

Oil in Somalia

Adding Fuel to the Fire?

Dominik Balthasar



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About the Author

Dr. Dominik Balthasar is a development policy fellow with the Heritage Institute. He currently holds a position with the Transatlantic Postdoctoral Fellowship for International Relations and Security, working with Chatham House, the United States Institute of Peace, and the European Union Institute for Security Studies. Dominik's work focuses on issues pertaining to conflict and state fragility, as well as international efforts towards state reconstruction and development, particularly in Somalia. Dominik has taught at the London School of Economics and Political Science and the School of Oriental and African Studies, and has consulted with a number of international development organizations in Somalia and other g7+ countries.

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Executive Summary

- As the latest ‘frontier region’ of hydrocarbon exploration and production in East Africa, Somalia remains not only one of the most promising, but also most challenging potential oil exporting countries. Apart from numerous technical obstacles, including scant infrastructure for transport and processing, Somalia boasts a host of challenges, including political volatility, institutional fragility, physical insecurity, and ambiguous property rights.
- While the specific Somali environment challenges oil producing companies in unique ways, the Somali state itself is challenged in many respects by the development of its hydrocarbon endowments. Not only is Somalia set to struggle with the common effects of the ‘resource curse’, but it will also have to confront a variety of additional challenges that are certain to arise from oil exploration and production in the context of its nascent state-making endeavour.
- One of the most crucial risks Somalia faces with regards to the development of its petroleum resources is that the exploration and exploitation of oil is likely to catalyse an already tense political situation and enhance chances for renewed conflict. The oil factor is likely to spur sub-national demands for an expanded federalism that grants significant autonomy to the respective federal units, which the central government emphatically resists.
- Whether Somalia’s hydrocarbon endowments will ultimately be a boon or bane for its future trajectory depends on a multitude of variables, evading simple projection. What is certain, however, is that great care needs to be taken from all actors involved, if the exploration and exploitation of the fragile country’s hydrocarbon potential is to advance rather than hinder its development.

Introduction

Constituting approximately one third of global energy consumption, oil remains one of the most strategic resources in the global economy and international politics (BP, 2012). Although universal demand for petroleum has continuously escalated in recent years, it is forecast to grow even stronger in the future. At the same time, concerns about increasing global scarcity are on the rise, nurtured by a combination of shrinking oil reserves, and growing demand by industrial powers and emerging economies, as well as global population growth.¹ Coupled with enhanced fears over disruptions from volatile supply bases in the Middle East and increasing oil prices that peaked at US \$145 per barrel in 2008, these trends have prompted oil companies to venture into 'frontier regions'.

One of these frontier regions is East Africa, which has recently experienced a resource bonanza. In 2012, London-based Tullow Oil found commercially viable oil in the north-western Turkana region of Kenya, while another UK-based company, BG Group, announced huge natural gas discoveries in Tanzania. Combined with gas fields off the coast of Mozambique, the latter add up to an estimated 100 trillion cubic feet of gas. In Uganda also, significant hydrocarbon fields have been uncovered, contributing to a 'black gold rush' across the region (see Shepherd, 2013). These developments led to Africa's proven oil and gas reserves increasing by more than 100 and 70 per cent respectively. Thus, even though East Africa's petroleum sector is still in its infancy – indicated by the fact that only some 600 oil wells have been drilled thus far – a new era is dawning.²

Within East Africa, approximately 10 per cent of all wells have been drilled in Somalia (Abiikar, 2012). While exploration in this latest and, in many respects, most extreme hydrocarbon frontier region remains in the fledging stages, estimates put the country's oil reserves as high as 110 billion barrels, placing it at eye-level with Kuwait (United Press International, 2012). Moreover, it is expected that Somalia's offshore territory also contains vast natural gas fields. Determined to join the race for

hydrocarbon production (ibid.), the Federal Government of Somalia (FGS) announced in 2012 that it sought to auction some of its 308 newly delineated oil blocks during the course of 2013. This proclamation fell on fertile soil, as signs of an improved political and security situation surfaced throughout 2012, causing optimism amongst oil producers.

The attractiveness of Somalia's hydrocarbon endowment is largely based on the promising large profit margins. Thereby, a central question for the hydrocarbon development sector is whether Somalia will significantly and sustainably stabilize with regards to its security, political, and legal landscape in the short and medium term in order to allow for commercial oil production. However, as Somalia's future trajectory is anything but independent of prospects for oil exploitation, an equally pertinent question is how far the development of the country's hydrocarbon sector will present a challenge to Somalia and its state-making endeavour. Put bluntly, the key questions are whether, why, and how Somalia's hydrocarbon endowments might oil rather than spoil its endeavour for state-making and stabilization.

