NADRA, support for convening meetings between the FGS and NADRA, and provision of expert support to address identified gaps or weaknesses with a view to mitigate risks, maximize opportunities for development, and foster the adoption of sound features related to system technology, operations, and maintenance[46]

- Setting up and operationalization of a competent and trusted authority to manage and implement the proposed digital ID system. Staff training, coaching, and mentorship to learn about the new digital ID system

- Support for consultation workshops for discussions and developing stakeholder consensus on a variety of issues relating to digital identification. Transportation, accommodation, per diems, coordination, validation workshops, stationery, printing, dissemination, and other similar costs

- Setting up of a small coordination secretariat for the new ID Authority and support the convenings. Hiring of consultants and additional technical expertise to help augment the FGS digital ID project management capacity to undertake planning and coordination functions as well as the development of strategies and provision of local implementation support

10. Detailed sequencing of digital ID-related activities is outlined in table 2.1 at the end of this annex.

Component 2: Enabling Financial and Digital Services (US$20 million equivalent)

Subcomponent 2.1: Financial intermediary financing for MSMEs (US$15 million equivalent)

11. **The project proposes to establish an MSME Financing Facility initially capitalized with US$15 million to fulfil the project objective of increased access to finance for MSMEs supporting entrepreneurship and employment.** The MoF will initially establish the MSME Financing Facility as an apex institution providing funds on a wholesale basis to PFIs, both banks and non-bank financial institutions. It will have an authorized share capital of US$100 million and the MoF will make available the US$15 million as a convertible loan (at 0 percent). Initially, the MoF may convert up to US$2 million of the convertible loan into equity (ordinary shares with voting rights) to form part of the start-up capital of the

[46] The Somali authorities are finalizing the TOR for the setting up of a TTWG to bring together the FGS, NADRA, and the World Bank to provide ongoing technical advice and review of the ID system's technical components, which are to be implemented by NADRA.

MSME Financing Facility to meet the estimated operational and administrative costs for the first three years. Over time, the MSME Financing Facility will introduce a range of financing instruments for on-lending the funds to PFIs, including for onward financing to MSMEs for loans, Islamic finance, performance-based finance, equity, and risk management products to significantly increase MSME financing in Somalia. To crowd-in investment capital from private sector sources, the MSME Financing Facility will use a range of blending tools consisting of core equity (with FGS accepting a high risk for a relatively low return) and subordinated/mezzanine debt (with FGS accepting first losses ahead of private investors). In this way, private investors (such as DFIs when they can invest on their own account further down the line) will be afforded the opportunity to achieve better returns at lower risk than other core equity shareholders such as the FGS, to the extent that they can provide finance to the MSME Financing Facility and indirectly to PFIs and beneficiary MSMEs. The conversion rates of the convertible loan to blending tools will be linked to performance benchmarks for the MSME Financing Facility agreed with FGS, covering aspects such as private sector representation on its governance structures; crowding-in of private capital and DFIs; portfolio assets quality (non-performing loans and recoveries); and outreach while creating opportunity for private capital risk-sharing and blended finance in targeted economic sectors and final beneficiaries such as energy and livestock as well as women and female-owned enterprises. Additionally, the MSME Financing Facility may establish and manage several funds at the same time on behalf of the FGS, other international DFIs including private sector investors keen on promoting MSME access to finance in Somalia.

12. **The MSME Financing Facility will have a commercial orientation and leverage private sector governance principles.** Discussions have been held that propose that IFC could have an implementation support role that goes beyond TA to include investment advisory. In the event this materializes, any potential conflict of interest connected with future downstream IFC investments, this will be managed through disclosures to FGS on the activities of the World Bank and IFC and how the two institutions will manage the conflict (whether it is actual or perceived).[47] All the while, IFC would have a duty to use its best efforts in executing its implementation support role to the MSME Financing Facility; just as the World Bank would have a duty to give its best advice. To help protect the integrity of the MSME Financing Facility throughout the project life cycle, it will operate in accordance with IDA-reviewed appraisal procedures and standards to be set out in an MSME Subproject Manual which will follow the World Bank Directive on Investment Policy Financing and ensure adherence to prudential regulatory ratios, and minimum capital and operational standards. The MSME Subproject Manual will also seek to draw on/reflect IFC's investment standards for the large loans window. Participating banks and non-banking financial institutions will assume the credit risk for on-lending to MSMEs and follow their respective credit and pricing policies for financing according to market conditions. In cases where subsidy is applied on pricing mechanisms by the MSME Financing Facility, this will be explicit and transparent so as not to distort the commercial market. This will be a condition of the IDA Grant Agreement and Project Agreement.

13. **Management of the MSME Financing Facility will be based on best practice private sector principles and entrusted to an independent board of directors.** The MSME Financing Facility, together with its board of directors and management, will be established in accordance with applicable national legislation. The establishment and operationalization of the MSME Financing Facility will be based on the high-level policy commitments signed on January 22, 2019 by the Prime Minister. Aspects related to

[47] In the event of the IFC engagement materializing, the nature and extent of implementation support to the MSME Financing Facility will be detailed in a TA Agreement.

ownership control and other governance issues of the entity will be set out in its charter. The charter will elaborate powers of shareholders and boards of directors to govern the financial and operating policies of the entity to obtain benefits for citizens from its activities. In addition, the approach of seeking to leverage private sector corporate governance principles and the approach to enable the entity to be private sector led as and when investment of private capital is made will be clearly set out in the charter. Some of the aspects of corporate governance to be covered include the appointment or removal of the members of that entity's board of directors, appointment or removal of the entity's Chief Executive Officer, and decision making at meetings of the board of directors or at general meetings of the entity.

14. **To protect its institutional integrity, the MSME Financing Facility will operate in compliance with World Bank reviewed appraisal procedures and standards stipulated in the World Bank Grant Agreement and Project Agreement and embedded in the MSME Subproject Manual.** The entity's appraisal procedures and standards will be elaborated in an MSME Subproject Manual developed with World Bank Group assistance to appraise all projects seeking funding. Risk factors in the MSME Subproject Manual will include AML/CFT risks and environmental assessment such as social, environmental, technological, economic, regulatory, political, geographical risks, and opportunities, with due consideration of the indicators which measure sustainable development issues. The MSME Subproject Manual will be updated from time to time based on experience in the field and in consultation with World Bank Group.

15. **The CBS will hold a special account as a DA for the MSME Financing Facility as well as the Reflows Account for collecting repayments from PFIs.** The CBS is already holding several DAs for IDA and the SMPF-financed projects and is recognized as having good practice in FM. A subsidiary Grant Agreement would be signed between the MoF and the MSME Financing Facility, setting out the obligations of both parties and supplemented by a project agreement as well as the MSME Subproject Manual that would establish the operating policies and procedures of the MSME Financing Facility. The provisional operational and administrative budget estimate for the MSME Financing Facility is US$1.5–US$2.0 million during the first three years of operations. See annex 4 for a complete description of the MSME Financing Facility.

Subcomponent 2.2: Digital ID services (US$3 million equivalent)

16. **The project proposes to support the registration of at least 1 million people to enable greater financial access and lay the groundwork for further scale-up of the system.** As of January 2019, the technical components of the ID system, which are to be delivered and installed by NADRA[48] and financed through a grant from the Government of Pakistan, were not yet operational. As such, project support for registration will begin with the drafting and adoption of a comprehensive legal and regulatory framework for the proposed digital ID system, the establishment and operationalization of a dedicated, independent

[48] The Somali authorities are finalizing the TORs for the setting up of a TTWG to bring together the FGS, NADRA, and World Bank to provide ongoing technical advice and review of the ID system's technical components, which are to be implemented by NADRA. The scope of works for the TTWG will include definition of a sustainable business model covering estimated annual costs of maintenance and upgrade of the system by NADRA; production of credentials and fees for ID authentication services, among other costs and revenues streams; and options for the ID system to avoid vendor dependence or lock-in and avoid dependence on license fees (and explore open source model) or credential expenses.

ID Authority, and the subsequent development of robust and inclusive implementation strategies and training of staff.

17. **The design and implementation of the digital ID system will follow the Principles on Identification for Sustainable Development and ensure accessibility to all, free from discrimination.** The digital ID system proposed to use biometric technology to verify the uniqueness of registrants and issue unique, random identification numbers to successful enrollees. A physical ID credential such as an ID card may also be issued to facilitate authentication and enable individuals to prove who they are and access services in a variety of settings (including low-connectivity environments).

18. **Banks, MTBs, MNOs, and other service providers will be among the first users of the ID system and are expected to play an active role in its implementation.** The new ID system and ID credentials issued will enable more people to access financial services by facilitating compliance with ID verification requirements of KYC regulations. The introduction of a robust ID system will also support more accurate SIM-card registration and compliance with ID verification requirements for mobile money services. The branch and agent network of these private sector partners can be leveraged to boost enrollment in the ID system by providing on-site opportunities for registration and potentially, ID card issuance or pickup services. Banks and MNOs may also act as local enrollment agents and may provide co-financing for registration activities and for the ongoing maintenance of a reliable and accurate population registry given the considerable benefits they are expected to reap from a robust, digital ID system. The World Bank could play a convening role to foster private sector participation and to promote alignment with the FGS' objectives, policies, and regulations on the issuance and use of the IDs.

19. **Building on the technical components to be delivered by NADRA, the project will cover certain additional costs associated with registration for the digital ID system, including for marginalized populations, with a target of 1 million enrollments.** Project-supported costs and activities will include the rollout of a resident engagement and communications campaign; operation costs related to enrollment, training, and transportation; and additional system component and operation costs beyond the first year.[49] Special measures and registration efforts will be put in place to ensure access to the ID system for remote, marginalized, and vulnerable populations including women, children, persons with disabilities, IDPs, and minority clans. These will include an 'ecosystem' approach to enrollment, leveraging banks, MNOs, and other service providers as well as trusted community-level organizations as enrollment agents for the ID system. Performance-based or output-based contract may be used to promote effective registration service provision. In addition, reaching out to the poorest and most marginalized groups will require engagement and support from local NGOs, civil society organizations, and entrepreneurs (for additional strategies to increase the enrollment of women, please see annex 5).

20. **The project proposes to work closely with WFP and other humanitarian agencies to integrate lessons learned from their experience with biometric registration and identity management and to facilitate the future use of the digital ID system for humanitarian service delivery and social protection more broadly.** WFP has registered over 4 million people in Somalia (of which 2 million through biometric registration), often by partnering with local NGOs —a strategy that could be leveraged by the FGS as well. Another important lesson learned from WFP registration and service delivery was the importance of

[49] This will be predicated and informed by the expert assessment of the technical elements of the ID system being implemented by NADRA.

putting appropriate support and grievance mechanisms in place for the users of the system, for example, through establishing assistance hotlines and clear follow-up protocols to investigate and address issues as they arose on the ground. This was also instrumental for building trust and ensuring its effective operation. Going forward, allowing for all beneficiaries across humanitarian assistance programs as well as FGS-provided social protection initiatives to be uniquely identified could help ensure that resources are allocated effectively and improve targeting across programs.

Subcomponent 2.3: Government and retail payment services (US$1 million equivalent)

21. **The project proposes to finance the integration of the mobile money services into the payment switch, allowing for communication and integration between different retail payment service providers using interbank payment mechanisms.** While some 70 percent of Somalis with a mobile phone regularly use mobile money transacting approximately US$2.7 billion per month,[50] the service has drawbacks in terms of interoperability and interconnectivity. Currently, mobile money does not allow for bank-to-bank transfers; transfers are only operable within a single bank or the MNO network. This is partially due to anti-competitive conduct, which necessitates that MNOs partner only with related banks and restrict access to own mobile money platform and interconnectivity of services. Existing World Bank programs have supported the introduction of an Automated Transfer System (ATS), national payment switch (the Switch), and piloting of mobile money bulk payments. The ATS and Switch complement each other, with the ATS facilitating urgent, large-value payments as well as bulk payments, using the automated clearing house capabilities, while the Switch will facilitate interoperability of retail payment services and interchange of data and payment instruments. These developments open the opportunity to interconnect the country to international payment schemes (such as Visa and MasterCard) and international money transfer operators (MTOs) from a single payments platform. It also includes the opportunity to integrate mobile money services onto the Switch, thereby defragmenting the payments landscape and constructing interoperable retail payment services economy-wide covering key use cases such as person-to-person (P2P), bill pay, cash-pull from bank account, and cash-push to bank account.

22. **The project plans to cover additional costs associated with supporting the CBS to spearhead efforts to introduce interoperability of retail payment services and the interconnectivity of Government digital payments.** The project will shore up public and private sector commitment to establish institutional arrangements supporting interoperable retail payment systems and support the development of clear policies and specific strategies, plans and road maps for retail payment systems, and interoperability covering mobile money services. Enabling interoperability fosters competition and deeper financial intermediation by incentivizing tangible value propositions to mobile money solutions and effective mobile money products in Somalia. Together, these developments will allow the CBS, and other MDAs, to facilitate direct G2P and G2B digital payments and vice versa. These systems will also lower transaction costs, improve transaction traceability, and facilitate the reach and exchange of payments for purposes such as social protection programming, tax collection, and intergovernmental fiscal transfers.

