



COMMENTARY REPORT

2

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**THE DEVELOPMENT
OF THE BANKING
SECTOR IN SOMALIA.**

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INTRODUCTION

The banking sector in Somalia has faced challenges and progress due to political instability and conflict, which have hindered its growth and stability. However, recent efforts have been made to rebuild and modernize the sector, leading to some positive developments. Historically, Somalia had a well-functioning banking sector before the civil war in 1991. The **Central Bank of Somalia**, established in 1960, played a crucial role in regulating and supervising the banking industry. However, the civil war severely disrupted the banking sector, leading to the closure of most banks and the collapse of the central bank. As a result, informal money transfer systems, known as hawalas, emerged as the primary means of financial transactions (Ahmed, A. A., & Ahmed, N., 2017).

The Somali government and international partners have taken steps to establish a new regulatory framework and reestablish the **Central Bank of Somalia**, strengthening its capacity in terms of regulation, supervision, and monetary policy implementation. Additionally, an influx of foreign banks has entered the Somali market, contributing to the expansion of banking services and introducing new technologies and products (World Bank, 2016, Ahmed, A. A., & Ahmed, N., 2017).). Despite these positive developments, challenges remain, such as limited access to financial services, weak infrastructure, and a lack of trust in formal financial institutions. The ongoing security concerns pose a risk to the stability and growth of the banking sector (World Bank., 2020). Nevertheless, the efforts to rebuild and develop the banking sector demonstrate the commitment of the Somali government and international partners to improve financial inclusion and support economic development (Ahmed, A., 2018).

1.2. THE SCOPE OF THE REPORT

The scope and purpose of this report titled “Development of the Banking Sector in Somalia” would be to provide a comprehensive overview of the progress, challenges, and initiatives related to the growth and transformation of the banking sector in Somalia.

1.3. THE PURPOSE OF THE REPORT

The purpose of this report is to inform readers about the current state of the banking sector in Somalia and its potential for further growth and stability. It would highlight the importance of a well-functioning banking sector for economic development and financial inclusion in the country. The article will also discuss the challenges and risks that need to be addressed to ensure the sustainable development of the sector.

THE PROGRESS OF THE BANKING SECTOR IN SOMALIA

Over the years, the development of the banking sector in Somalia has been marked by both challenges and progress. After the collapse of the central bank and the disruption caused by the civil war, efforts have been made to rebuild and modernize the sector.

- The banking sector in Somalia has experienced both challenges and progress over the years. Following the collapse of the central bank and the civil war, efforts have been made to rebuild and modernize the sector. Since the reestablishment of the Central Bank of Somalia in 2009, there have been notable advancements in the regulatory framework and supervision of the banking sector. The World Bank has been working to strengthen its regulatory capacity to ensure the stability and soundness of financial institutions (Ahmed & Ahmed, 2017).
- Foreign banks have also entered the Somali market, attracted by the country's potential for economic growth. Their entry has contributed to the expansion of banking services, introduction of new technologies, and increased competition. Technological advancements, such as mobile banking and digital payment systems, have played a significant role in the development of the banking sector in Somalia (World Bank, 2020).
- Efforts to promote financial inclusion and expand access to banking services have been made, such as the establishment of microfinance institutions and financial literacy programs (World Bank, 2020). However, challenges such as limited access, weak infrastructure, and a lack of trust in formal financial institutions continue to hinder the sector's development (Ahmed & Ahmed, 2017).

THE INITIATIVES RELATED TO THE BANKING SECTOR DEVELOPMENT IN SOMALIA

The development of the banking sector in Somalia has been a complex and gradual process, marked by both challenges and progress. The key initiatives include:

- Rebuilding the Regulatory Framework. Somalia has been strengthening regulatory capacity, encouraging foreign bank entry, embracing technology and innovation, promoting financial inclusion, addressing security concerns, and establishing the Somalia Banking Association (SBA). The Central Bank of Somalia was reestablished in 2009 to restore confidence in the financial system and provide a stable foundation for the banking sector. The SBA has been working to enhance its ability to supervise banks and enforce prudential regulations, building necessary skills and expertise within the central bank. Encouraging foreign bank entry has contributed to the expansion of banking services and the introduction of new products and technologies (Ahmed & Ahmed, 2017).
- Technological advancements. In Somalia technological advancements have been adopted to overcome infrastructure challenges and improve access to financial services, with mobile banking and digital payment systems becoming popular. Efforts have been made to promote financial inclusion and expand access to banking services in , including the establishment of microfinance institutions and the implementation of financial literacy programs to educate the population about the benefits and importance of formal financial services (World Bank, 2020)

- Additionally, the Somali Bank of Somalia (SBA) is a key player in fostering collaboration among banks in Somalia. It facilitates meetings to address common challenges, share best practices, and explore cooperation opportunities, enhancing the stability and efficiency of the banking sector. The SBA represents the interests of its member banks and advocates for a supportive regulatory environment, policies, and reforms. It also organizes training programs and seminars to improve the sector's competence and professionalism (Central Bank of Somalia, 2016).

In conclusion, the development of the banking sector in Somalia has been shaped by several key initiatives, including rebuilding the Regulatory Framework, strengthening regulatory capacity, encouraging foreign bank entry, promoting financial inclusion, and addressing security concerns.

THE CHALLENGES HINDERING THE DEVELOPMENT OF BANKING SECTOR IN SOMALIA

- The banking sector in Somalia is facing several challenges, including prolonged conflict, a weak regulatory framework, a lack of infrastructure, and limited access to financial services. The ongoing conflict and political instability have led to the destruction of bank branches, loss of customer confidence, and disruption of banking operations (Mumin, A. A., 2018, Ahmed and Ahmed 2016). The lack of a robust regulatory framework also hinders effective governance, risk management, and consumer protection mechanisms, creating opportunities for money laundering and financing terrorism.
- The limited physical and technological infrastructure in Somalia also poses challenges, with the absence of reliable power supply, internet connectivity, and basic banking infrastructure hindering the provision of efficient and secure financial services (Ahmed, A. M., 2020). Additionally, a significant portion of the Somali population lacks access to formal financial services due to geographical barriers, high costs, and low financial literacy (Isse, H. H., & Abdi, I. B., 2017).

In conclusion, addressing these challenges is crucial for the sector's growth and the overall economic development of Somalia.

RECOMMENDATIONS

To accelerate the development of the banking sector in Somalia, several recommendations can be made and they include the following:

1. Establish a robust and transparent regulatory framework to promote stability, accountability, and compliance.
2. Invest in financial education programs to increase awareness of banking services and their benefits among the general population.
3. Encourage innovation and technology adoption by embracing digital banking solutions, such as mobile banking and online payment systems.
4. Foster financial inclusion by expanding access to banking services for underserved populations, such as rural communities and women.

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5. Improve the technological infrastructure of banks to support efficient and secure financial transactions.
6. Promote collaboration between Somali banks and international financial institutions to facilitate knowledge transfer and access to capital.

CONCLUSION

The banking sector in Somalia has seen significant growth, with new banks and financial services expanding across the country. This has facilitated economic growth, promoted financial inclusion, and boosted investment opportunities. However, challenges such as limited access to financial services in rural areas, inadequate infrastructure, and a lack of skilled human resources persist. Additionally, concerns about money laundering, terrorism financing, and weak governance practices need to be addressed through enhanced regulatory oversight. To ensure sustainable development, the government, regulatory authorities, and banking institutions must work together to address these issues, including investing in infrastructure, promoting financial literacy, and developing a robust regulatory framework. Collaboration with international partners can also provide valuable support in capacity building and technical assistance.

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