This problem arises in light of the fact that Somalia not only needs to counter the standard challenges arising from the resource curse, but must do so in the context of fragility. What is more, the Somali polity has embarked on the delicate process of redefining and reconstructing the parameters of its statehood. As these parameters are likely to be significantly influenced by (prospects for) oil production, this paper explores the question of why and how the prospects for oil exploitation may jeopardize Somalia's state-making project. After briefly discussing Somalia's hydrocarbon potential and the country's vulnerability to falling prey to the resource curse, the paper goes into greater depth with regards to particular challenges Somalia is likely to face. Having outlined a number of key obstacles Somalia will likely encounter on the road to successful petroleum development, a conclusion presents some essential policy recommendations.

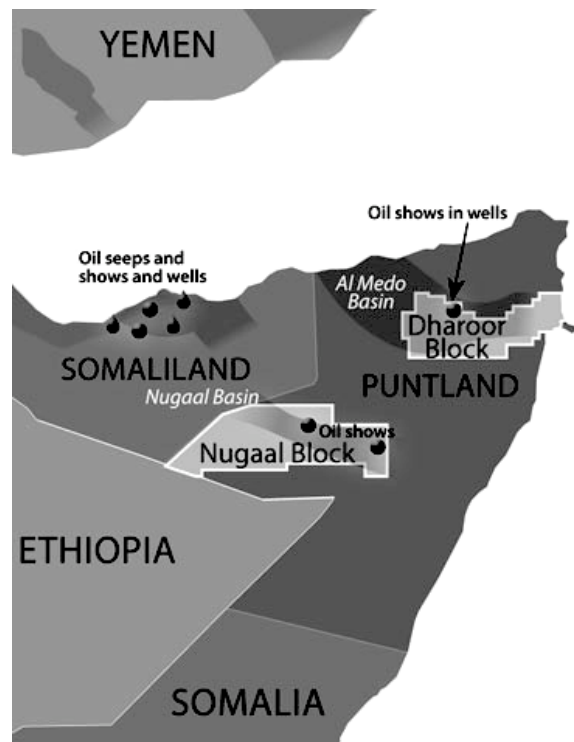
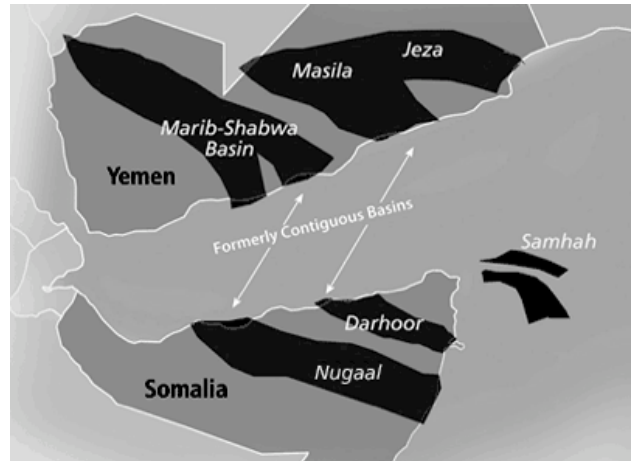
Oil in Somali Soil

Somalia's history of oil exploration dates back several decades. During colonialism, Italian and British geologists were the first to identify oil seeps. Starting in the early 1950s, Italy-based Agip (now Eni) and US-based Sinclair Oil Corporation began to study the petroleum geology of Somalia. This was followed by another major phase of hydrocarbon exploration in the late 1980s, spearheaded by ConocoPhillips, Shell (Pecten), Eni, Amoco, Total and Texaco (ibid.). Yet, with the overthrow of the Mohamed Siyad Barre regime in 1991 and the ensuing civil war, these companies – together with other actors such as BP and Chevron – declared force majeure and put their operations on hold. Ultimately, hopes for embarking on oil production in Somalia were buried when the US-led and UN-approved humanitarian intervention 'Restore Hope' in 1992/93 failed to bring political stability to the country.

Roughly two decades later, oil is back on Somalia's agenda. A key reason for oil companies' continued interest has to do with the country's promising geology. Somalia's geological formation bears important parallels to that of Yemen, which holds some 9 billion barrels of proven oil reserves. According to petroleum geologists, the South Yemeni Marib-Shabwa and Sayun-Masila basins are associated with the Nugaal and Dharoor blocks in northern Somalia respectively (see Maps 1 and 2). A hydrocarbon analysis undertaken by the World Bank and the United Nations Development Programme (UNDP) in 1991 confirmed such favourable assessments. It concluded that of all countries bordering the Red Sea and Gulf of Aden, Somalia had the best future hydrocarbon prospects in the region, second only to Sudan.

While expectations about Somalia's hydrocarbon sector run high, its potential remains vastly underexplored. Most exploration efforts have, to date, been confined to Somalia's northern territories, owing in large part to security considerations. In the internationally unrecognized Republic of Somaliland, which unilaterally declared independence from Somalia in 1991, the three oil companies of Australia's Jacka

Resources, UK-based Ophir Energy, and Anglo-Turkish Genel Energy have started exploration. Whereas Ophir Energy and UAE-based Ras Al Khaimah Gas Company (RAK Gas) are currently participating in the Berbera Production Sharing Agreement (PSA) (Oil Investing News, 2012), the government of Somaliland announced on 25 April 2013 that it had entered into another PSA with the Norwegian oil and gas company DNO International (Mallory, 2013).



