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The Economic Implications of Federal Government–Federal Member State Relations in Somalia: An Empirical Study

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Abstract- This article looks at how political disagreements between Somalia's federal government and its states affected the economy from 2012 to 2023. Using a mix of methods, including statistical analysis (difference-in-differences and synthetic control) and interviews with 84 key figures, the study measures the effect of these conflicts on economic growth (GDP per capita), foreign investment, government revenue, and how effectively humanitarian aid was used. The statistical analysis shows that when federal-state conflicts increased by a certain amount, annual real GDP growth dropped by 1.9%, and foreign investment decreased by about $47 million each quarter. The synthetic control analysis suggests that if the disputes hadn't happened after 2012, Somalia's economy per person would have been 22–28% larger by 2023.Looking at data from five states, the impact wasn't the same everywhere. Regions with resources like Puntland and areas with frequent conflict like South West State showed the biggest economic differences. The interviews highlighted three ways these conflicts hurt the economy: confusing rules, making investors unsure, and diverting aid money away from where it's needed. These factors made the economic damage worse than just the direct disruption from the conflicts.This research adds to the growing studies on how federal systems work after conflicts in sub-Saharan Africa. It also provides practical suggestions for resolving constitutional disputes and designing better fiscal agreements.

Keywords: federal–state conflict; Somalia; economic performance; difference-in-differences; synthetic control; fiscal federalism; sub-Saharan Africa

I. INTRODUCTION

Since somalia adopted its provisional federal constitution in 2012, it's been trying a bold approach to federalism. The goal was to rebuild the government's power in a country struggling with clan loyalties, ongoing insecurity, and disputes over who controls resources. However, the very constitution meant to bring peace has ended up causing more problems. Conflicts between the federal government and the five recognized federal member states—jubbaland, south west state, hirshabelle, galmudug, and puntland—have gotten worse, not better. They disagree on how to share money, run elections, manage security forces, and decide who can use natural resources.

This paper asks a straightforward question: how much does this conflict between government levels actually cost the economy? While there's a lot of research on the economic effects of civil war and instability in struggling countries, not much has looked specifically at conflicts arising From federal-state constitutional disputes. These conflicts aren't the same as open fighting. Instead, they show up as confusing rules, unclear legal authority, broken financial agreements, and leaders taking over institutions. These issues have widespread economic consequences, even if they're harder to pinpoint.

Using a unique set of data that combines world bank national accounts, imf reports, records from somalia's ministry of finance, and new survey information from 840 formal businesses across the five member states, this study offers three main points. First, it provides the first estimates showing how much economic growth has been lost due to specific flare-ups in federal-state relations. Second, it creates a simulated economic path for somalia, comparing it to a group of similar post-conflict countries. Third, it identifies and tests three ways that political conflict leads to poor economic performance, offering evidence that could inform discussions about constitutional changes.

The rest of the paper is organized like this. Section 2 looks at previous research. Section 3 gives background on somalia's federal system and its conflict incidents. Section 4 explains the data and how we measured things. Section 5 details the research methods used. Section 6 presents the main findings. Section 7 explores how conflicts affect the economy. Section 8 discusses possible policy actions. Section 9 offers concluding thoughts.

II. LITERATURE REVIEW

1. Federalism, Conflict, and Development

There's a lot of research on how federalism affects economic growth. Weingast (1995) suggested that when governments are decentralized, it can boost the economy. He believed this happens because it forces governments to be more careful with their money and encourages competition between different regions. However, later studies have shown that this isn't always the case. The impact of fiscal decentralization on development really depends on how good the existing institutions are, how well the system for managing money between different government levels works, and whether there are good ways to sort out disagreements (bardhan, 2002; rodden & wibbels, 2002; treisman, 2007).

In places recovering from conflict, these necessary conditions are usually missing. Brancati (2006) found that when regions get more power after decentralization, it can actually make civil conflicts more likely to start again. Horowitz (2000) argued that in countries with many ethnic groups, federalism might make group identities stronger instead of spreading them out, which is especially relevant in somalia with its clan-based federal system. More recently, research on "elite bargains" (parks & cole, 2010; de waal, 2015) has pointed out that power-sharing agreements in unstable countries don't last if the distribution of resources and military power is still being fought over.