23. **The project proposes to cover costs associated with repositioning of the Government and humanitarian actors as central role players in fostering digital finance development in Somalia.** This will be justified by the surge in demand by the Government and humanitarian actors for low-cost interoperable retail payment services. The surge in demand will be leveraged to foster the innovation,

[50] World Bank. 2017. *Mobile Money Ecosystem in Somalia: Household Survey and Market Analysis*. Washington, DC.

competition, and collaboration needed to drive mass migration to interoperable systems while incentivizing the decommissioning of legacy fragmented retail payments services. By discontinuing fragmented legacy arrangements, Somalia could eliminate an element of unacceptable cost in the retail payments ecosystem[51] and encourage multilateral interbank payment mechanisms to meet everyday payment needs of consumers and small business retailers as well as Government and humanitarian actors. Access to shared infrastructure—and related business management processes—enables services providers to maximize opportunities for cost reduction and effectiveness. This is particularly in the areas involving front-end customer engagement issues (for example, customer and small business retailer onboarding, ID enrollment, KYC/CDD identification verification); payment mechanisms and risk management issues (for example, shared multilateral clearing and settlement services, fraud management and control services, harmonized operating rules and interchange fees); and back-end customer support/protection issues (for example, application programming interfaces [APIs]; ICT/cyber security; transaction authentication, authorization, and non-repudiation).

24. **To support these objectives, this subcomponent will directly support the following activities:**

- Undertake a stocktaking exercise of all retail payments by the FGS and humanitarian actors by payment flow (value and number) and type of payment instrument (cash, transfer, mobile money) and apply an ecosystem approach to uncover obstacles and opportunities for lowering costs and improving convenience, reliability, and security for digital payment services. By using rigorous assessments of existing arrangements, the project will help encourage the FGS and humanitarian actors to demand corresponding investments needed to improve retail payment policies and products.

- Hire one consultant with experience constructing interoperable retail payment/mobile money services that are aligned with Committee on Payment and Settlement Systems (CPSS) and the Technical Committee of the International Organization of Securities Commissions (IOSCO) Principles for Financial Market Infrastructure and facilitation of stakeholder consultation and debate on interoperability issues.

- Prepare detailed functional specifications for interoperable services that meet the identified use cases and payment needs for the FGS, humanitarian actors, and final beneficiaries.

- Draft scheme regulations and rules for interoperable retail payment systems.

- Set up a small coordination secretariat under the CBS on interoperability and support the convenings. This will include development of TORs for the multi stakeholder committee and coordination activities, and the recruitment of additional technical expertise to help augment the capacity of the CBS to undertake planning and coordination function for the development of the strategy and provide implementation support.

[51] MNO/MTB charges for money transfers are typically 1.5 percent of transfer amount and reportedly higher for special money transfer arrangements.

Subcomponent 2.4: e-Registration Services for SMEs (US$1 million equivalent)

25. **The project proposes to cover costs associated with supporting the MoCI to facilitate unique identification of legal entities through integrated online 'one-stop shop' business registration services.** Building upon the work on enactment of the Company Law and launch of the online business registration system supported under the SCORE Project (P152241), the project plans to focus on facilitating integrated online services using a single interface combining business registration with tax registrations and business licenses issued by the municipalities. While the primary focus will be to help the SMEs register, the proposed online system will also cater to other forms of businesses, that is, large, domestic, and foreign direct investment enterprises. The online platform will also enable secure data sharing across FMSs depending on the readiness of the states. Procedural reforms, simplified forms and documentation, and consolidated fees will be important building blocks to align with Somalia's Ease of Doing Business priorities for the Starting a Business indicator. The project will support interoperability measures including data exchange protocols and institutional coordination mechanism with digital ID system which NADRA plans to implement. Once it is fully implemented and sustained, the proposed system will build a solid foundation for a virtual OSS in future.

26. **Online features to enhance efficiency and transparency.** The proposed online system will be web based (with options for mobile access for SMEs located outside Mogadishu) and will include a client-facing portal covering online access to all relevant information, procedures, and forms for download by users. To enhance efficiency and transparency, all forms, fees, and supporting documents will be made available upon necessary process reengineering. The system will also allow for enterprises to apply for registration as well as post registration and change requests online. The proposed system will allow online submission of applications and enable users to track their respective transactions online. Following the electronic submission, a single visit by the applicant to the relevant office may be necessary for hard copy submission and manual payment. Going forward, this step could be made fully electronic through Government digital payment services. The new system will also contribute to improving the database quality and make selected data publicly available according to the proposed Company Law and international good practices. In addition to general information on the sectors, activities, and contact information, the database will include (a) gender-disaggregated data and women-owned and managed businesses, (b) geographic location of businesses, and (c) information on economic subsectors.

27. **Extensive citizen engagement will be important.** Gender-sensitive citizen engagement, including stakeholder outreach and communications campaign, will be carried out to enable strong uptake of online registration among the SMEs and all other forms of businesses. Hands-on training on the system targeted for internal Government users and outreach to end users will be a key component to establish embedded capacity and sustain the system in the long term.

28. **Fiscal and operational sustainability will be critical.** To ensure operational sustainability of the OSS and provide access to applicants without Internet connectivity, the project will support the establishment of computer terminals (that is, helpdesks) and handholding support to businesses at the company registration office, allowing the applicants to scan, upload, and submit documentation at the office premises. To ensure fiscal sustainability beyond the project life cycle, the FGS will make necessary budget provision for maintenance and operations of the system through an annual maintenance contract (AMC) with the technology solution vendor covering hosting, software licenses, trouble-shooting, immediate first-line support by phone, and second-line on-site support. The project covers the costs of

the initial two years of the AMC after confirmation of the FGS budget provision. The project will also fund TA and capacity-building activities provided to the MoCI around this agenda.

Component 3: Project Management and Coordination (US$4 million equivalent)

29. **This component will finance support for project implementation.** The project will be implemented by the FGS using a PIU anchored at the MoF in Mogadishu, with project focal persons appointed and embedded within the PIU from key MDAs, including the MoF, MoCI, MoIFAR, MPTT, CBS, FRC, NCA and new ID Authority.

30. **The PIU will be headed by the project coordinator.** The PIU will include procurement, FM, impact evaluation, and safeguards specialists who are familiar with the World Bank's rules and procedures to ensure smooth implementation. The PIU will include a project-level GRM specialist. The PIU will also include project focal persons to act as the focal points in agreed priority areas targeted by the project with responsibilities to (a) exchange information with other MDAs and stakeholders interested in the subject area; (b) report periodically on matters of interest, activities, and progress relevant to their priority area; (c) monitor progress within their priority area; and (d) report to the PIU and other interested stakeholders.

31. **The project proposes to set up a single PSC.** The PSC will coordinate and oversee the implementation of activities, paying due attention to sequencing and timing issues as well as stakeholder consultants and engagements. The FGS shall not later than 30 days after the effective date, establish and thereafter, maintain throughout the project implementation, the PSC with a mandate, resources, TOR, and functions, satisfactory to the Association. Without limitation, the PSC shall be responsible for (a) approval of annual work plans and budgets, and project reports, including Financial Management Reports, and (b) provide overall policy and strategic guidance for the project.

32. The FGS shall, not later than October 31 of each year, prepare and furnish to IDA, a consolidated annual program of activities proposed for implementation under the project during the following fiscal year, together with a proposed budget for the purpose. The FGS shall exchange views with IDA on each such proposed consolidated annual work plan, and shall thereafter adopt, and carry out such program of activities for such following fiscal year as shall have been agreed with IDA, as such plan may be subsequently revised during such following fiscal year with the prior written agreement of IDA (annual work plan and budget).

33. The FGS shall furnish to IDA each Project Report not later than 45 days after the end of each calendar semester, covering the calendar semester.

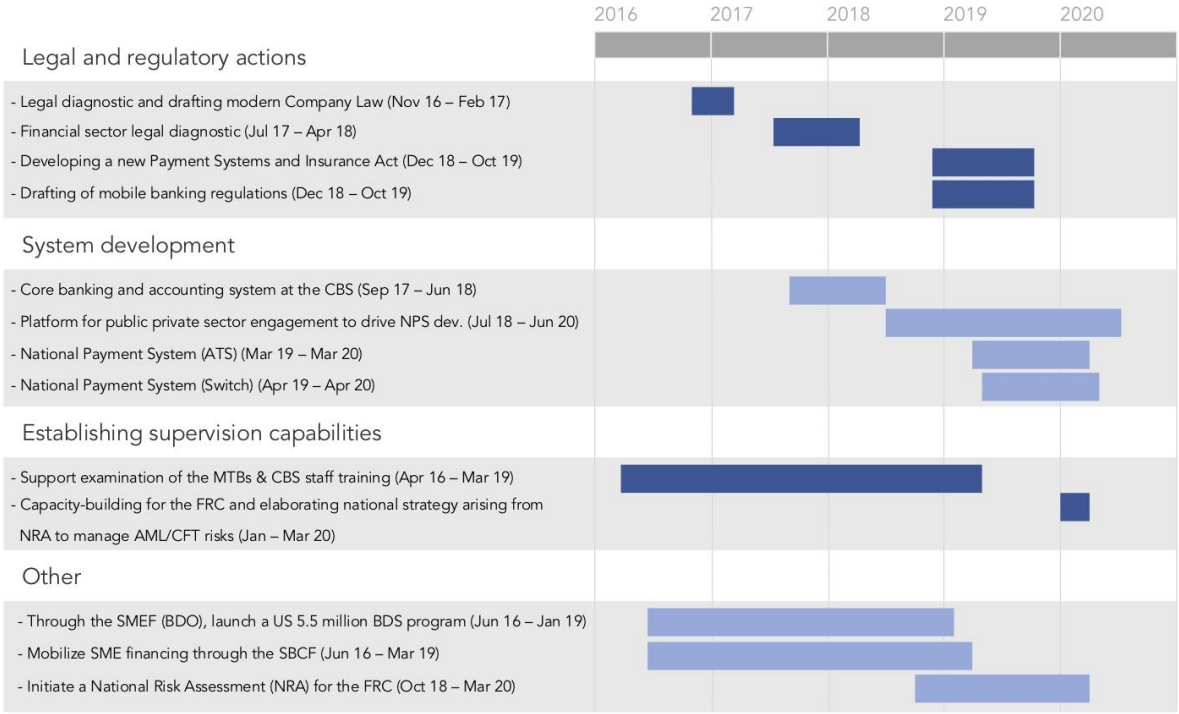
34. **Financing to be provided for the PIU** may, among others, include equipment, consultant compensation, operating costs, organizational and systems development, training, capacity building, and TA. The project proposes that the PIU hires experts/consultants on call (part time) for the targeted priority areas as needed.

Table 2.1. Sequencing of Digital ID Activities

Subcomponents 1.4 and 2.2		Expected/ Ideal		Accounting for Potential Delays				
Activity	**Period (H - half year)**							**Estimated Cost**
	Year 1: H1	**Year 1: H2**	**Year 2: H1**	**Year 2: H2**	**Year 3: H1**	**Year 3: H2**	**Year 4: H1**	**Year 4: H2**	
Legal framework on digital ID *Development of comprehensive legal and regulatory framework, including drafting, consultation, passage by Parliament, assented to by the President.*									US$350,000
ID Authority institutional setup support *Capacity building and advisory on the operationalization of an ID Authority (including governance arrangements, organizational structure, business plan)*									US$400,000
ID Authority technical setup support and capacity building *Advisory and capacity building on technical aspects of the digital ID system, including database management, registration, and credential issuance, and authentication*									US$400,000
ID consultations/logistical support *Logistical, transport and travel support for public consultations, workshops, seminars, trainings, and meetings*									US$350,000
ID user-centricity and inclusion support *Development of Grievance Redress Mechanisms, Social Management Plan, and Digital ID Outreach Strategy to women and other vulnerable groups*									US$250,000
Financial sector ID applications *Integrating the use of digital IDs in the financial sector, including for KYC and payment systems*									US$250,000
Citizen and Resident Engagement and Communications Campaign									US$600,000
ID enrollment support for 1 million residents *Support for registration activities excluding technical components*									US$2,400,000

Figure 2.1. Phased and Iterative Approach of Implementing SCORE and ICT Project Activities