Source: <http://www.hornpetroleum.com/Operations.html>

Moreover, after pledging almost US \$40 million – a significant investment in the context of Somaliland's national budget that stood at an average of US \$175 million over the past three years – for exploration activities in Somaliland, Genel

Energy gained a license from Somaliland authorities in November 2012 to explore and develop oil and gas reserves. In line with Somaliland President Ahmed Mohamed Mohamoud's electoral promise of 2010 to see through the successful completion of the first exploration stage during his term in office, Genel Energy had hoped to drill its first well in 2014. However, in August 2013 the company announced that it had suspended its activities due to growing security concerns (Africa Confidential, 2013c).

In neighbouring Puntland, the semi-autonomous state that formed in 1998, government authorities granted Australia-based Range Resources a majority stake in two sizable onshore hydrocarbon exploration licenses, in addition to offshore rights, in October 2005. Two years later, the company entered into a PSA with Puntland, and obtained a 100 per cent interest in the Nugaal and Dharoor Valley blocks, concurrently farming out 80 per cent of that share to Canada-based Canmex Minerals (now Africa Oil Corp). In 2012, Puntland authorized the first official oil exploration, leading Range Resources and its partner Horn Petroleum – a subsidiary of Africa Oil Corp – to drill in the Dharoor Block in February. However, after two exploratory wells showed no signs of oil or gas, both were plugged.

Nonetheless, petroleum experts remain optimistic that both the Dharoor and Nugaal blocks, with acreages of 14,384 km² and 21,784 km² respectively, contain commercially viable hydrocarbon fields in the range of about 20 billion barrels of oil (Currie, 2012). Thus, companies such as UK-based BP and Soma Oil have been in negotiations with federal and regional authorities in order to gain exploration rights, while unveiling an initiative to support job-creation projects in coastal regions of Somalia (Assl, 2012). This interest is echoed by actors from emerging economies. China National Offshore Oil Corporation (CNOOC), for example, successfully sought legal permission from Somali authorities to drill for oil, striking a deal with Somalia's Transitional Federal Government (TFG) under President Abdullahi Yusuf Ahmed in July 2007 (Jopson, 2007). India has also shown interest, proposing to train the Somali National Army, increase bilateral trade ties, and integrate Somalia

into its e-network to enhance the country's IT capacity in exchange for concessions (Assl, 2012; Africa Confidential, 2013c).

Opaque state of affairs

Unlike Somalia's geology, its political landscape underwent numerous shifts and rifts over the course of the past decades. Not only did the country experience several phases of civil war and witness different administrations succeeding one another, it has also seen the formation of new political entities on its territory. While Somaliland and Puntland constitute the most pronounced and well-known sub-national polities, there are currently numerous attempts to establish other regional entities, including Galmudug, Himan and Heeb, and the recently established Jubbaland administration in southern Somalia. Given that some of these polities have signed their own deals with oil production companies without necessarily obtaining the consent of the federal government in Mogadishu, a situation has evolved in which both contractual obligations and property rights remain both opaque and contested.

One example illustrating this ambiguity concerns the 12,000 km² block 'SL 18', which is located in Sool Region, an area disputed between Somaliland and Puntland. While the Somaliland government awarded this block to Norwegian company DNO International in a PSA signed on 22 April 2013, the Puntland government sold the Nugaal Valley Basin – in which block 'SL 18' falls – to Horn Petroleum (Indian Ocean Newsletter, 2012). Furthermore, ConocoPhillips and Shell also possess exploration rights in the same region, dating back to the late 1980s. While the territory into which the respective block falls is claimed by the administrations of Somaliland, Puntland, and the 2012 established Khatumo State of Somalia, the FGS argues that the authority to issue licenses remains the purview of the federal government. A similar case in point is a deal struck in February 2013 by PetroQuest Africa – an affiliate of US-based Liberty Petroleum – with the regional government of Galmudug (Manson, 2013).

Legal difficulties aside, there are also numerous

other hurdles to oil production in Somalia. First, the country's oil remains difficult to access, and significant obstacles exist regarding Somalia's infrastructure and processing capacity. Thus, if Somalia's oil fields are to be developed, considerable prior investments are required. Second, the security situation remains tenuous despite recent military gains registered against the al-Qaeda-aligned al-Shabaab. Just weeks after a consortium of oil companies declared their drilling activities in Puntland in early 2012, al-Shabaab announced that "Somali oil carries death", and that all oil exploration contracts in northern Somalia are void (NewsBank, 2012b). Third, in light of the large-scale absence of functioning institutions in the central government, political decision-making processes will remain highly unpredictable and will depend more on individuals than institutions.