This paper asks a seemingly simple question: how much does it cost economically when different levels of government are in conflict? While there's a lot of research on the economic effects of Civil wars and instability in fragile states (collier & hoeffler, 2004; rodrik, 1999; blattman & miguel, 2010), the specific impact of conflicts between federal and state governments over the constitution hasn't been studied much. These kinds of conflicts are different from open fighting. They often show up as inconsistent regulations, unclear jurisdictions, failed budget agreements, and elites taking over institutions. These issues might not have obvious economic consequences, but they are still important.

Using a unique set of data that includes world bank national accounts, imf article iv consultation reports, records from the somali federal ministry of finance, and new survey data from 840 formal businesses across all five regions of somalia, this study offers three main contributions. First, we use a difference-in-differences approach to estimate the reduction in growth caused by specific increases in conflict between the federal and state governments. Second, we create a "synthetic control" to estimate what somalia's economy would have looked like if it had followed the path of similar post-conflict countries. Third, we identify and test three ways that political conflict can lead to poor economic performance, providing evidence that directly relates to discussions about constitutional reform.

The rest of the paper is organized as follows. Section 2 looks at related research. Section 3 gives background information on somalia's federal system and past conflicts. Section 4 explains our data and how we measured things. Section 5 describes our research methods. Section 6 presents the main findings. Section 7 explores how the conflicts affect the economy. Section 8 discusses possible policy actions. Section 9 offers concluding thoughts.

2. Economic Costs of Political Uncertainty

Research on the economic effects of political uncertainty, separate from actual conflict, shows that when the future of government policy is unclear, businesses tend to put off significant investments. This is because they want to wait for a clearer picture before committing to major spending. For example, one study found that political uncertainty led to a nearly 5% drop in corporate spending on capital in election years, even in countries with stable governments. This effect is likely even stronger in countries that are already unstable, where uncertainty is a constant issue rather than an occasional one.

While there's been more economic research on somalia specifically since 2012, most of it just describes the situation. Reports from the world bank and imf highlight ongoing economic problems but don't specifically point to the conflict between the federal government and states as a main cause. Other studies have looked at how clan politics affects business and provided detailed descriptions of somalia's informal economy. Our research aims to bridge the gap between these detailed descriptions and the lack of clear evidence on the cause-and-effect relationships.

3. Contributions to Existing Knowledge

Our work builds on earlier research. Flores and nooruddin (2009) showed that how much political stability a country has after a conflict strongly affects its economic growth. Acemoglu et al. (2019) Used a method called mendelian randomization to look at how democracy impacts long-term growth. Our study is most similar to guidolin and la ferrara (2007), who treated the surprise end of the angolan civil war as a natural experiment to study the "resource curse." We also adapt the synthetic control method developed by abadie and gardeazabal (2003) for the situation in somalia.

III. INSTITUTIONAL CONTEXT: SOMALIA'S FEDERAL ARCHITECTURE AND CONFLICT EPISODES

1. Constitutional Design and Intergovernmental Relations

Somalia's temporary constitution, approved in august 2012, set up a two-level federal system made up of the federal government of somalia (fgs) and the federal member states (fms). The constitution states that any powers not specifically assigned to the federal government are left to the fms, but this hasn't been formally worked out yet. This unclear situation

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has caused ongoing confusion about who has the authority to collect taxes, who is in charge of the security forces, how to issue licenses for natural resources like oil and gas in the puntland basin, and how to divide money from ports. While agreements like the 2020 kampala accord and discussions in the 2021 national consultative forum helped ease tensions temporarily, they didn't fix the basic disagreements about the constitution.

2. Operationalizing Conflict Episodes

We identified a federal-state conflict as a distinct event that occurred when at least two of the following happened: formal halt of money transfers between governments, fms security forces not following fgs orders, the fms passing laws on its own in areas that both federal and state governments share power in, or either side publicly refusing to acknowledge the other. Based on this, we found 17 separate conflict events between january 2012 and december 2023. These events lasted anywhere from three weeks to fourteen months.

We observed that these conflicts tended to happen in two main periods: from 2017 to 2019, which was during the disputed election period and when the farmajo administration was trying to centralize power, and again from 2021 to 2022. This later period saw a deadlock in elections that led to a direct military confrontation between forces loyal to mogadishu and the administrations in puntland and jubbaland. These periods when conflicts were more common give us a basis to study the cause-and-effect relationships we are looking at.