Financial Sector Support Activities



ICT Sector Support Activities

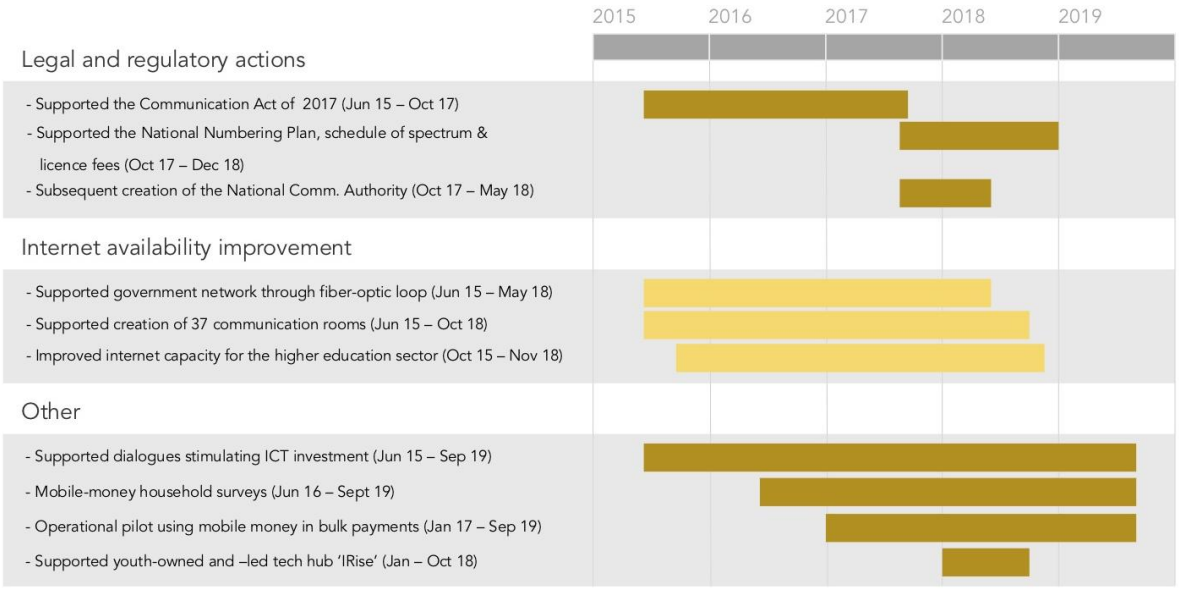
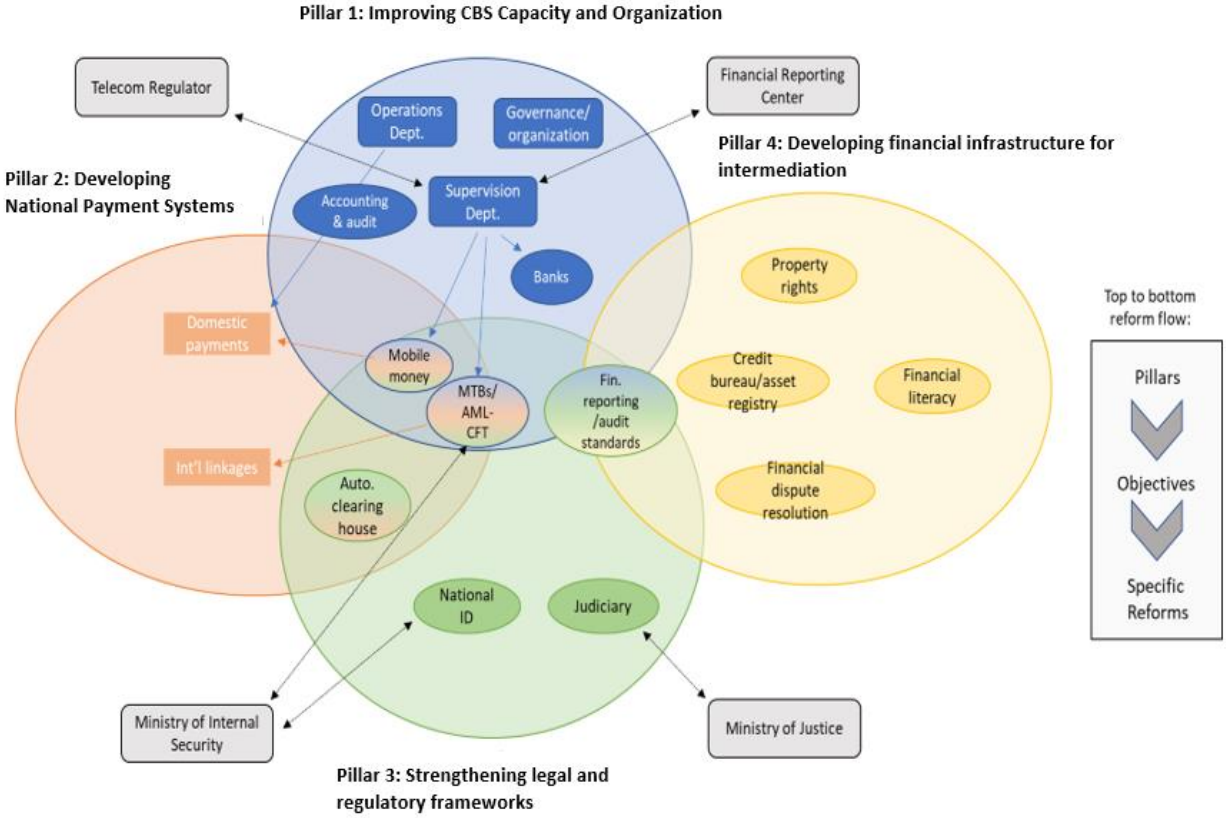


Figure 2.2. Somalia Financial Sector Development Roadmap 2018–2020: A Broad Structure



Source: Central Bank of Somalia. 2019. *Somalia: A Roadmap for Financial Sector Development*.

ANNEX 3: RECENT MONETARY AND FINANCIAL SECTOR DEVELOPMENTS

Macroeconomic Developments

1. **Somalia's economy is recovering but remains vulnerable to recurrent shocks.** The size of the economy is estimated to be US$7.1 billion in 2017 with a per capita GDP of US$511. The economy has been growing at an average rate of 2.5 percent between 2013–2017. However, climate-related shocks, export bans, and sporadic terror attacks threaten economic recovery, making the growth cyclical. Specifically, real GDP growth in 2017 weakened to 2.3 percent (from 4.4 percent in 2016) due to severe drought and sporadic terrorist attacks. Total losses and damages due to drought in 2017 were estimated at US$3.2 billion with agriculture (mainly crops and livestock) accounting for 60 percent. The source of economic growth is private consumption—financed by remittances. Economic activity is rebounding with growth projected to increase to 3.1 percent in 2018, mainly supported by recovering agricultural productivity because of a favorable rainy season, sustained remittances, and donor inflows.

Table 3.1. Selected Economic and Financial Indicators 2015–2017

	2015	2016	2017
National Accounts and Prices			
GDP (US$, millions, nominal)	6,659	6,767	7,052
GDP growth (%, real)	3.9	4.4	2.3
Per capita GDP (US$)	511	504	511
Inflation (%)	−1.2	0.0	5.3
Central Bank summary balances	**US$ (millions)**		
Gross foreign assets	68.6	60.9	89.2
Net foreign assets excluding IMF	21.6	21.6	24.0
FGS total deposits	19.1	12.1	33.6
External sector	**% of GDP**		
Current account balance	−4.7	−6.3	−6.6
Trade balance	−45.1	−46.8	−55.2
Exports of goods and services	15.6	15.1	11.5
Imports of goods and services	60.6	61.8	66.7
Remittances	19.5	19.7	23.5
Grants	21.2	21.1	25.6
Foreign direct investment	4.5	4.9	5.2
External debt	66.3	64.7	65.0

Source: IMF.

Monetary Developments

2. **Inflationary pressure is easing from the effects of drought due to increased productivity in the first half of 2018.** Overall, inflation has declined to 3.1 percent in July 2018 compared to 5.2 percent in

July 2017.[52] The scope for monetary policy is limited as the economy is highly dollarized. The Somali shilling is used for only small face-to-face transactions with an estimated 95 percent of the national currency in circulation being fake. Progress has been achieved on this front under the IMF SMP. However, the Somali economy remains highly dollarized, and the CBS does not control the money supply.[53] The authorities have set currency reform and financial sector development as one of their highest priorities. The CBS is at advanced stages in replacing the existing Somali shillings in circulation with a new currency while strengthening its institutional capacity and developing independent monetary policy instruments and reserve management capabilities. By regaining control of the national currency, the CBS will have a key prerequisite for reengaging in monetary policy, according to its statutory obligations under the Central Bank Law. Nonetheless, expectations are that dollarization will persist for some time irrespective of the outcome of the currency reform program.

Fiscal Sector

3. **Implementation of fiscal policy has improved but challenges remain.** Domestic revenue collection increased, achieving 103.2 percent of the 2017 budget target. The FGS continued efforts to broaden the tax base, enhance compliance, and improve collection capacity. As a result, domestic revenue increased to US$143 million in 2017 from US$113 million in 2016. However, this remains too low—about 2 percent of GDP—to deliver meaningful services to the citizens. Expenditure priorities remain unchanged; almost all expenditure is recurrent and sector spending is skewed toward security and administrative services both accounting for about 90 percent of the total spending hence crowding out social and economic sectors.

External Sector

4. **The external sector remains a source of vulnerability.** The economy is highly dependent on imports with the share of exports to GDP being only 11.5 percent in 2017. Imports account for more than two-thirds of GDP, creating a large trade deficit, mainly financed by remittances and donor flows. Trade deficit rose by 18 percent, closing at 55.2 percent of GDP in 2017, as exports fell, and imports rose due to drought. The drought devastated livestock exports with exports of live animals—which normally account for more than 70 percent of export earnings—declining by 75 percent to 1.3 million in 2017 from 5.3 million animals in 2015. The current account deficit rose to 6.6 percent of GDP in 2017 from 6.3 percent of GDP in 2016.

Financial Sector Developments

5. **Somalia's financial sector is limited in size, simple in structure, and extremely isolated from the global financial system.** The financial system comprises central banks (including in Somaliland), banks, MFIs, MTBs, and MNOs providing mobile money services. In 2015, the mobile phone penetration rate stood at of 59 percent and in 2017, some 70 percent of Somalis with a mobile phone regularly used mobile money services, transacting for approximately US$2.7 billion per month—yet, mobile money remains

[52] Crops prices declined in most regions because of increased supply compared to the same period in 2017. The exchange rate remained stable at SOS 23,099 to the U.S. dollar in 2017 due to steady remittances and donor inflows.
[53] Published estimates suggest that U.S. dollars make up around 90 percent of the currency circulating in Somalia.

unregulated. As of January 2019, there were five banks and 11 MTBs licensed by CBS and operating in Somalia. Most banks met the minimum capital requirement of US$7 million.[54] See boxes 3.1–3.4 for a snapshot of key financial sector players in Somalia.

6. **Between 1991 and 2011, Somalia had no central monetary authority and hence no regulated financial sector.** Following the collapse of the Government in 1991 and corresponding breakdown of the domestic banking system, an extensive network of MTBs was developed to facilitate international remittance flows, domestic financial transactions, and trade. In 2011, the FGS passed the Central Bank of Somalia Law, which reinstated the CBS. In 2012, the FGS passed the FIL, which created a national framework for financial institution regulation and supervision by the CBS. However, the FIL only covered banks and MTBs.

7. **An emerging trend in the sector is the consolidation of financial service operators into a few large companies, which deters competition from prospective entrants.** Somali money transfer and telecommunications businesses have always been intertwined, but the rapid growth of mobile money has forced key players in the strategic sectors of banking and money transfer services to not only protect their market niche but to occupy new ones as well. They do so largely through mergers and alliances.[55] There is also a growing trend of partnerships to facilitate international transfers/remittances directly to customers, resulting in large conglomerates, and the crowding out of smaller MTBs. As a result, there are overlapping financial sector interests covering banking, microfinance, and mobile money. The leading financial service providers include the Amal Group, Dahabshiil Group,[56] and Hormuud Group.

8. **Access to global banking systems remains uncertain.** Over the past three years, banks in international jurisdictions such as Australia, the United Kingdom, and the United States have closed accounts of some Somali remittance companies due to risks related to money laundering, as well as legal and regulatory weaknesses.[57] In this setting, the impetus for institutional reform is driven by external pressures on Somali policy makers and financial institutions to improve governance and institutional effectiveness.

9. **Under the World Bank SCORE Project (P152241), investments and TA are being provided to build the core foundations for financial and private sector development.** Concretely, a basic core-banking system has been installed at the CBS and has begun to shore up the CBS' fiscal agency role enabling SFMIS integration and facilitating the MoF, the Office of the Accountant General, and other MDA digital payments, strengthening the legal and regulatory framework for mobile money services and a broad range of financial services beyond banking and money transfer services, building financial sector infrastructure, and institutional and enforcement capacity—all of which have effectively been absent. This will help strengthen CBS' supervision of the financial services market and build national payment platforms in

[54] These banks include (a) Dahabshil Bank International, (b) Salaam Somali Bank, (c) Premier Bank, (d) International Bank of Somalia, and (e) Amal Bank.
It is estimated that there are an additional 15 MTBs that have not applied for licensing and are operating as MTBs (World Bank 2015).
[55] These mergers are not limited to companies that provide financial services. They include sectors such as energy, construction, and real estate as well.
[56] The Dahabshiil Group is the largest and longest-established MTB in Somalia. It controls about 40–60 percent of the market (Lindley, A. and J. Mosely 2014).
[57] IMF Somalia Country Report No. 17/61 (Feb 2017).

support of greater financial inclusion, stability, and integrity. Other areas include supporting the MoCI to improve the country's investment climate; developing entrepreneurship and SMEs in support of the jobs agenda through support for the passage of a modern Company Law and implementing of a digital business registry; launching a BDS program for entrepreneurs; and mobilizing financing through the SBCF, which as of June 2018 reached 82 firms and committed to disburse US$6.5 million to firms in the agriculture, manufacturing, and fisheries sectors, and catalyzed the mobilization of US$1.1 million from financial institutions.

10. Boxes 3.1 to 3.4 provide snapshots of the key players in the financial sector in Somalia.[58]

Box 3.1. Overview of CBS

With the enactment of the FIL of 2012, the CBS embarked on the licensing and supervision of banks and MTBs. It recently partnered with the Somali Bankers Association to consider development of a centralized payment and clearing system.

Regulation of the sector includes the following measures:

- **Banks.** The CBS has developed subsidiary bank regulations to support bank licensing and supervision, including bank licensing, capital adequacy, liquidity risk management, internal audit, audit committees, audited financial statements, and related person transaction regulation. Banks had started to report quarterly earnings during September 2016.
- **MTBs.** The CBS has approved five regulations: (a) MTB Registration, (b) MTB Licensing, (c) MTB on Customer Identification, (d) MTB Operation, and (e) Anti-Money Laundering for MTBs. The CBS kicked off examination of the MTBs in 2016 with World Bank support under the "trusted third-party agent" project that monitored transaction flows and provided independent audits of the MTBs.
- **Mobile network operators.** There is no regulation on mobile money services provided by MNOs. However, draft regulations were finalized in September 2018 and the CBS is expected to seek comments on review of the draft. The regulations are expected to be implemented in January 2019.
- The CBS is also receiving TA and capacity development.
- **World Bank.** (a) Under the World Bank's SCORE Project (P152241), a new financial infrastructure for the CBS banking operations was developed; (b) development of the national payment Switch and ATS is under way as of September 2018; and (c) modernization of the 2012 FIL, national payments law, and insurance law is ongoing.
- **IMF.** The IMF's financial sector program includes TA and capacity development efforts covering the production of macroeconomic statistics and the development of adequate macroeconomic frameworks for monetary and fiscal policy formulation and implementation. Regarding bank supervision, the main components of this support are developing legal and regulatory frameworks, establishing supervision systems, and building capacity in all these areas.
- **U.S. State Department.** The State Department is providing TA to address deficiencies in Somalia's AML/CFT framework and developing the capacity of CBS to build AML/CFT assessment capability.