Yet, not only international oil companies face major obstacles with regards to oil production in Somalia. There are also significant challenges for the Somali government and its people that will need to be tackled in order to turn the natural resource wealth into a boon rather than bane for the country's future trajectory. One of the most fundamental challenges is the resource curse.

The Resource Curse

Despite its significant potential, it is well-known that oil wealth is not a panacea for conflict and underdevelopment. Whereas Chile, Botswana, and Indonesia have significantly benefited from their natural resources, the oil experiences of Venezuela, Turkmenistan, and Nigeria have been less favourable. Despite registering US \$800 billion in oil revenues over the past 50 years, Nigeria's average per capita income has stagnated at just US \$1 per day. Why have development indices for this and other oil-producing states remained as low as for other developing countries without natural resource wealth? And to what extent is Somalia likely to suffer the same fate?

The economic side of the resource curse

The hypothesis of the resource curse (see Gelb, 1988; Auty, 1993), also referred to as the 'paradox of

plenty' (Karl, 1997), is that economic growth and development trajectories of countries with large natural resource endowments are worse than those of countries without such wealth. A number of studies show that countries which derive a high proportion of their revenue from rents, rather than from broad-based taxation of their citizens, suffer from a negative correlation between natural resources and economic development (see Auty, 2004; Humphreys, Sachs and Stiglitz, 2007; Beland and Tiagi, 2009). The central underlying mechanism that is hypothesized to drive this effect is found in the phenomenon known as 'Dutch disease' (Economist, 1977).

Principally, a significant inflow of unearned resources leads to an overvaluation of currencies and, thus, appreciation of real exchange rates. In turn, this results in wage increases across the economy, higher production costs and, consequently, a decline in competitiveness of the respective country's productive economic sectors, hitting tradable sectors such as agriculture and manufacturing particularly hard (see Sachs and Warner, 2001; Gylfason, 2000; Bazilian et al., 2013). Against the backdrop that Somalia's economy relies significantly on the export of livestock and agricultural products as well as other trade-based sectors, Dutch disease constitutes a real danger for its development.

Acknowledging the underlying economic dynamics of the resource curse, it has rightly been pointed out that it is not the abundance of natural resources per se, but rather the rents it produces, which cause the effects of economic distortion (Kolstad and Wiig, 2008). Going one step further, it can be argued that it is not even the rents in and of themselves, but rather the way they are managed, which can lead to resources becoming problematic. This is to say that the paradox of plenty is neither a predetermination nor an unavoidable destiny, but that there is considerable room for human agency both in catalysing and correcting its effects (see also Humphreys et al., 2010; Roll and Sperling, 2011). Thus, political agency plays as much a role in explaining, as it does in resolving the resource curse. Yet, it remains questionable whether Somalia's leadership can muster the skills

necessary to manage these challenges sufficiently to fend off such detrimental economic effects.

The political side of the resource curse

Apart from exercising distortionary effects on the economy, the resource curse has also been documented to have adverse implications on states' political landscapes. For one, it is argued that an abundance of natural resources renders governing elites more autonomous from their populations, thus leading to state-society disjunction and decreasing politicians' accountability to their constituencies. Moreover, it is suggested that the significant inflow of unearned resources provides the ruling class with abundant capital to strengthen the security apparatus, largely used to keep political opposition in check and establish a more authoritarian political system. The challenge oil poses for the prospects of democracy in hydrocarbon-rich countries has been stressed extensively in the state-making literature (see Karl, 1997; Chaudhry, 1997; Vandwelle, 1998).

In light of Somalia's fledgling state institutions, the de facto absence of effective checks and balances, as well as its nascent democratic structures, the hydrocarbon sector's economic spoils are likely to also spoil politics. Given that high-level corruption continues to be rife, the transparent and just management of the profitable hydrocarbon sector is very likely to provide a considerable challenge to Somalia's institutions. The lack of transparency and oversight are also likely to foster corruption and social divisions, which can constitute key drivers for (renewed) conflict (see Karl, 1998, 2000, 2005; De Soysa, 2000; Silberfein, 2004; Roll and Sperling, 2011; Ross, 2012).

Proposed solutions to the resource curse

In light of growing awareness of the risks associated with vast natural resource endowments, policy solutions to avoid the paradox of plenty are increasingly being discussed. The literature on the resource curse boasts numerous 'lessons learned' and offers guidance on how to design effective economic solutions and governance frameworks. Such measures include the careful control of

spending, the establishment of stabilization funds (notably, so-called sovereign wealth funds), as well as transparency initiatives such as the 'Extractive Industries Transparency Initiative' (EITI) or 'Publish What You Pay' (PWYP). Simultaneously, the literature features a long list of governance improvements, ranging from capacity building to anti-corruption mechanisms.

While many lessons can be learned from past empirical case studies and accumulated analysis, there are still several problems with the sets of solutions that have been offered. For one, there is no easy one-size-fits-all formula to escape the resource curse, due to different countries' political, economic, and social specificities. For another, many of the proposed solutions presume relatively well-functioning political and legal environments (Carbonnier and Jerbi, 2013), which is hardly characteristic of the states under consideration in general, and Somalia in particular. As is the case in other developing and fragile states, the weakness of formal institutions in Somalia will make it difficult to develop and implement complex financial mechanisms.