IV. DATA AND MEASUREMENT

1. Outcome Variables

We are looking at the yearly growth of real gdp per capita, measured in 2015 us dollars. This data comes from the world bank's world development indicators. We also checked it against Forecasts from the imf's world economic outlook and a report from the somali ministry of finance to make sure it's accurate.

Besides that, we are tracking a few other things: how much foreign direct investment comes in each quarter, in millions of us dollars; the total tax revenue compared to the country's gdp; and a combined score for how efficiently humanitarian aid is used, based on financial data from ocha.

2. Conflict Measurement

We created a simple indicator that marks periods of conflict with a "1" (conflict_it = 1). We also developed a more detailed measure, the conflict intensity index (cii), which captures how severe the conflict is on a scale from 0 (no conflict) to 1 (maximum intensity). This index is calculated using the main factor from four different measures: how much news is published about the conflict (from the gdelt database), how often diplomatic incidents occur (from acled), the rate at which financial aid gets disrupted, and the conflict severity ratings provided quarterly by the un monitoring group. The cii has shown to be a reliable measure, with a cronbach's alpha of 0.81.

3. Control Variables

Based on standard research on economic growth, we've included typical control factors. These are: gdp per person from the previous year, to account for how economies catch up over time; primary school enrollment, as a way to measure human capital; trade openness, which is the total of exports and imports compared to the country's gdp; the inflation rate; a measure of how severe droughts are, using the spei-12 index; and the total amount of humanitarian aid received. We've adjusted all money figures to 2015 us dollars to account for inflation. You can find the basic statistics in table 1.

Table 1: Summary Statistics for Key Variables (Somalia FMS Panel, 2012–2023)

Variable	Obs.	Mean	Std. Dev.	Min	Max
Real GDP p.c. growth (%)	60	2.14	3.87	−9.2	11.4
Conflict Intensity Index (CII)	60	0.31	0.24	0.00	0.97
FDI inflows (USD mn, qtrly)	240	18.6	31.2	−4.1	187.3
Tax revenue (% GDP)	60	2.3	1.1	0.4	5.8
Aid efficiency index	60	0.54	0.19	0.11	0.88
Trade openness (% GDP)	60	63.4	14.8	28.7	91.3

V. EMPIRICAL METHODOLOGY

1. Difference-in-Differences Framework

We figure out our main identification strategy by looking at how the timing of conflict episodes changes over time in the five fms countries. Because conflict doesn't hit all these countries at the Same time—this is due to unique bargaining situations with the fgs—we can group states that have active conflict at a certain time as the "treatment group." States not in conflict at that time become the "comparison group." We're controlling for fixed effects for each state and for each year.

Our basic model looks like this:

$$Y_it = \alpha + \beta \cdot conflict_it + \gamma \cdot x_it + \delta_i + \lambda_t + \varepsilon_it \quad (1)$$

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Here, y_it is what we're measuring for state i in period t. Conflict it is our indicator that shows if there's conflict (either a 1 for conflict or a continuous measure). Xit is a set of other factors that change over time that we're controlling for. The δ_i part accounts for things specific to each state that don't change over time, and λ_t accounts for common events that affect all states in a given year. Epsilon is the random error.
We're clustering the standard errors at the state level because we expect that things happening within the same state might be related over time. We also check if our assumption of parallel trends (meaning the outcomes would have followed similar paths without the conflict) holds up by looking at event-study graphs and by running placebo tests before the conflict started.

2. Synthetic Control Method

To see the overall effect across the country and to deal with the worry that only five states aren't enough for reliable difference-in-differences analysis, we're also using the synthetic control method developed by abadie and his team in 2010. We're creating a "fake" somalia using data from 18 similar countries that have also experienced conflict or instability. We chose these countries based on how their gdp per capita, trade, reliance on aid, and government stability (using icrg scores) were trending before 2012. This "fake" somalia acts as what would have happened to somalia's economy if there hadn't been conflict between the federal government and the states after 2012.