[58] During project preparation, the task team held discussions with development partners, targeted beneficiaries, and other stakeholders. The task team will maintain close collaboration throughout project implementation.

- Implementation capacity at the CBS is still weak; it lacks documented systems and procedures. The CBS will require strong TA to build institutional effectiveness in the short term coupled with long-term training and capacity-building efforts for officials.

Source: Interviews with financial sector stakeholders in Somalia conducted in September 2018.

Box 3.2. Overview of Commercial Banks in Somalia

- The Somali financial sector remains underdeveloped. Most of the population has limited access to banking services.
- Five banks operate across the Somali peninsula. The largest are the Dahabshiil Bank and the Salaam Bank (owned by Hormuud).
- Bank branches are in urban areas only.
- Only a few banks offer ATM and credit card services.
- Corporate banking and investment banking are being developed in line with Sharia. Savings of firms are pooled to vehicles in line with Sharia.
- Banks provide microfinance services using Islamic financing mechanisms such as asset-based financing instead of charging interest for loans.
- To reduce the risk of being associated with terrorism, Somali banks try to comply with international standards, especially KYC processes. To open a bank account, one needs to submit a passport, a national identification card, a job identification card, or a driver's license—documents that few Somalis possess.
- Not much data are available on the health of financial institutions.

Source: World Bank. 2017. *Mobile Money Ecosystem in Somalia: Household Survey and Market Analysis*. Washington, DC; interviews with financial sector stakeholders in Somalia conducted in September 2018.

Box 3.3. Overview of MTBs

- Eleven licensed MTBs operate across Somalia. Most have their headquarters abroad, in the United Arab Emirates, Canada, the United Kingdom, and the United States.
- Remittance companies usually have a good geographic coverage, with branches in most districts of Somalia and Somaliland.
- The largest MTBs are Taaj Remittances (owned by Hormuud), Dahabshiil Remittances, Jubba Express, Tawakal Express, Mustaqbal Express, and Amal Express.
- MTBs specialize in international remittances, which constitute their core business.
- MTBs also offer domestic money transfer services (for a fee), but this business has been largely taken over by domestic mobile money services (which handle these transactions for free).
- Competition among MTBs is strong. People usually choose remittance companies based on the fees they offer, which differ by the sending country. A recent competitive advantage for MTBs is the ability to send money directly to mobile money accounts, which have proliferated in the last few years.
- In the wake of the September 11 terrorist attacks and the general trend of global ‘de-risking’, banks have threatened to cut off Somalia’s remittance corridors to stop money laundering and terrorism financing. Al Barakat hawala network was then listed by the U.S. Government as a terrorist entity. As the then largest

private employer in the country, transferring over US$140 million a year from the Somali diaspora, the firm's shutdown placed an enormous strain on the Somali economy. Even now, the MTOs are afraid the situation might recur and are placing an increasingly strong emphasis on developing KYC processes that meet international standards.

Source: World Bank. 2017. *Mobile Money Ecosystem in Somalia: Household Survey and Market Analysis*. Washington, DC; interviews with financial sector stakeholders in Somalia conducted in September 2018.

Box 3.4. Overview of Mobile Money Operators

- The ICT sector in Somalia and Somaliland is dominated by the Hormuud conglomerate, which includes Hormuud in South Central, Golis in Puntland, and Telesom in Somaliland. All have similar shareholder structures, including common shareholders.
- Somtel is Hormuud's largest competitor. It is investing heavily in South Central to expand its market share.
- All MNOs provide mobile money services.
- Telecom companies in Somalia and Somaliland currently share three main features: (a) lack of regulation or 'self-regulation', (b) strong links with MTBs to facilitate international transfers, and (c) competitive strategies to maintain market monopoly of mobile money services. For instance, there are no charges for mobile money services which helps for take-up and retention of customers.

Source: World Bank. 2017. *Mobile Money Ecosystem in Somalia: Household Survey and Market Analysis*. Washington, DC; interviews with financial sector stakeholders in Somalia conducted in September 2018.

ANNEX 4: FINANCIAL INTERMEDIARY FINANCING

Objective

1. **The project proposes to establish an MSME Financing Facility initially capitalized with US$15 million to fulfil the project objective of increased access to finance for MSMEs supporting entrepreneurship and employment.** The objective is to kick-start financial intermediation for underfunded MSMEs representing the core of the Somali economy including women. PFIs will assume the credit risk for on lending to MSMEs and follow their respective pricing policies for financing taking into consideration prevailing market conditions.

Access to Finance Constraints

2. **MSME access to finance is very low in Somalia.** Current levels of lending by banks meet only 7 percent of the demand.[59] In 2019, Somalia ranked 186 out of 190 countries for access to credit indicator.[60] The MSME finance market can be characterized by supply-side and demand-side challenges. Some of these include the high cost of credit, underdeveloped product range, missing financial infrastructure (credit refencing and moveable collateral registries), security concerns, the informality of business structures, and poor organization of MSMEs as well as the elevated levels of guarantees required by banks (sometimes much higher than the amount of the loan). These challenges coupled with weak formal recourse to enforce contracts often block access to finance for MSMEs thereby crippling enterprise growth.[61]

3. **A recent market study commissioned by the CBS found that banks are largely bypassed by both businesses and individuals.** Banks only account for less than 45 percent of the actual supply of finance.[62] Somali financial institutions tend to concentrate on trade financing[63] and commercial financing to larger established enterprises that have sufficient collateral or urban customers that have already established steady cash flows (for example, from remittances) and are looking for short-term loans to address temporary liquidity constraints.[64] The lending portfolio of four banks surveyed during project preparation confirms the concentration on trade finance, making up on average 85 percent of the total portfolio. There is little to no investment in productive sectors such as agriculture or energy. Banks consider productive sectors as risky, especially agriculture, where most agricultural production is in areas under the control of

[59] CBS (Central Bank of Somalia). 2018. “Unleashing the Power of Financial Intermediation in Somalia: Expanding the Circles of Trust Beyond Family and Friends.”
[60] Doing Business Report, 2019.
[61] Somalia Systematic Country Diagnosis, 2018.
[62] CBS (Central Bank of Somalia). 2018. “Unleashing the Power of Financial Intermediation in Somalia: Expanding the Circles of Trust Beyond Family and Friends.”
[63] Trade financing within the portfolio of Somali financial institutions refers to any trade-related financial transaction, be it domestic or international, utilizing asset-based Murabaha financial products for all sectors and project-financing Istisna products targeting the real estate sector. Domestic trade financing constitutes the overwhelming portion of the Somali commercial banks’ trade portfolios. This is due to difficulties in accessing correspondent banking and global financial systems.
[64] Based on task team discussions with banks during project preparation in September 2018.

Al Shabaab.[65] On the energy side, there was some interest in expanding energy investment portfolios, especially for off-grid solutions.

4. **Lending to women and female-owned businesses is virtually nonexistent.**[66] The welfare consequences are dire when it is estimated that women are the main breadwinners in 70 percent of Somali households. The informal and micro nature of female-run businesses is an important factor that is both a determinant of their financial constraints (because banks lend less to these types of businesses) and their consequence (because women lack external finance they are forced into low capital requirement sectors). The higher incidence of female-operated microbusinesses is also attributed to their need for a 'coping mechanism' from the high rates of unemployment; however, they remain trapped for reasons related to the cost of doing business, including lack of access to collateral for loans, lack of BDS and business networks, and immobility due to insecurity. More highly educated women and returning diaspora are beginning to enter sectors traditionally dominated by men, such as agriculture and fisheries, but their total numbers remain low.[67]

Rationale for the MSME Financing Facility

5. **The line of credit available to eligible bank and non-bank financial institutions will be adapted to the current country context of access to finance constraints.** The FGS will create an autonomous and independent MSME Financing Facility that would help kick-start MSME banking in underfunded sectors and market segments. The MSME banking will need to be integrated into the commercial strategy of each participating bank and non-bank financial institution in so far as the MSME Financing Facility signs a participation agreement with that bank or non-bank financial institution. The agreement will define the eligibility criteria/rules for final beneficiaries with freedom of credit decisions left to the banks. The agreement will be reviewed annually.

6. **The MSME Financing Facility will use private sector management and governance principles, thereby providing important complementarities to investors and private capital mobilization efforts by the FGS.**[68] This will be achieved through initial capitalization of the entity using public funding from IDA but subsequently opening up the entity to sequential private sector investing and shareholding through additional calls for capital investments, co-investing in business expansion, or deal referring. Broadening the capital sources for the autonomous entity and the choice of financial instrument available over time will help create a Somali entity with a commercial orientation that can act as a platform used to crowd-in additional private and public financing from other sources and potentially future engagement by DFIs, thereby fostering financial sector development and sustaining the most dynamic MSMEs, in a capital constrained environment. As such, the MSME Financing Facility represents the first step to a long-term challenge to improving private capital mobilization and investment capacity of financial institutions and

[65] The productive areas of agriculture are concentrated in the basin between the two rivers in south Somalia.
[66] Somalia Country Partnership Framework, 2018.
[67] UNDP. 2015. *The Role of Somali Women in the Private Sector*.
[68] There is no overlap between the MSME Financing Facility under SCALED-UP and SCORE's (P152241) SBCF. This is because the SBCF is a matching grant scheme that completely intermediated directly with beneficiaries, rather than delivering financing through the domestic financial sector. The scheme will be phased out in January 2019 to focus development efforts on strengthening market-based financial intermediation and capacity building of financial institutions.

reducing their overreliance on humanitarian assistance to support income-generating lending in micro and small businesses using noncommercial lending channels and sources of capital.

7. **The eligibility criteria for participation in the MSME Financing Facility will involve a holistic assessment of the participating bank or non-bank financial institution to credibly serve underfunded MSMEs.** Capabilities assessed will include capacity to (a) develop, design, and launch new products targeting MSME market segments beyond trade finance; (b) market and execute promotional campaigns to build awareness of new products and offerings; (c) connect with specific customers to sell specific products and offerings; (d) onboard customers and set up accounts and products, managing relationships and potentially expanding services over time; (e) work across product families and customer types; and (f) assets and liabilities management (ALM).

8. **The establishment of the MSME Financing Facility will incentivize PFIs to develop necessary skills of their staff on MSME banking techniques to improve on the financial products offered.** In this regard, IFC support covering provision of TA to PFIs for the development of MSME banking will be central. Potential conflict of interest connected to IFC investments further down the line will be managed through disclosures on how the conflict will be managed (whether it is actual or perceived). The envisaged implementation support will include operationalization of the MSME Financing Facility and capacity building TA for the PFIs to equip them with adequate skills and tools for using alternative approaches to evaluate the creditworthiness of loan applications. Specifically, the project activities will be complemented by the IFC's Financial Institutions Development Program (FIDEP, ID: 602159) that will help PFIs develop enterprise capability to enter new markets (see box 4.1). The PFI eligibility criteria to the MSME Financing Facility will be linked to the PFI capacity of reaching out to women and female-owned MSMEs as an integral element of their commercial strategy.

Box 4.1. Scaled-Up Design Is Closely Linked to FIDEP Support to Somali Financial Institutions

FIDEP (ID: 602159) is currently under preparation by the IFC. The program will aim to strengthen Somali financial institutions, size up market potential, and identify key players and strategic partnerships to launch new products and services with select financial institutions to expand access to finance in Somalia.

The program aims to identify gaps in institutional capacity through investment services-led bank appraisals and advisory services-led diagnostic assessments of individual financial institutions and provide them in-depth advisory support to strengthen governance, risk management, financial and prudential reporting, MIS, and E&S capacity to remove bottlenecks to investment and improve performance. It aims to further support financial institutions to build capacity to launch innovative products and services to expand financial services to MSMEs and the retail segment to help reduce their constraints to investment and economic growth.

FIDEP will cover the following three components:

- **Institutional assessment and strengthening component** which aims to strengthen key players in the financial sector to address governance and compliance constraints will support them to improve MIS, financial and prudential reporting, governance, E&S capacity, and risk management.
- **Innovative financial products and services component,** which aims to launch innovative financial products and services for MSMEs and retail customers to expand financial inclusion, will scope market opportunities, select FI implementation partners, and provide in-depth support to build capacity.

- **Training and knowledge-sharing events component,** which aims to reinforce the strengthening of financial sector players, will provide skills training, awareness raising, and knowledge-sharing events anchored on the activities supporting the strengthening of individual financial institutions.

9. **The MSME Financing Facility will help drive competition in financing MSMEs by operating as a revolving line of credit offering advances to banks on a first-come first-served basis.** So far, four of the five registered Somali banks have solicited the FGS and the World Bank to set up the MSME Financing Facility. Banks are aware that this market segment is insufficiently supplied with credit and has a strong growth potential. Therefore, the MSME Financing Facility will operate through two separate financing windows addressing different customer-facing channels and lines of business emphasizing the need to tailor the framework to an individual PFI's line of business structure, products, and priorities as follows:

- **A 'large loans' window to cover large loans to SMEs (large businesses).** The eligibility criteria for borrowers would be flexible. However, informal enterprises will not be accepted. All advances will be in U.S. dollars and all types of credit would be eligible (working capital and investment loans), except trade finance.

- **A 'micro and small loans' window that would be open to micro and small enterprises, individuals, and groups**. This will include informal microenterprises and groups with a commitment to formalize during the loan repayment period. All advances will be in U.S. dollars and all types of credit would be eligible (working capital and investment loans) except trade finance.