A third obstacle is that even though improvements in economic and political management are necessary to defy the resource curse, success stories like Botswana, Chile, and Indonesia clearly show that it does not simply boil down to the political elites' ominous 'political will'. Rather, a central lesson from these countries is that states need a well-trained cadre of technocrats and administrators in order to manage oil production, revenue management, and the establishment of a productive economy beyond the sector of hydrocarbon exploitation, if sustainable and broad-based benefits are to be made of a country's resource wealth (see Shepherd, 2013).

Somalia: Ready for Oil?

After two decades of instability and conflict, hope is gradually returning to Somalia. The African Union Mission in Somalia (AMISOM) has registered important military gains against the radical insurgence of al-Shabaab since 2011 in general, and since its March 2014 offensive in particular.

Moreover, 2012 saw a sharp and sustained decline in piracy attacks off the Somali coast. These improvements in the security realm were accompanied by political advancements. Somalia's much criticized eight-year period of 'political transition' came to an end, when the Transitional Federal Institutions (TFIs) were replaced by a Federal Parliament on 20 August 2012, followed by the election of a new President in September and the establishment of the new FGS from October onwards.

On an international level, the FGS managed to achieve important diplomatic goals, which significantly strengthened its position. It gained formal recognition from the United States of America and the International Monetary Fund (IMF) in January and April 2013 respectively, and also saw the partial lifting of the arms embargo by the United Nations Security Council in March 2013. Two months later, the same international body unanimously voted to establish a new political mission, the United Nations Assistance Mission in Somalia (UNSOM), and major conferences were held in London, Brussels, Yokohama, and Istanbul, thus paving the way for a renewed engagement with a country that had long been considered to be the world's failed state nonpareil.

However, despite these positive developments and accompanying enthusiasm, Somalia still has a long road ahead before exiting its state of fragility. As demonstrated by sporadic yet recurrent terrorist attacks in Mogadishu as well as in neighbouring countries, Al-Shabaab is far from defeated. Simultaneously, it remains questionable whether peace will reign if the terrorist group is defeated, as the revival and amplification of regional tensions and inter-clan conflict cannot be ruled out. Moreover, the political landscape remains shaky and hard to predict, not least due to the continued weakness of formal institutions and chronic contestations over political and resource control.

In light of these and a host of other remaining challenges, the question is whether Somalia is ready for oil. Asked differently, how likely is Somalia to escape the resource curse, and what are some of the most pressing obstacles it is likely to

face beyond this hurdle?

Vulnerable to suffer from the resource curse?

The establishment of a productive economic sector is not only central to any state-making project in general, but also key to countering the economic hazards associated with the resource curse. The literature on the paradox of plenty stresses that countries rich in hydrocarbon endowments must establish a productive economy in order to sustain economic diversity and balance. To accomplish the latter, it is generally advised that investments accruing from oil revenues should be directed towards the build-up of a country's productive capacity of non-oil industries (AfDB, 2008). According to the Hartwick rule, economic stability can only be secured if any depletion of natural resources is compensated for by increases in non-human and/or human capital (Hartwick, 1977). Since oil wealth alone is unlikely to generate sustainably high living standards for the majority of the Somali population, achieving economic diversification will be critical in order to create income-creating opportunities, tackle unemployment, and ensure greater resistance to volatile budgets caused by global price shocks in natural resources.

Somali actors thus need to focus significant attention on achieving economic recovery. Neither the Somali government nor the international community has made significant strides in this direction so far. The Somali economy continues to be characterized by low levels of manufacturing and industrialization, as a noteworthy productive economy beyond livestock barely exists to date. Simultaneously, (youth) unemployment remains stubbornly high and the population's energy provision insufficient. While universal access to electricity is a fundamental precondition in order to allow for greater economic diversification, Somalia is unlikely to achieve this objective – in part because it is highly unlikely that Somalia will have its own oil refinery – anytime soon. In the absence of refining capacity, there are only very limited economic and technological spill-over effects that could promote growth in the rest of the

economy (Bazilian et al., 2013).

Somalia hardly possesses the well-trained cadre of technocrats and administrators necessary to counter the politically and economically detrimental effects of the paradox of plenty (Shepherd, 2013). Moreover, the state not only lacks clear property rights and sufficient capacity to enforce these, but it also exhibits extraordinarily weak bodies of political oversight, while simultaneously featuring entrenched corruption. Although perceptions about the current trajectory of the country's levels of corruption are ambiguous, Somalia remains ranked as the most corrupt country in the world (Transparency International, 2012). For these and other reasons, it seems unlikely that Somalia is in a position to successfully tackle the challenge of countering the adverse economic effects generated by the resource curse. As if that was not enough, the country faces a multitude of additional challenges associated with the early stages of re-defining and re-constructing statehood.