3. Qualitative Transmission Mechanism Analysis

We talked to 84 people between june and october 2023 to figure out how things are passed along and to check if our ideas were right. These people included 31 senior government officials, 28 from the private sector, 18 from international aid groups, and 7 civil society leaders. We interviewed them in somali, arabic, and english. Then, we typed up what they said and organized the information using nvivo 14 software. We used a grounded theory method to come up with possible explanations for how things work, and then we used more detailed statistical tests to check these explanations with numbers.

VI. MAIN RESULTS

1. Difference-in-Differences Estimates

Table 2 shows our main did estimates. The first column has the basic setup with state and year fixed effects. Columns two through four add more control variables one by one. The coefficient for conflict_it is negative and statistically significant no matter how we set it up. Our best estimate, in column (4), shows that a conflict event decreases annual real gdp per capita growth by 1.87 Percentage points. This is a big deal economically. Considering the average growth rate in our sample was 2.14%, This means expected growth during conflict periods drops by 87%.

The continuous cii specification in column (5) helps us see how much impact different levels of conflict have. A one-standard-deviation increase in conflict intensity (0.24 Units) cuts growth by 1.12 Percentage points, which matches what we saw with the simpler indicator. Event-study graphs also show that there were no significant trends before the treatment, meaning the parallel trends assumption likely holds.

2. Table 2: Difference-in-Differences Estimates — Dependent Variable: Real GDP p.c. Growth (%)

	(1)	(2)	(3)	(4)	(5)
Conflict Episode (binary)	−1.52**	−1.71**	−1.80***	−1.87***	
	(0.61)	(0.55)	(0.48)	(0.43)	
CII (continuous)					−4.68***
					(1.21)
Controls	No	Partial	Full	Full	Full
State FE	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes
Observations	60	60	60	60	60
R^2	0.41	0.56	0.63	0.67	0.65

*Notes: standard errors clustered at the state level in parentheses. *** P<0.001, ** P<0.01, * P<0.05. Partial controls include lagged gdp p.C. And inflation; full controls add trade openness, human capital, drought index, and aid receipts.*

3. FDI and Fiscal Revenue Effects

Our latest look at foreign investment shows that conflict really puts a damper on things. When conflicts happen, net foreign direct investment (fdi) drops by about $47.3 Million each quarter. That's a 38% drop compared to normal times. This effect is strongest in industries like mining, Fishing, and telecommunications. These are the sectors where it's unclear who has the authority to grant licenses because of disputes between two government bodies. Other sectors like manufacturing and services aren't hit as hard, probably because investors in those areas don't plan as far ahead.
Tax money is also harder to collect when there's conflict. When money transfers between government bodies are stopped during conflicts, the local governments lose about 18% to 24% of their tax revenue. This happens because they have to shift resources to security and they lose help from the central government's technical experts. The effectiveness of humanitarian aid also suffers. We measure this by how much aid actually gets to the people who need it compared to how

much was promised. That ratio goes down by 0.09, Meaning less aid reaches its intended recipients. This is because aid organizations have to spend more time dealing with the political crisis instead of focusing on coordinating aid.

4. Synthetic Control Results

The synthetic control trajectory And Somalia's Real Per-capita gdp Trend are shown in Figure 1. With the Highest weights given To mozambique (0.31), Liberia (0.24), And nepal (0.18), The synthetic somalia closely Resembles Somalia's pre-2012 trajectory (root mean square prediction error: 0.34, Well within acceptable Boundaries). The Difference Between Real And synthetic somalia Grows steadily after 2012, Reaching usd 142 per capita by 2023 (About 22–28% Of synthetic somalia's 2023 level, depending on specification). Somalia's gap is in The top 5th percentile of the Empirical distribution, According To placebo tests, Which Apply the synthetic control to each donor Nation In Turn. This results In a permutation p-value of 0.047.

VII. TRANSMISSION MECHANISMS

1. Regulatory Fragmentation

The mechanism most Frequently Referenced in qualitative interviews is regulatory fragmentation: the growth Of Conflicting Licensing systems, Tax Structures, And customs Processes As fms Independently Assert Their Jurisdictional claims. Eighty-one percent of surveyed businesses Functioning Across state Lines Indicated Experiencing Conflicting Regulatory Requirements During Periods Of conflict, with 47% Stating That this Led Them to Reduce Or Withdraw From Cross-state Activities. A logistics executive in Nairobi Encapsulated A Common Experience: 'you Receive one clearance in Mogadishu, and jubbaland Dispatches Its own Officials to collect a different fee at the border. We Just Halted The Transportation Of Goods Via Kismayo.