10. **The credit files of borrowers will be analyzed by the PFIs rather than the MSME Financing Facility itself.** The Participation Agreement signed between the MSME Financing Facility and the PFIs will require the application by the PFI to meet good banking practices and processes for granting credit to MSMEs including the responsibility for E&S safeguards assessments and monitoring of the risk of nonrepayment. The MSME Financing Facility will not carry out any analysis of the quality of the credit risk in the loan file of the final borrowers as this will have to be undertaken and approved by the PFI before being submitted for financing.[69]

11. **The MSME Financing Facility will use simple management tools to protect itself against excessive risk deterioration in the loan portfolio.** For disbursement calls made on the MSME Financing Facility, the Participation Agreement signed with PFIs will designate that the reserve currency account held at the CBS as the collections account. On advice of the MSME Financing Facility, direct credits will be raised by the CBS for payments (disbursements) or direct debit for receipts (collections). In the case of collections, direct debits will be raised in accordance with the loan amortization schedule for loan repayments and charged against the PFI's balances held on the reserve currency account. This effectively spreads out the MSME loan portfolio into a series of fixed repayments over time and will ensure that the MSME Financing Facility's Reflows Account (revolving fund) is sufficiently funded to facilitate multiple

[69] Qualifying firms may access on-demand BDS with support from the MSME Financing Facility. SCORE (P152241) has helped activate the BDS market in Somalia through the US$5.5 million SMEF which is being phased out in March 2019.

cycles of new loans on an ongoing basis (that is, this is expected to be at least fortnightly loan repayments by the PFIs). A maximum amount of borrowing for each bank will be set at 20 percent of total capital.

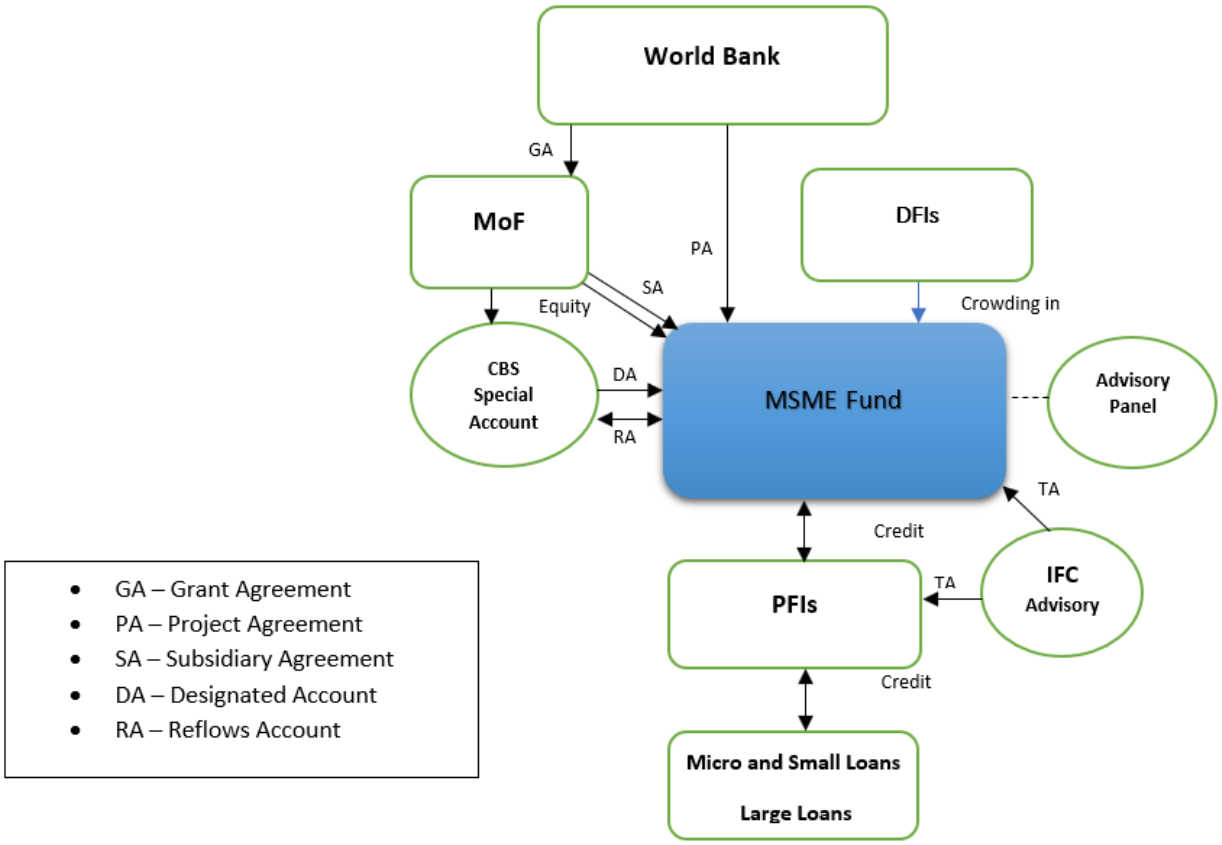
Governance and Flow of Funds

12. **The MoF will set up the MSME Financing Facility as a legal entity under national legislation.** The MSME Financing Facility would be managed using private sector governance principles.[70] A subsidiary agreement will be signed by the MoF with the MSME Financing Facility setting out the obligations of both parties on management of the US$15 million. The project proceeds from IDA and the SMPF will be channeled through the DA-BB, which will be used to manage funds earmarked for Subcomponent 2.1 (financial intermediary financing for MSMEs). Figure 4.1 depicts the key features of the MSME Financing Facility's flow of funds from the World Bank to the final beneficiary. The agreement will be supplemented by an MSME Subproject Manual that would establish the operating policies and procedures for the MSME Financing Facility which will include application of the World Bank's Anti-Corruption Guidelines considering the specifics of the project. The MSME Financing Facility will use automated/digital systems on M&E of PFIs and borrower subprojects and reporting on the loan portfolio performance. An independent board of directors will have oversight of the MSME Financing Facility. It will also have responsibility for setting up a robust system to deal with actual or perceived malfeasance or unfairness in terms of who benefits from the MSME Financing Facility. As the representative of the FGS, currently the sole shareholder, the MoF will have oversight mandate on the MSME Facility through a strengthened PIU. Furthermore, the Auditor General will according to the Public Financial Audit Act carry out regular and systematic audits on the operations of the MSME Financing Facility.

13. **The MSME Financing Facility will initially set up a special account at the CBS.** The CBS will not bear the financial losses of the MSME Financing Facility. Initially, no credit subsidies or Government-sponsored guarantee programs are envisaged under this project. Changes to the implementation arrangements will be made in consultation with IDA. Similarly, the MSME Subproject Manual will be updated from time to time based on experience in the field and in consultation with the World Bank Group.

[70] CBS has experience in managing special ring-fenced accounts on behalf of the FGS and the FMS in accordance with Subsidiary Administration Agreements. A fitting example is the two special accounts set up for the potential petroleum and fisheries revenues which is administered by CBS on behalf of the FGS and FMS.

Figure 4.1. Flow of Funds



14. **The MSME Financing Facility MSME Subproject Manual will address possible areas where conflict of interest might arise internally.** The main safeguard against this is that the MSME Financing Facility will not analyze the quality of risk on the credit file of the sub-loan borrowers. The assessment of quality of risk on the individual borrower or the PFI will be made by the PFI. The MSME Financing Facility will assess the capability of the bank to serve MSME segments and productive sectors targeted by the project.

15. **The end of life of the MSME Financing Facility will not be determined.** The MSME Financing Facility is intended to operate for as long as possible, thus rendering a sustainable service for the financing of MSMEs. The operational flexibility of the MSME Financing Facility, concerning the definition of eligibility criteria, would make it possible to consider the FGS priorities for specific segments of the economy. Any changes to the charter, board of directors, and senior management as well as eligibility criteria during the life cycle of the project can be implemented in consultations with IDA. The focus of the MSME Financing Facility on underfunded market segments in key service and productive sectors representing the core of the Somali economy, including the quest for fiscal sustainability, are two aspects to differentiate the

MSME Financing Facility from the previous World Bank SME financing programs in Somalia under the SCORE Project (P152241).[71]

16. **Limited TA will be provided within the MSME Financing Facility.** This aims to support the launch and the first phase of development of the two financing windows and the PFIs that will use them. The MSME Financing Facility will be managed by a lean and professional management team with experience in banking, microfinance, investments, and accounting. This will ensure that the eligibility criteria are respected and independence from political influences is maintained in the evaluations of PFIs and loan applications by final beneficiaries. Depending on the quality of management and their financial strength, PFIs may benefit from TA to improve enterprise capacity to reach the targeted MSME market segments. As stated previously, FIDEP (ID: 602159) will help Somali financial institutions develop enterprise capability in these new markets. IFC may also provide TA to the MSME Financing Facility on defining a strategy that would as far as possible ensure continuation of services and professional management of the MSME Financing Facility after project closure, provisionally set for June 2023.

Apex Pricing Mechanism and Retail On-lending Rates

17. **The MSME Financing Facility will deliver funds to PFIs for on-lending at a minimum rate of 4 percent per year.** The expectations are that PFIs may add a markup of at least 4 percent to the cost of funds such that the borrowing cost for final beneficiaries would be at least 8 percent per year. This is equivalent to the current 12-month U.S. dollars LIBOR interest rate + 5 percent per year (see table 4.1).[72] As of September 2018, the pricing (mark-ups) range for murabaha facilities was between 8 percent and 12 percent. The terms and conditions of loan obligations of the PFIs to the MSME Financing Facility may be designed after taking into consideration implications for viability and risk profile, although, in some cases, banks may require collateral from final beneficiaries—the MSME Subproject Manual will reflect a more detailed and final position on this and other design factors. Nevertheless, transaction fees on loans will be charged by the MSME Financing Facility, which will cover the cost of funds to the FGS marked to market, covering credit risk losses, and fund management costs.

Table 4.1. Rate, Margin, Spread Models

	Commercial Bank Model	Islamic Model
Cost of the IDA credit to the Government	Fee 1% per year (40-year term)	1% per year
Margin to Government/Apex Unit (credit risk)	Approx. 2.5% per year of outstanding funding allocation to PFIs	Annual fee to Government 2.5% of outstanding funds
Apex Unit management fee	Approx. 0.5% per year of outstanding funds to PFIs	0.5% per year of outstanding funds
Cost of funds to bank (to be confirmed in discussion with CBS)	Approx. 4% per year	Up-front premium on sub-loans to borrower enterprises (equals 4% per year of outstanding funds)

[71] The SCORE Project (P154421) operated the SBFC, which was a matching grant program.
[72] The 12-month U.S. dollars LIBOR interest rate is the average interest rate at which international banks are prepared to lend to one another in U.S. dollars with a maturity of 12 months. LIBOR interest rates are also used as the base rate in setting the level of their loan interest rates.

	Commercial Bank Model	Islamic Model
Sub-loan at market rate/ premium to borrower enterprises (total of above plus markup by bank depending on borrower credit risk and tenor).	Approx. 8% per year[a]	Up-front premium (equals cost of funds to bank [4%] plus markup by banks depending on borrower credit risk and tenor)

Note: a. This is equivalent to current 12-month U.S. dollar LIBOR interest rate + 5% (as of January 2019).

18. **Any subsidy component in pricing will be explicit and transparent** with a view to gradually being phased out as scale is built up for commercial credit to hard-to-reach micro and small enterprises in underserved market segments. PFIs will have the freedom to add a markup depending on borrower risk, as assessed using information from third parties (for example, credit referencing services) or based on information submitted by the borrowers themselves. The longer the repayment period for a loan, the higher the fees the final beneficiaries may pay. The loan pricing may be reviewed semiannually after taking into consideration changes in pricing policies for PFIs and market conditions.

Eligibility Criteria for PFIs

19. **Every bank or non-bank financial institution seeking to participate on the MSME Financing Facility will be required to fulfill the minimum eligibility criteria described, on an ongoing basis:**

Corporate Requirements

- Valid license to operate by the CBS.
- Compliance with World Bank Directive on Investment Policy Financing and adherence to prudential regulatory ratios, minimum capital, and operational standards as may be set out in the MSME Subproject Manual such as fit and proper controllers and managers, adequate profitability and capital, strong management and healthy portfolio quality, that is, liquidity, loan loss provisioning, and NPLs[73] at 10 percent or less.
- Governance structures that demonstrate adequate managerial autonomy and commercial orientation. Credit policies and procedures covering analysis of loan appraisal process, loan granting, loan monitoring and recovery, credit risk rating, and E&S safeguards assessments of subprojects in accordance with World Bank E&S safeguards standards.
- MIS and financial statements that demonstrate conformity with international financial reporting norms.

[73] Currently, CBS has no regulatory benchmark on NPLs. However, CBS is committed to a new regulation by March 2019 on loan classification and provisioning and would enforce compliance by banks. The MSME Subproject Manual may be updated from time to time in consultation with the World Bank Group. PFI access to the MSME Financing Facility is subject to compliance with said CBS regulations to ensure the soundness of PFI operations and shore up fiscal sustainability. TA support may be triggered and provided by IFC's FIDEP and an FIDP developed and monitored to improve PFI regulatory compliance and risk management.

Strategic Requirements

- Bank and non-bank financial institution applicants must demonstrate capacity and strategy to raise capital resources contributing to the PDOs, as well as demonstrating the financial and technical viability, market analysis, and business capacity.

- MSME banking capabilities to address MSME financing needs in market segments and sectors targeted by the project and capacity to manage the corresponding portfolio, that is, to appraise and supervise sub-loans, especially in the case of sector-specific financing (such as energy and livestock) and market segments (such as microfinance, consumer finance, women and female-owned MSMEs), and manage loan collections in specific sectors, that is, MSMEs.

- Bank and non-bank financial institution applicants must keep accounting for MSME Financing Facility sub-loans separate and distinct from the rest of their loan portfolios.