Catalysing regional power play

It is well-established that a country's natural resources can provoke political tensions with neighbouring states (see Billon, 2004). This is the case in Somalia, where neighbouring countries as well as states further afield have been alleged to have interests beyond the humanitarian and political situation. The links in the early 1990s between the international humanitarian intervention and the interest of Western oil companies have been pointed out by a number of analysts, and today's international military engagement is frequently believed to be partially driven by a quest for oil exploration (see, for example, Gibbs, 2000; Assl, 2012). One clear indication of this can be found in the fact that one of the US government's six conditions it put in place prior to recognizing the FGS lay in the Somali government recognizing the rights of US oil companies that had declared force majeure when the regime of Siyad Barre crumbled (Heritage Institute for Policy Studies, 2013).

Similarly, Kenya's interest in Somalia's

hydrocarbon endowments appears to have been a key driver behind Nairobi's 2011 decision to militarily intervene in Somalia, and lend its support to the regional administration of Jubbaland (Jopson, 2007). The circumstances under which Kenya opened a liaison office in Kismaayo without seeking prior permission from the FGS, and the fact that Italy-based Eni "intentionally signed a contract with Kenya over a territory that clearly belongs to Somalia", support this proposition.³ While the FGS is hardly in a position to dispense of international partners like Kenya in its fight against al-Shabaab, it seems that Nairobi's desire for near-term hydrocarbon exploration and exploitation in Somalia not only adds a layer of complexity to the situation, but may actually run counter to re-establishing a stable and functioning state.

Enhancing sub-national divisions

The yet greater hurdle for Somalia's trajectory lies with the likelihood that oil will also catalyse rifts and political tensions at the sub-national level. This risk is particularly likely in an environment in which demands for federal state structures have gained momentum. During the 'roadmap process' designed to end Somalia's transitional era, and since the selection of President Hassan Sheikh Mohamud in September 2012, sub-national fissures have increasingly come to the fore. Puntland has felt increasingly marginalized by President Mohamud's government. Analysts judge that "Mogadishu's relations with Puntland are far from good and could worsen if oil prospects prove fruitful," (Africa Confidential, 2013a). Similarly, tensions with Somaliland also remain significant – as shown not least in the recent dispute between Hargeisa and Mogadishu over the control of Somali airspace – and are likely to harden if commercially viable oil is found in Somaliland.

Even more acute fissures have emerged within south-central Somalia. Recent discussions concerning the envisaged nature and shape of a future Somali state have been strongly marked by demands for federalism by both national and international actors.⁴ Even though the President has shown reservations – due in part to the

challenges a federal formula holds for re-establishing a united Somali state – the national and international push for federalism sanctioned the formation of the Jubbaland administration. This and the controversial selection of Ahmed Mohamed Islan ‘Madobe’ as President of Jubbaland on 15 May 2013 sparked significant tensions not only between Kismaayo and Mogadishu, but also within Jubbaland itself. While events in Kismaayo have historically been influenced by numerous factors, the contestation over the port city has increasingly been regarded as a “key element in a brewing dispute over oil and natural gas” (United Press International, 2012b).

Given that tensions between centralising and devolutionary tendencies have sharpened to the extent that analysts now fear that a next phase of Somalia’s civil war could be between the central government and embittered regional administrations (Africa Confidential, 2013b), recent oil and gas strikes are believed to “have raised the strategic context of the conflict to a new level,” (United Press International, 2012b). Prospects of further hydrocarbon discoveries have spurred a ‘resource race’ in which different political actors have started to carve up oil blocks in order to enhance their politico-economic bargaining power vis-à-vis political competitors, as perhaps demonstrated by the deal struck between the administration of Galmudug and PetroQuest Africa in February 2013.

This poses a very real threat to the country’s stability, given the absence of a national framework that would govern the distribution of rents accruing from natural resources. Although the FGS is confident that an interim agreement with administrations in Puntland and Jubbaland can be reached in the not too distant future,⁵ any legal regulation on this issue is palpably missing. Meanwhile, the Provisional Constitution asserts in very general terms in Article 44 that “[t]he allocation of the natural resources of the Federal Republic of Somalia shall be negotiated by, and agreed upon, by [sic] the Federal Government and the Federal Member States in accordance with this Constitution”, leaving ample room for conflicting interpretations. While the FGS partly uses the

Provisional Constitution’s sovereignty clause (Article 7.1) in order to claim ownership over the country’s resources, authorities of (aspiring) federal member states point out that the document explicitly instructs negotiation between the two levels of government with respect to “[t]he allocation of the natural resources”. Moreover, the latter also refer to Article 54 on the allocation of powers between the federal government and federal member states, which does not include natural resources as the exclusive prerogative of the central government.