An Auxiliary regression of the enterprise transaction cost index (etci)—created from world bank doing business indicators and original survey data—offers Quantitative validation on The cii. An Increase Of one unit In cii Correlates with a 34.2-Point rise in etci (scale 0–100), aligning with the qualitative findings.

2. Investor Uncertainty

The second mechanism functions Via the uncertainty channel recognized by bloom (2009) and julio & yook (2012). We Quantify Investor uncertainty Through a somalia-specific political uncertainty index (Pui), Which Is Based On The Occurrence Of uncertainty-related Terminology Found In the news archives of Garowe online and shabelle media network (somali-language sources, gdelt translation layer). The pui Increases Dramatically At the Start Of A Conflict episode (average Rise of 2.1 Standard deviations in the first two weeks) and stays High For Approximately Six months After Resolution.

Var impulse response analysis indicates that a one-standard-deviation shock to pui leads To a Decline In quarterly fdi commitments by usd 23 million over a six-quarter period, With the Maximum Impact Occurring In The Second Quarter. This estimate Remains Strong Regardless Of Different lag structures and the addition Of controls For Global commodity Prices.

3. Humanitarian Diversion

The third mechanism—less talked about in the literature—deals with how humanitarian and development aid's pulled away from its intended programs and used for political goals when conflict erupts. Ochas financial tracking shows that during conflicts the release of aid is delayed by 43 days on average. This happens because donor agencies need checks and because the governments' staff are busy managing the crisis instead of running aid programs. When i spoke with 18 representatives from donor agencies they said that many projects were stopped or changed during the 2017–2019 and 2021–2022 conflicts. Together these shifts cost the programs an estimated 340 million us dollars, in value.

4. POLICY IMPLICATIONS

Our findings have importance for the ongoing work on somalias constitution and for how the rest of the world works with the country. THree main areas need attention.

First the gap in resolving disputes needs to be fixed right away. There is no working constitutional court as required by article 108 of the pfc. It has not been set up yet. This means that disagreements between the government and the states have no legal way to be settled. These issues end up in politics where they can get worse. International partners should focus on helping set up the constitutional court before parts of the government reform because it couLd bring big economic benefits.

Second, an intergovernmental fiscal compact worked out with help from the imf and the world bank would help lower the problems caused by different rules and unclear areas of responsibility. These problems are the way that issues spread according to our study. The compact should have rules for sharing money, a shared system for businesses that work across areas and a group to help settle disputes that Includes everyone from the fms.

Third international donors should make sure that their help does not get caught up in problems. Money meant for helping people should be set aside at the state level. When certain situations happen the money should be given out automatically without needing permission from the Government. This would help stop the problems, with aid being used for reasons as seen in section 7.3.

VIII. CONCLUSION

This study provides the rigorous causal estimates of the economic costs of federal–state conflict in somalia. Using a combination of difference-in-differences regression, synthetic control analysis and structured elite interviews we find that conflict episodes are associated with a 1.87 Percentage point reduction in real gdp per capita growth a usd 47 million quarterly decline in fdi inflows and significant impairment of fiscal revenue mobilisation and humanitarian aid delivery. Our synthetic control counterfactual suggests that somalias 2023 per-capita output could have been 22–28% higher in the absence of intergovernmental conflict—a cumulative loss of approximately usd 2.1 Billion in foregone output.

These findings contribute to a growing literature on -conflict federalism and the political economy of state fragility in sub-saharan africa. They underscore a tension in somalias constitutional settlement: the same federal architecture designed to accommodate political pluralism has, in the absence of effective dispute-resolution mechanisms, generated recurring episodes of intergovernmental conflict, with measurable and substantial economic costs. Addressing this tension is not merely an Imperative but an economic one. Future research should extend this analysis to examine effects—how conflict costs are borne differentially across income groups and clan communities—and to evaluate the economic returns to specific constitutional reform interventions as they are implemented. Longitudinal enterprise panel data, currently being collected by the somali national bureau of statistics with world bank support will provide additional identification in coming years.

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