- Bank and non-bank financial institution applicants must support monitoring and reporting of the PDO and intermediate results indicators including key performance indicators (KPIs) defined by the MSME Financing Facility in consultation with IDA on issues such as number of new jobs generated through the sub-loans, data on sales revenues and the additional reporting requirements stipulated in the MSME Subproject Manual. Covenants may be added in the MSME Subproject Manual on promoting responsible MSME banking practices by PFIs and these may be embedded in the Participation Agreement. KPIs will be collected as baseline when the loan is given to a final beneficiary. At mid-term another collection will be undertaken and thereafter at the end of the project.

20. **Conditional eligibility (Institutional Development Plan).** In cases where a prospective PFI does not fully comply with all the criteria, it can still be allowed to participate in the MSME Financing Facility on an exceptional basis, provided it agrees to an FIDP. The areas covered by the FIDP may include target quotas for lending to women, improvement of products, market outreach, and risk management practices to women customers and female-owned MSMEs. The level of access to the MSME Financing Facility will be linked to achieving the performance targets stated in the FIDP, and continued eligibility of the PFI would depend on its satisfactory compliance with the agreed FIDP. However, those PFIs deemed to pose a significant challenge to the financial integrity and sustainability of the MSME Financing Facility due to noncompliance with the CBS' prudential regulations particularly on asset classification as well as risks and internal controls would only be brought on board upon full compliance. In all cases, FIDEP (ID: 602159), working together with the bank, may use the FIDP to provide timely and targeted TA addressing the gaps identified by the capability assessment. The participating banks and non-bank financial institutions will be required to appoint a designated staff member who will be accountable for implementing project E&S requirements (although responsibilities may be assigned to a qualified, external consultant).

Eligibility Criteria for Subprojects/Final Beneficiaries

21. **The MSME Financing Facility will operate two financing windows.**

Large Loans Window

- Funding availability for large loan applicants will range between US$50,001 and US$150,000. Currently it is expected that the tenor for large loan financing is expected to not exceed three years.[74] The grace period of up to 12 months may apply.

- SME applicants must be engaged in business activities in productive sectors such as energy and livestock sectors (covering value chains, renewable energy, dairy, including processing and distribution activities, manufacturing, and technical and business services).

- SME applicants must demonstrate innovative approaches in addressing enterprise growth and development objectives as elaborated in the MSME Subproject Manual, as well as demonstrating the subproject's economic growth potential, financial and technical viability, market analysis, and business capacity.

- SME applicants that are start-ups must demonstrate that they have been active in establishing a business by the time the loan is awarded. This entails demonstrating that they have been operating for at least 12 months. Such applicants must show that they have demonstrated business experience and strong knowledge of the sector.

- SME applicants should also show evidence that they can maintain a sound accounting system and have internal controls in place to support the FM of the loan. They should also show that they are maintaining a transparent business consistent with World Bank procurement rules and E&S safeguards requirements.

- SME applicants must be officially registered by the MoCI and tax authorities and must attach the business and tax registration certificate. No loans will be awarded without proper registration and current business license (if applicable).

- SME applicants may submit only one application to the MSME Financing Facility and can only have one active loan at a time. However, earlier beneficiaries can participate in the subsequent loan cycles once the facility is fully repaid.

Micro and Small Loans Window

- Funding availability for individual microenterprise or consumer loans will range between US$500 and US$5,000 and small loans will range between US$5,001 and US$50,000. Tenor

[74] Though this and other design factors may evolve over time and the policies/updates will be reflected in the MSME Subproject Manual.

for micro loans is expected to not exceed 18 months, and for small loans to not exceed three years. Maximum grace period of six months may apply for both micro and small loans.

- For microenterprises investments, short-term/working capital loans are eligible. For consumer loans, life cycle expenses including those that address emergencies and children's enrollment in schools are eligible. For businesses (operational or start-ups), microloans are open to all sectors of the economy except trade financing.[75]

- It would be impractical for the MSME Financing Facility to assess individual microloans to final beneficiaries. Instead the due diligence assessment by the MSME Financing Facility will focus on the overall adequacy of the MFI program for each PFI. As such, the MSME Financing Facility may fund an MFI program up to US$1 million or 20 percent of total capital of the PFI, whichever is lower, depending on management strength and banking enterprise capability.

- Currently, loan products are typically catered to traders. As such, every bank or non-bank financial institution will need to show how its MFI program meets finance demands of productive and consumer markets.

- Every bank or non-bank financial institution must demonstrate capacity and strategy to mobilize resources to achieve financial sustainability of microfinance services, that is, sound, responsible commercial orientation; transparent reporting processes; operational self-sufficiency, human resources, and internal controls; and customer orientation (especially for women and female-owned microenterprises).

- Every bank or non-bank financial institution will need to demonstrate that it has adequately targeted low-income populations with MFI instruments to increase financial access at the bottom of the pyramid, especially increasing women's access to financial services.

- MFI programs need to demonstrate capacity for economic empowerment of beneficiaries supported by microfinance services in terms of economic participation or increased decision making at the microenterprise level, increased self-esteem gained from being able to provide for their family (for example KPIs may track increased ownership of assets, improvements in household welfare by beneficiaries overcoming food insecurity, paying bills for energy, education, medical, and other life cycle expenses).

Monitoring, Reporting, and Evaluation

22. **The purpose of monitoring, reporting, and evaluation will be to aggregate the project results.** The MSME Financing Facility will undertake the monitoring of funded subprojects and report to the board of directors and IDA on individual subprojects and the portfolio. It will be necessary to be able to collect data from individual subprojects within a consistent framework. A Monitoring and Evaluation Framework

[75] Trade financing within the portfolio of Somali financial institutions refers to any trade-related financial transaction, be it domestic or international, utilizing asset-based Murabaha financial products for all sectors and project-financing Istisna products targeting the real estate sector. Domestic trade financing constitutes the overwhelming portion of the Somali commercial banks' trade portfolios. This is due to difficulties in accessing correspondent banking and global financial systems.

(MEF) will address both the accountability and learning needs for internal and external audiences. The MEF will be designed to collect information on subproject results and assess how these results are contributing to the project's purpose and goal over time including the measurement of systemic changes to markets.

23. **Milestone targets set out by applicants in their loan applications to PFIs will serve as KPIs to be measured throughout the life span of the project.** The baseline targets for these KPIs will be verified and agreed on during the pre-financing phase by the PFI and will be included in the PFI's disbursement request to the MSME Financing Facility and thereafter tracked as milestone deliverables. The MSME Financing Facility will rely on the final beneficiaries to deliver accurate information on the progress of their projects. The MSME Financing Facility will require two types of reporting from beneficiaries: (a) from PFIs: financial performance indicators (capital adequacy, profitability, portfolio quality) and technical milestone reporting for IDPs and (b) from final beneficiaries: KPI reporting.

MSME Financing Facility Governance, Terms of References, and Basic Accountabilities

MoF

- The MoF enters into the Subsidiary Agreement with the MSME Financing Facility to manage a ring-fenced special account at the CBS, that is, DA and RA of the MSME Financing Facility.
- It acts as the legal sponsor mandated to set up the MSME Financing Facility.
- The MoF provides initial equity to set up the MSME Financing Facility using IDA financing of about US$1.5–US$2 million.
- It appoints an independent and autonomous board of directors to oversee the MSME Financing Facility according to charter. The board in turn appoints a qualified management team. IFC and other DFIs or donors may also consider an implementation support role, including participating as directors on the board of the MSME Financing Facility.
- Any conflict of interest in view of proposed IFC involvement will be managed through disclosure to the FGS, through a letter that describes the activities of the World Bank and of IFC and how the two institutions will manage the conflict (whether it is actual or perceived).[76]

MSME Financing Facility

- The MSME Financing Facility will be set up as a dedicated and autonomous entity. Its board of directors will be appointed by the MoF together with other participating donors and contributors on clearly defined criteria set out in the articles of incorporation (charter) and stipulated in the MSME Subproject Manual. The board will independently supervise the MSME Financing Facility and management team.

[76] In the event of the IFC engagement materializing, provision of implementation support will be defined in the TA Agreement with the MSME Financing Facility.

- The MSME Financing Facility will have ultimate authority for operational decisions and risk management, as well as how it will manage capacity-building activities of the PFIs.
- It will be furnished with a competent and experienced management team recruited on merit by the board.
- It will be responsible for undertaking independent decisions on selection of prospective PFIs as stipulated in the MSME Subproject Manual and pricing based on market terms and conditions.
- It will also be responsible for outreach, monitoring, and reporting of the performance of the MSME Financing Facility.
- It will be exposed only on credit risk of the PFIs and not on subprojects.
- The MSME Financing Facility will enter into a Subsidiary Agreement with the MoF. The agreement gives the entity the legal mandate to manage the DA and RA through a ring-fenced special account at the CBS.
- The MSME Financing Facility will also sign a Project Agreement with IDA to enable coverage of obligations and responsibilities related to, among other things, safeguards and anticorruption.

Advisory Panel

- A broad-based outside panel will bring together relevant experience and expertise covering the FGS MDAs, FMS (including Somaliland), private sector, and civil society. IFC and other DFIs or donors may also consider participating. In the event of IFC engagements materializing, potential conflict of interests connected to IFC investments further down the line will be managed through disclosures (whether the conflict is actual or prescribed).
- The panel will provide recommendations and advice to the board of directors and management of the MSME Financing Facility.
- The panel will include provision of Sharia advice regarding the financial instruments used by the MSME Financing Facility.
- It will also include an external monitoring agent.

ANNEX 5: GENDER ANALYSIS

A. Overview of Gender Gap Analysis

Labor Market Gender Gaps in Somalia

1. **Women currently face discrimination and considerable socioeconomic barriers to accessing jobs and livelihood opportunities in Somalia.** The Gender Inequality Index for Somalia is 0.776, making it the fourth highest level of inequality recorded globally.[77] Somalia also remains one of the few countries worldwide that has failed to ratify the 'Convention on the Elimination of All Forms of Discrimination against Women'. In 2017, women's labor force participation was a mere 37 percent, compared to 58 percent for men—corresponding to a 20 percentage point gender gap.[78] Women are thus experiencing far lower levels of employment than men—the employment rate for women is estimated to be a mere 10 percent, while it is 32 percent for men—equivalent to a 22 percentage point gender gap.[79] Moreover, women typically earn much lesser than men when undertaking work of equal value to men.[80]

2. **Traditional gender roles still limit women's employment opportunities, often excluding them from work within formal sectors**.[81] The gender gap in workforce participation is mainly due to women engaging in unpaid domestic work, assuming responsibility for family and household care. Though 64 percent of Somalis deem it acceptable for women to work outside the home,[82] few women are active in profitable sectors such as livestock export and fishing, and women face higher barriers in terms of accessing nonfarming job. Qualitative data from gender-focus groups, for example, suggest that current social norms limit the practice of employing women. Moreover, insecurity and internal migration has resulted in many female-headed households within the IDP community.[83] Women are therefore more prone to being self-employed[84]—starting a microbusiness due to economic push rather than pull factors.[85]

Gender Gaps in Relation to Financial Services Access and Lending

3. **Somali women are largely responsible for a growth in microenterprise and yet are not supported to grow and expand their businesses.** Up to 60 percent of microbusiness owners are women. However, these businesses struggle to expand due to, for example, poor access to credit, weak availability

[77] UNDP. 2012. *Somalia Human Development Report: Empowering Youth for Peace and Development*. p. xviii.
[78] World Bank. 2018. *Somali Poverty and Vulnerability Assessment*. However, the poverty profile from the year prior points to an even large gender gap—some 32 percentage points—with 55 percent and 23 percent participation among men and women, respectively.
[79] World Bank. 2016. *Somali Poverty Profile*.
[80] World Bank. 2018. *Doing Business Survey*.
[81] Bertelsmann Stiftung. 2016. *Somalia Country Report*; ITC (International Trade Center). 2012. *Women and Trade in Somaliland*. See: http://www.tradeforum.org/article/Women-and-trade-in-Somaliland/.
[82] World Bank. 2018. *Somali Poverty and Vulnerability Assessment*.
[83] Out of 10 households, 4 are headed by women, according to the World Bank, 2018, Somali Poverty and Vulnerability Assessment. However, among IDPs, households are slightly more likely to be headed by women—every second house (54 percent) is estimated to be female headed.
[84] Gender Focus Groups, organized as part of the World Bank's Somalia Mobile Money Ecosystem Survey - thematic extension, 2018.
[85] World Bank. 2018. *Somalia Systematic Country Diagnostics*.

of BDS, a complex taxation policy, and other administrative requirements.[86] Limited availability of supporting networks for incubation disproportionately affects women as they have weaker access to strategic networks and strong clan connections that men typically leverage to help ensure business success.[87] The same barriers are assumed to limit women's access to finance as most borrowing is currently sourced informally through friends and family. However, other common reasons cited for not borrowing include not knowing how to access lending services.[88] Moreover, women struggle to function in an environment where vital business information is still shared in a very informal manner.[89] In sum, there is ample scope for boosting women's contribution to economy and their participation in the labor market, by supporting female entrepreneurship and greater access to enabling digital and financial services.