While regional authorities have been hostile to central government claims to the country’s natural resources, tensions between the regions have also increased. Competition over the Nugaal Block that stretches across not only Somaliland and Puntland, but also the more recently established Khatumo state, serves to illustrate this point well. These developments indicate that, in light of missing agreements and legal frameworks, the oil factor is likely to hamper rather than help Somalia’s endeavour to rebuild a stable state. Hence, there is reason to fear that if a scramble for petroleum precedes the forging of a political settlement, and subsequent establishment of a legal framework, between the federal states and Mogadishu, conflict will be likely (see Jopson, 2007).

Increasing local tensions and insecurity

The potential for hydrocarbon development may also spark local tensions and undermine the Somali government’s endeavour to establish lasting peace and security. As evidenced by the case of Puntland, oil production can foster local insecurity. In August 2005, Puntland’s then President Mahmud ‘Adde’ Muse flew to Dubai and met with representatives of Range Resources, with whom he had signed a contract, disregarding the region’s constitution and the establishment of the new federal government. Subsequent attempts by Range Resources to send geologists to the area sparked civil unrest in the erstwhile peaceful mountainous village of Majiahan. In March and April 2006, local villagers took up arms against Puntland security forces protecting the geologists, resulting in the death of at least ten people, including soldiers and

villagers. Consequently, Puntland and Range Resources suspended their operations as it became increasingly obvious that the local Warsangeli clan violently opposed any encroachment upon their territory without prior clan approval (Newsbank, 2008).

It is partly these developments that prompted the formation of new security agencies in Puntland. Africa Oil Corp, for example, has its operations protected by the security firms Salama Fikira of Kenya and Pathfinder Corporation of South Africa. The security companies' operations have resulted in the formation of an Exploration Security Unit (ESU) – a special branch of the Puntland Security Forces whose sole purpose is to provide security for the Horn Petroleum-Canmex-Africa Oil Corp consortium – in 2011. Hired from the Puntland army and police forces and trained by Pathfinder, the ESU includes over 300 armed men receiving monthly salaries from Canmex (Indian Ocean Newsletter, 2012). Such changes not only further fragment Somalia's security architecture, but render it increasingly difficult for the federal government to establish a monopoly over the means of large-scale violence and enforce particular policies. Consequently, the UN Monitoring Group recommended in a letter dated 12 July 2013 that “oil companies should cease and desist negotiations with Somali authorities or risk fuelling non-transparent practices and political disagreements that could exacerbate clan conflict and constitute threats to peace and security,” (Africa Confidential, 2013d).

The challenge of legal quicksand

The likelihood of violent conflict is enhanced by ambiguous and disputed property rights that result from oil production enterprises having signed competing contracts with leaders of different political entities within Somalia. In this situation, oil companies are likely to increasingly try to hold their respective signatories to account in order to see their contract rights enforced and protected, thus putting additional strain on already tense communal relationships. In February 2013, for example, PetroQuest Africa signed a deal for a block with the regional administration of

Galmudug, a self-declared state south of Puntland. As this concession overlaps with an offshore block also claimed by Shell, the latter demanded in a letter dated 24 April 2013 that the federal government take action to protect its “exclusive rights” to the block (Manson, 2013), thus raising the possibility of a violent ‘solution’.

However, Somalia's legal quicksand does not help to clarify the situation. For one, the country's 2008 oil law is sketchy and leaves much room for diverging interpretation, even though it allegedly ranges among the country's most progressive laws. Moreover, fundamental questions on which political actors are ultimately allowed to sign oil production agreements in the first place remain unclear. While interim President Abdullahi Yusuf Ahmed had officially granted regional administrations the authority to enter into oil production contracts (NewsBank, 2012a), President Sheikh Sharif Sheikh Ahmed's senior adviser Abdullahi Haider proclaimed in October 2012 that all energy contracts signed by regional administrations were ‘null and void’. Simultaneously, other government officials made statements to the contrary (Gilblom, 2012). President Mohamud for his part has been very critical of having regional polities sign oil contracts, fearing that conflictive oil rights may turn Somalia into a political powder keg. He called on international oil enterprises not to enter into deals with regional authorities, threatening that this “will block their future engagement in Somalia,” (Manson, 2013).

Conclusion and Policy Considerations

While it has been argued that the discovery of oil could provide a genuine push to put an end to Somalia's social, political, and economic problems (Assl, 2012), there is reason for caution. Just as “[o]il has fuelled the struggle for power and rent, and delayed, if not derailed the state building process [in Iraq]”, Somalia could be met by a similar fate (Larbi, 2012). This risk not only flows from the country's significant vulnerability to suffer from the effects of the resource curse, but is also related to the nascent stage of Somalia's state-making project. Given the wider context Somalia finds

itself in, it appears that oil exploration and production is likely to exacerbate an already difficult process of forging a functioning elite bargain and setting up transparent and reliable institutions in order to advance the country's state-making endeavour.

The transparent and just management of the profitable hydrocarbon sector poses a significant challenge to Somalia's policy-makers. Yet, the lack of adequate institutions and oversight enhances the risk of corruption and deepened social divisions, which can constitute key drivers for (renewed) conflict. Another central obstacle for the beneficial development of Somalia's petroleum resources lies with the sequencing of production vis-à-vis political progress. There is a real risk that hurried hydrocarbon production that precedes the forging of a political settlement between federal members states and the federal government will spark violent conflict.

Consequently, the majority of the standard policy recommendations to counter the phenomena of the resource curse and Dutch disease are not only insufficient, but wholly inadequate to address the risks emanating from hydrocarbon production for Somalia. What, therefore, are the essential policy recommendations major actors should consider in order to tackle the challenges emanating from hydrocarbon production in Somalia?

First, the FGS urgently needs to address existing legal ambiguities and political points of contention. For one, this means that Somali legislators should – in collaboration with elected representatives of regional states – revise the country's legislation that regulates the exploitation of natural resources. This includes the closing of any loopholes and ambiguities that feature in Somalia's provisional constitution. For another, the FGS's executive branch must find a politically viable and binding solution to the question of who has the right to enter into – and the responsibility to honour – contracts with oil companies. This is a hard nut to crack, and will require the cooperation of Somalia's more or less developed federal units. Moreover, Somalia must investigate how to best acquire and sustain technical expertise and administrative

capacity in order to effectively negotiate and manage oil agreements with international companies.

In the meantime, the creation of a sovereign wealth fund receiving all revenues accruing from hydrocarbon production on Somali soil may offer a solution. Policymakers from across the country could agree on a legislation that would freeze such a fund's financial resources until a watertight legal framework is in place, clearly spelling out how the rents are to be divided among different political entities. Such a mechanism could not only be Somalia's best bet to avoid internal strife and conflict, but may also accelerate the process of finding a viable political and legal solution so as to move the development of its hydrocarbon potential forward. While the federal government's Petroleum Strategy pushes for speedy steps in the directions of exploration and production, the country's political, legal, and institutional ambiguities need to be addressed first, if adverse effects of hydrocarbon development are to be minimized.

Second, Somali authorities instantly need to devise a strategy on how to actively manage public expectations emerging in relation to natural resource exploitation. As can be seen in other countries, such as Tanzania, the management of public expectations is critical in order to minimize potentially negative consequences that accrue from a disappointed public. The constituencies' expectations should not simply be dampened, but rather approached in an open and transparent manner. An interstate commission on natural resources could potentially take on this task. By acting as a knowledge platform and drawing on experiences from other oil-producing countries with federal state structures, such a commission could also mediate among different levels of government and advise them on how best to move forward.

Third, international oil production companies need to take great caution not to upset the little progress towards state-making that Somalia has achieved throughout the recent past. For one, this means that they should strictly abide by Somalia's national laws. For another, rather than narrowly focusing on

the natural resource sector itself, oil firms should consider a more holistic approach to developing Somalia's hydrocarbon potential. This would start by helping the Somali authorities to carry out a proactive campaign to manage popular expectations and to set up relevant institutions as well as technical and managerial capacity. It would also entail that international firms await the conclusion of political and legislative proceedings at the part of Somali authorities, before moving exploration and exploitation initiatives forward. By jumping the gun the government is not only likely to jeopardize the establishment of much needed institutions, but also to find itself being associated with smaller and short-lived financial profits rather than larger and more sustainable ones.

Fourth, the international donor community should, at a bare minimum, promote corporate social responsibility initiatives amongst the companies planning or engaged in hydrocarbon production in Somalia. More generally, international aid organizations should seek to integrate these private enterprises into its broader development programs, so as to help forge a more effective coalition and create synergies between the two sectors. Moreover, Somalia's international partners should consider investing more strongly into the establishment of a productive economy in Somalia by rebuilding, for example, the country's feeble (energy) infrastructure. Last, but by no means least, the international donor community should explore possibilities of using aid funds in such ways as to smoothen out volatile government budgets that are certain to fluctuate if Somalia becomes increasingly dependent on oil revenues.

For Somalia, the road towards the development of its hydrocarbon potential is winding and full of challenges. The country's fragile political situation, weak institutions, and legal immaturity raise doubts as to whether it is sufficiently prepared to embrace the obstacles that come with hydrocarbon development. In order not to add fuel to the fire, but to make the greatest use of the country's hydrocarbon potential, a great deal of caution is required from all parties involved. Only if oil exploitation is seen as a means to the end of establishing a viable state, rather than an end in

itself, can Somalia's hydrocarbon endowments possibly oil rather than spoil its future trajectory.

Footnotes

¹ While global demand for oil stood at around 75 million barrels per day in 2000, the International Energy Agency estimates that this demand may nearly double by 2030 (Anderson and Browne, 2011).

² By comparison, some 14,000 wells have been sunk in West and 20,000 in North Africa (Anderson and Browne, 2011).

³ Interview with senior government official, 22 May 2014.

⁴ See, for example, the Communique of the 2013 London Conference on Somalia.

⁵ Interview with senior government official, 22 May 2014.

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