4. **Weak access to tailored formal finance and microcredit schemes limit female entrepreneurship.** A recent review of the World Bank's SMEF, which provided BDS to SMEs, reiterates that women-led businesses struggle to access funding. Moreover, the present level of female participation in the SMEF's support programs indicate that there is demand for financing among female-headed SMEs.[90] However, key lending institutions and financial service providers do not necessarily offer women-friendly loans or financial products that target women nor do they implement a cohesive policy that targets women in a way that removes barriers that currently restrict access.[91] For example, women face discrimination in accessing credit due to existing collateral requirement. Existing inheritance laws, based on Sharia law, entitle women to inherit less than men, leaving women with less collateral.[92] Moreover, even when women have the required collateral, banks typically ask for a male guarantor. Finally, when women do receive loans, the amounts are typically very small—that is, in the range of US$1,000. The problem is both a supply-side (banks are nervous about lending) and demand-side (women possibly ask for smaller amounts) issue.[93]

5. **Women have weaker access to traditional financial services, more broadly.** One reason for this is lower ownership of identification documents (more on this in the following paragraphs). While access to banking is generally low—a mere 16 percent for Somalis over the age of 16—female access is considerably lower. A mere 11.5 percent of women use traditional banking services, versus 19.0 percent for men, resulting in a 8 percentage point gender gap. Among current bank account holders identified, 63.3 percent were men and 36.7 percent were women.[94] Women's access is also much lower than in neighboring Kenya, where 53 percent of women have bank accounts.[95] Gender income inequality has

[86] World Bank. 2018. *Somalia Systematic Country Diagnostics*.
[87] UNDP. 2014. *Strengthening Gender Equality and Women's Empowerment in Somalia 2015–2017*; UNDP. 2015. *The Role of Somali Women in the Private Sector*.
[88] World Bank. 2017. *Somalia Mobile Money Ecosystem Mapping - Household Survey.*
[89] UNDP. 2015. *The Role of Somali Women in the Private Sector*.
[90] BDO. 2018. *Establishment and Management of a Somali SMEF, 7th Progress Report January 2018–March 2018*.
[91] UNDP. 2015. *The Role of Somali Women in the Private Sector*; and the World Bank consultation with financial service providers.
[92] World Bank. 2018. *Somalia Systematic Country Diagnostics*.
[93] Based on the World Bank's conversation with local banks that extend credit to microfinance institutions.
[94] World Bank. 2017. *Somalia Mobile Money Ecosystem Mapping - Household Survey*.
[95] World Bank Group. *World Development Indicators*. https://tcdata360.worldbank.org.

been identified as another key reason for stronger male bank account ownership.[96]

6. **Conversely, there is a smaller gender gap related to access and usage of mobile money services, creating a compelling entry point for scaling women's access to financial services through mobile and digital finance.** The gender gap in usage is a mere 5.0 percent, whereas it is 19.5 percent on average in the rest of Sub-Saharan Africa. Most women do not claim to be subject to discrimination when using mobile money and view mobile money as safe and as a tool for increasing their financial independence. [97] These findings suggest that a scale-up of digital payments and business models that leverage mobile money could boost women's access to Government and private services.

Gender Gaps in Relation to ID Ownership

7. **Not having access to ID limits both movement and other opportunities for women.** Survey data from 2017 suggest that 56.2 percent of people in Somalia of age 16 and above do not have a proof of identity. If the under-five birth registration rate is applied to estimate ID coverage for the whole under-16 population, over 77 percent of the population, or close to 12 million people, are estimated to lack an ID today. Women are more likely to lack an ID than men: the current gender gap in ID access is estimated to be larger than 10 percent.[98] On average, the gender gap in ID ownerships is estimated to be 15 percent in low-income countries. [99]

8. **Having a formal proof of identity is a prerequisite to be able to act independently, in both the socioeconomic and political spheres.** For example, having a proof of identity is typically a prerequisite for opening a transaction account in one's own name. Evidence from Somalia suggests that in the absence of ID, women need to rely on male relatives or community leaders to confirm their identity, creating a high level of dependence.[100] Equally, being able to uniquely identify customers is also instrumental for establishing a credit history and thus for accessing affordable and formal credit. Identification is also critical to securing ownership over assets, such as land, property, a business, or to establish a formal claim to an inheritance. In other words, gender gaps in ID access have ripple effects on women's financial inclusion, entrepreneurship, and livelihoods. Boosting women's ID ownership could thus help to also close the gender gap in these areas.

Gender Gaps in Sectoral Strategy

9. **Existing Government policy frameworks pertaining to the financial and ICT sector take little to no consideration of existing gender gaps.** This is partially due to weak female representation in politics and public administration, more generally.[101] Moreover, in cases where policies have been developed,

[96] World Bank. 2017. *Somalia Mobile Money Ecosystem Mapping - Household Survey.*
[97] World Bank. 2017. *Somalia Mobile Money Ecosystem Mapping - Household Survey.*
[98] Preliminary research findings from Somaliland suggest that the gender gap in ID access is 9 percent. However, Somaliland is known to have the most comprehensive ID coverage. The national figures are thus estimated to be significantly higher.
[99] World Bank. 2017. *ID4D-Findex Survey*. http://pubdocs.worldbank.org/en/953621531854471275/ID4D-FINDEX-Note-Release2018.pdf.
[100] World Bank. 2017. *Somalia Mobile Money Ecosystem Mapping - Household Survey.*
[101] For example, women hold only 14 percent of the seats in the federal Parliament. Equally, traditional clan-based systems, such as Xeer, also prevent women from speaking at public hearings.

they are often not well implemented and truly attuned to the barriers that women face. This issue extends to the private sector, as noted earlier.[102] However, evidence from Somalia suggests that tailored strategies can boost women's access to financial and Government services when these strategies are consciously implemented. [103]

B. Project Activities to Address Identified Gender Gaps

Strategy Development and Capacity Building

10. **The project will encourage a gender-sensitive approach to the development of sectoral strategies, which will help address the gender gaps identified.** The project has, for example, earmarked funding to support the MPTT in developing a sectoral strategy, among others, looking at how to expand e-government and digital skills. The team will ensure that this strategy proposes concrete steps on how to bridge gender gap in financial and digital access. The same principle will be applied with respect to the development of a strategy for ID rollout (more on this in the following paragraphs).

Digital ID Enrollment

11. **The creation of a new foundational digital ID and progressive movement toward universal coverage will help bridge the ID gender gap.** The following strategies will be employed to actively enhance female enrollment, in connection with the planned ID rollout:

(a) **Targeted citizen engagement campaigns** related to the ID registration should feature messaging that is compelling to women and highlight the concrete benefits of ID ownership for women. Local women's charities and community organizations could be leveraged to help deliver this message to local communities and could also be designated as local registration partners, allowing women to register through organizations they already know and trust.[104]

(b) **Ensure the involvement of banks, MTOs, and MNOs**, who have access to more female users of critical financial services covering remittances and mobile money. ID enrollment will initially be targeting users of financial services. However, only working with banks could introduce a gender bias, given current bank account ownership figures among women.

(c) **All-female registration units** will help overcome social/cultural/religious barriers to women's registration, creating a more inclusive environment for registration. The use of mobile registration units was successfully used in Pakistan to help increase women's ID registration rates.

[102] Based on World Bank consultation with Somali financial service providers.
[103] The MoCI has adopted a conscientious strategy, which has yielded an increase in women seeking trade licenses, microcredit, and technical support from the ministry. http://www.tradeforum.org/article/Women-and-trade-in-Somaliland/.
[104] This strategy has been successfully employed by development partners such as the WFP. In fact, many local NGOs have already been trained in biometric registration.

(d) **A higher enrollment reward for women** could be applied, if a pay-per-registration approach is used for registration, that is, where enrollment partners receive a fixed fee after each successful registration. A higher registration fee reward for women could incentivize the registration of women.[105]

(e) **A direct (cash-based) incentive** could also be offered to women, if they obtain a digital ID card.[106] The Government could, for example, partner with certain businesses or an aid organization to offer a discount to women on certain products or access to additional services, upon registering and showing their digital ID card.

Access to Financial Services

12. **The program will support the CBS in undertaking additional surveys to produce data, diagnostics, and an evidence base to inform policy development and sequencing of a comprehensive package of actions that are prioritized and resourced to promote the uptake and use of a broad range of financial services by women.** The project also plans to convene a series of gender-themed workshops, targeting financial service providers, with the view of enhancing their advisory services, product range, and outreach strategies to increase their female client base. At a foundational level, the workshops will help sensitize both Government officials and members of the private sector to the benefit of increasing their female client base and women's wider contribution to socioeconomic development. The workshops will also seek to highlight barriers facing female entrepreneurs, across a variety of sectors. By inviting female business associations, women will be given the opportunity to inform business strategy and the development of tailored services.

13. **By supporting the repositioning of Government and humanitarian actors as central role players in fostering digital finance development in Somalia and demanding low-cost interoperable retail payment services, the project will also encourage women's access to Government and humanitarian services.** Linking these services to the digital ID enrollment will also serve as a reinforcing strategy to encourage women to enroll.

MSME Financing Facility

14. **By introducing target quotas for lending to women, through the MSME Financing Facility, the project will actively seek to encourage participating banks and non-bank financial institutions to increase women's access to finance.** Participating banks will be required to demonstrate capability in reaching out to women and female-owned MSMEs as an integral element of the commercial strategy, thereby ensuring effective application of the quotas of the lending pipeline. In cases where it is determined that a prospective participant bank would need to develop the skills of the staff on MSME techniques targeting women and female-owned MSMEs, IFC's FIDEP (ID: 602159) will be leveraged to help banks and non-bank financial institutions develop enterprise capability in these focus markets.

[105] However, this needs to be applied carefully, as it may also create perverse incentives for enrollment partners to falsely code registrants as women at the time of enrollment.
[106] This would need to be implemented in a manner that does not place any additional financial burden on public authorities.

Community Engagement: Feedback and Grievance Mechanisms

15. **Finally, the project will ensure that all feedback and grievance mechanisms in place are accessible to women.** By employing voice-based messaging services and call centers, current gender gaps in literacy will not adversely affect women's ability to influence the project. Additionally, mechanisms to enable ethical, confidential, and safe reporting of and response to GBV incidence will be integrated into GRM design.

C. Indicators and Targets

Activity	Indicator	Target
Component 1		
Supporting sector strategies that help address gender barriers	Gender component integrated	Yes
Developing a strategy for ID rollout that will boost female enrollment	Gender component integrated	Yes
Convene the CBS conference promoting uptake and use of a broad range of financial services tailored for women	Conference convened Number of participants at the CBS conference	Yes 100
Component 2		
Supporting female ID enrollment	% share of women enrolled	50%
MSME Financing Facility eligibility criteria includes assessment of PFI outreach strategy to women	Gender component integrated	Yes
Encouraging PFIs to (a) develop tailored financial products for women, (b) improve their outreach strategy to women, and (c) expand their advisory services to women-led MSMEs	% share of transaction accounts owned by women Number of FIDPs tailored for outreach strategy to women Number of financial products developed by PFIs tailored to women	50% 3 3
Introducing a quota for lending to women-led MSMEs under the MSME Financing Facility	% value of loans to women-led MSMEs supported by PFIs	30%

ANNEX 6: DIGITAL ID and MSME FINANCING FACILITY RISKS ASSESSMENT

Key Risks and Mitigation Measures for the Proposed Digital ID Activities

1. Identification systems—particularly digital ones—have transformational potential for development. However, they also create a number of challenges and risks, which need to be particularly and carefully addressed when systems are implemented in fragile and conflict-affected contexts, as is the case in Somalia. The Principles of Identification for Sustainable Development, endorsed by the World Bank Group and 23 other organizations, including UN agencies, MDBs, and private sector entities, provide a guiding framework for the project on how to maximize the benefits of digital identification systems for development while mitigating the risks. The design and implementation strategy for the digital ID component of the project will thus be closely aligned with the principles and will follow additional guidance on international good practices for ensuring inclusion, data protection, privacy, and sustainability from the World Bank's ID4D Initiative.

2. Although there are a number of risks associated with the implementation of digital ID systems, they can also play a risk mitigating role in the financial sector and the administration of public programs.

Table 6.1. Risks and Mitigation Measures

Key Risks	Mitigation Measures
Data misuse/ privacy Any system that collects personal data carries an inherent risk to privacy and that the data will be misused. Misuse may take a number of forms: data could be used to track the activities of system users, discriminate against individuals based on (sensitive) personal data collected, or commit identity fraud. Information could be shared with (unauthorized) third parties for commercial advantage.	The project is taking a multipronged approach, leveraging both legal and regulatory instruments as well as privacy-by-design techniques, to reduce the risk for misuse and to ensure that the impact of any potential unauthorized access or data breach on individual well-being would be minimized. **Pre-effectiveness:** To mitigate risks associated with slow pace of adoption of legislation, FGS delivered policy commitments '**Policy Letter'** dated January 22, 2019, which will be complemented by a more formal policy statement regarding its digital ID system, including data protection, at effectiveness. The policy commitments in the letter demonstrate alignment of the proposed ID system with the principles and include a strong commitment to data protection and privacy, cybersecurity, and privacy safeguards. **Post-effectiveness/project activities:** The first project activity under Subcomponent 1.4 will focus on the elaboration and adoption of a **comprehensive legal and regulatory framework** for the proposed digital ID system, including provisions to safeguard data privacy, security, and user rights (for example, defining clear conditions and limitations for data access, storage, and sharing). Cognizant of the FGS' limited enforcement capacity, in addition to legal and regulatory safeguards, the project also seeks to mitigate risks to privacy/data misuse **through trust- and privacy-enhancing institutional and governance arrangements** for the ID Authority as well as through the use of **'privacy-by- design' features** in the design

Key Risks	Mitigation Measures
	and implementation of the ID system. By supporting the **establishment of a dedicated ID Authority** that is institutionally, legally, and financially independent, the project seeks to mitigate the risk of undue political interference in the operations of the digital ID system and ensure that it can serve as a platform for the delivery of multiple services across the public and private sectors. Fostering **inclusive governance arrangements**, such as including representatives of users and a wide range of stakeholders from both the private and public sectors on the ID Authority's board and other supervisory or advisory bodies, can also help ensure that the ID system remains responsive to user needs and concerns. Strengthening the technical and administrative capacity of the ID Authority staff will also be critical to ensure that privacy-enhancing technical solutions and data protection measures are effectively implemented. **Privacy-by-design features** will be integrated in the proposed digital ID system, including • Minimal data collection (for example, no data collected on religion, clan affiliation, or economic status) to reduce the risk of discrimination and profiling; • Issuance of random ID numbers that do not reveal any information about their holder; and • Minimal data sharing for authentication (for example, only yes/no response to queries). The project will also support the implementation of **appropriate project level GRMs** to facilitate the early reporting of and rapid response to any misuse of data.
Pre-project contracting of NADRA for the delivery of technical components Financed by a grant from the Government of Pakistan, FGS has contracted Pakistan's NADRA to deliver the technical components (software and hardware) of the digital ID system, including maintenance and support for one year, and to provide skill and knowledge transfers. The contract, signed in May 2018, represents a value of US$10.5 million. There are two main risks associated with this existing contract: • **Risk that the promised technical components and assistance will not materialize** if the Government of Pakistan does not continue to finance NADRA's activities	**To address the risk of non-delivery** In case the financing from the Pakistani government for NADRA's delivery of technical components and TA does not materialize, additional donor financing would need to be sought for the digital ID system. Subcomponent 1.4, which will support a robust ID enabling environment, including the adoption of a comprehensive legal framework and establishment of a competent and well-governed ID Authority, could still go ahead and, by mitigating reputational and implementation risks, would likely make it easier to secure additional donor financing for the project. During discussions with donors as part of the project preparation, all recognized the pressing need for the digital ID system and its transformational development potential. If needed, the World Bank could play a convening role, leveraging its long-standing engagement with the donor community in Somalia. **To address the risk of suboptimal technical features** The completion of the **Policy (document)** by the FGS, which is expected to reflect the policy commitments, communicated in the policy letter from the Prime Minister on January 22, 2019, will help guide discussions between the FGS and NADRA on the specifications and

Key Risks	Mitigation Measures
• **Risk of potentially unsuitable and/or unfavorable features to be coded into the system** delivered by NADRA, if components are delivered/deployed before a clear policy framework for the ID system has been developed and/or without sufficient consultation with Somali authorities	features of the system and ensure that it reflects global good practices. The task team will continue to engage with FGS counterparts to deliberate on and understand the FGS position on key system features and objectives before the technical components of the system are implemented. In addition, the Somali authorities are finalizing TORs to set up a **TTWG to bring together FGS, NADRA, and the World Bank Group** to provide ongoing technical advice and review the ID system's technical components, which are to be implemented by NADRA. To further mitigate the risk of adopting suboptimal technical solutions, the project will finance an **in-depth assessment of technical components**, with a particular emphasis on mitigating risks to privacy and data integrity, preventing vendor lock-in, and promoting interoperability with existing and planned registries.
Low coverage/exclusion risk Enrolling a 'critical mass' of people early on (within a couple of years of implementation) is often instrumental for the long-term success of identification systems. For this reason, the project aims to support the enrollment and issuance of unique ID credentials to 1 million Somali residents and citizens. At the same time, the project seeks to ensure that women and vulnerable populations are well represented among the first 1 million enrollees and ensure that the system is designed and implemented in a way that it minimizes barriers to registration and remains accessible to all. There are two main risks related to enrollment: • **No demand for ID overall**: risk of not reaching 1 million target • **Exclusion** of women, remote, vulnerable, and marginalized populations	The team is working with the FGS to minimize barriers to enrollment and facilitate access to the system to women and vulnerable and marginalized populations through multiple channels. **Clear communication on the benefits of ID.** The project will finance the elaboration and implementation of an **inclusive outreach/communication strategy**, including elements targeted at women and vulnerable populations, to raise awareness about the registration process and its benefits. Improved and more secure access to financial and other services, greater freedom of movement, and greater potential for formal employment opportunities are among the possible benefits to be highlighted. In addition, experiences from other countries show that **people value an official proof of identity for a diverse set of reasons** and will take the time to obtain one even if there is no immediate monetary or other benefit associated with it. **Incentives for the use of the system.** Linking the unique IDs to the opening of transaction accounts, applications for credit, and access to other financial, mobile, and public services will help incentivize enrollment. Experiences from other countries show that linking IDs to SIM-card registration or to the receipt of government assistance has also greatly helped boost enrollment. It will, however, be important that sufficient time and opportunities are provided for all to obtain an ID before it is mandated for any critical service or transaction. Authorities have indicated that once sufficient coverage is reached, the new unique IDs will be linked to an ever-growing number of services and transactions, starting with financial services. **Free (no charge) registration/ID issuance.** Providing the ID for free will help mitigate the risk of exclusion of the poor and can incentivize enrollment for all. FGS commitments to providing registration and ID credentials free of charge are being sought through the Policy Letter, Policy (document), and subsequent legal and regulatory framework. **Minimal documentary requirements for registration.** Given that the majority of Somalia's population lacks official identity documents,

Key Risks	Mitigation Measures
	minimizing documentary requirements for enrollment and offering flexible alternatives (for example, witnesses/ introducers) will be important to ensure the accessibility of the system. Commitments to minimal and flexible identity proofing requirements at the time of enrollment are being sought through the Policy Letter, Policy (document), and subsequent legal and regulatory framework. The planned project activities include the preparation of a **Social Management Plan** to address risks of exclusion and facilitate the adoption of registration and identification processes that minimize barriers to access for all. **'Ecosystem' (multipartner) enrollment strategy.** The FGS, with support from the project team, has been engaging with the private sector and NGOs to explore the feasibility of these entities to serve as registration/ID service partners under an 'ecosystem' approach. This would help increase enrollment opportunities to more remote areas and, by enabling people to interact with entities they are already familiar with on matters related to identification, could help build trust in the digital ID system. **Robust GRMs.** The project will also support the implementation of robust GRMs to facilitate the reporting and rapid resolution of any instances of discrimination and other difficulties with enrollment and the receipt and use of the ID credentials issued.
Financial sustainability risk A critical challenge for the ID system will be to develop a business model and to identify long-term sources of financing without compromising accessibility for all.	The project will support the **development of a robust business model** that will enable the continued operation of the ID system beyond project completion. A number of revenue-raising options, including the **possibility to charge authentication fees for private sector service users** and to **charge for premium processing** (for example, expedited issuance of ID documents) have already been communicated to the authorities. It may also be possible for more 'premium' ID services, such as passport issuance or driver's license issuance, to **cross-subsidize the digital ID program** (for example, a part of the ID Authority's budget is financed from fees collected for passport issuance). The team will continue the dialogue with the FGS to ensure that the digital ID program is financially and technologically sustainable without compromising its accessibility to all.

Key Risks	Mitigation Measures
Security risk Extremist groups may consider the proposed ID system a threat to their activities and, as a result, may target ID registration points and/or may threaten or inflict violence on individuals holding a government-issued ID.	To mitigate the security risk, the FGS will continue to **emphasize financial access** and use of mobile money, banks, and remittance services as the entry point for the digital ID activities. There is a broad consensus about the need to **depoliticize the initiative**, including delinking it from voter registration and security-related activities. The project design also incorporates **continuous citizen engagement** activities through outreach and dialogue to strengthen the narrative around the digital ID system as an enabler for financial access and development, including for the most vulnerable groups of society.

Key Risks and Mitigation Measures for MSME Financing Facility

3. Setting up a sustainable entity to manage the line of credit will require mitigation of risks at entry and during implementation. The inadequate capacity of the client warrants frontloading safeguards guaranteeing institutional integrity of the MSME Financing Facility with robust and transparent governance structures. This includes mitigation measures such as developing a comprehensive charter that builds on the policy commitment made by the Government and communicated through a letter from the Prime Minister on January 22, 2019. Furthermore, the design and implementation of the MSME Financing Facility will thus be closely aligned with the policy commitments and other key risks identified as follows:

Table 6.2. Key Risks and Mitigation Measures for MSME Financing Facility

Key Risks	Mitigation Measures
Crowding-out investment private capital Setting up the MSME Financing Facility	**Pre-effectiveness:** To mitigate risks associated with crowding-out private capital, the FGS will create a Somali entity with a commercial orientation that can act as a platform to crowd-in additional investments of private capital from international sources and potentially future engagement by like-minded DFIs. The articles of incorporation or charter of the MSME Financing Facility will confirm that initial capitalization will be achieved through use of public funding from IDA PACG but subsequently opening the entity to sequential private sector investing and shareholding through additional calls for capital investment. **Post-effectiveness/project activities:** Overtime, the FGS may progressively convert the initial loan to the entity into equity (ordinary shares with voting rights) to form part of the start-up capital of the MSME Financing Facility. The remaining financing under Subcomponent 2.1 may be converted into subordinated debt or non-voting preference shares, thereby avoiding crowding-out potential private sector investors using blended finance tools.

Key Risks	Mitigation Measures
	The conversion rates will be linked to performance benchmarks for the MSME Financing Facility agreed with the FGS covering aspects such as private sector representation on the governance structures of the entity, crowding-in of private capital and DFIs, portfolio assets quality (non-performing loans and recoveries), and outreach while creating opportunity for private capital risk-sharing and blended finance in targeted economic sectors and final beneficiaries such as energy and livestock as well as women and female-owned enterprises.
Delays in setting up the MSME Financing Facility and changes in the operating environment Slow disbursement by MSME Financing Facility Weak PFI capacity	**Pre-effectiveness:** To mitigate risks associated with delays in setting up the MSME Financing Facility, the FGS delivered policy commitments on January 22, 2019, setting out a stable policy framework and a predictable operating environment for setting up the MSME Financing Facility. Combination of the World Bank and IFC policies and standards will be reflected in the design the MSME Financing Facility MSME Subproject Manual to ensure flexibility. The MSME Financing Facility will follow private sector governance principles. The MSME Financing Facility will adopt commercial and business principles and retain objectivity, operational autonomy, and accountability in the delivery of services. **Post-effectiveness:** A legal entity, together with its board of directors and management, will be established in terms of national legislation. Changes of the governance arrangements will be made in consultation with IDA. Formal setup of the entity in accordance with national legislation will be a condition of effectiveness. PFI capacity strengthened through TA by IFC FIDEP (ID: 602159).
Institutional integrity of the MSME Financing Facility and AML/CFT risks	**Pre-effectiveness:** To protect the institutional integrity of the entity, the MSME Financing Facility will operate in compliance with IDA reviewed appraisal procedures and standards stipulated in the IDA Grant Agreement and Project Agreement including stipulations related to anti-corruption and AMF/CFT. The MSME Financing Facility's appraisal procedures and standards will be elaborated in an MSME Subproject Manual developed with World Bank assistance to appraise all projects seeking funding. The manual will also embed IFC investment standards. The key design element will ensure (a) access to finance by MSMEs in underserved and underfunded economic segments based on risks of the underlying sub-projects and (b) clarity, transparency, and administrative efficiency in MSME Financing Facility appraisal operations. Risk factors will include environmental assessment such

Key Risks	Mitigation Measures
	as social, environmental, technological, economic, regulatory, political, and geographical risks and opportunities and with due consideration of the indicators which measure sustainable development issues. **Post-effectiveness:** The MSME Subproject Manual will be updated from time to time based on experience in the field and in consultation with IDA. The apex pricing mechanism and retail on-lending rates will be marked to market. Any subsidy component in pricing will be explicit and transparent with a view to gradually being phased out as the underlying market failure is addressed. PFIs will be subject to fit and proper tests, CBS supervision, and adequate AML/CFT reporting and controls as per FATF standards. Operationalization of the FGS Business Registry to facilitate obtaining MSMEs basic information (see FATF interpretative note to recommendation 24). PFI to commit to put in place an effective and multilayered due diligence process on the firms and individuals accessing the MSME Financing Facility. PFIs will undergo stringent due diligence of AML/CFT programs and capacity building to ensure an understanding of AML/CFT risks and controls and ensure proper reporting and supervision, including through compliance with United Nations Security Council resolutions relating to the prevention and suppression of terrorism and terrorist financing. Digital ID is going to be a further instrument to verify those accessing the MSME Financing Facility.

ANNEX 7: TEAM LIST

Name	Title	Role
Thilasoni Benjamin Musuku	Senior Financial Sector Specialist	Team Leader (ADM Responsible)
Axel Rifon Perez	Young Professional	Team Leader
Francis Akolu Muthuiya	Senior Procurement Specialist	Procurement Specialist
Leonard Mutuku Matheka	FM Specialist	FM Specialist
Tracy Hart	Senior Environmental Specialist	Environmental Specialist
Harub Ahmed Harub	Consultant	Social Specialist
Asta Bareisaite	Private Sector Specialist	Team Member
Fuad Mohamed Sharif	Consultant	Team Member
Anna Zita Metz	Consultant	Team Member
Margrit Nzuki	Senior Investment Officer	Team Member
Patricia Mwangi	Senior Operations Officer	Team Member
George Ferreira Da Silva	Finance Officer	Team Member
Hadija Rahama Diba Kamayo	Financial Sector Specialist	Team Member
Isabella Maria Linnea Hayward	Consultant	Team Member
Mahjabeen N. Haji	Consultant	Team Member
Maria Kristina Nordwall Liungman	Senior Economist	Team Member
Patrick Thaddayos Balla	Energy Specialist	Team Member
Rokuhey Fordyce Fukui	Consultant	Team Member
Sheila Lucrecia Francisco Pene Neves	Finance Analyst	Team Member
Sonia Plaza	Senior Economist	Team Member
Timothy John Charles Kelly	Lead ICT Policy Specialist	Team Member
Yara Quiros Soto	Senior Financial Sector Specialist	Team Member
Kamal Siblini	Senior Monitoring & Evaluation Specialist	Team Member
Taneem Ahad	Private Sector Specialist	Team Member
Elizabeth Mumbi Kibaki	Consultant	Team Member
Aisha Abdulaziz Mahmoud	Consultant	Team Member
Shiny Jaison	Team Assistant	Team Assistant
Salome Awuor Aganda	Team Assistant	Team Assistant

ANNEX 8: MAP OF SOMALIA