INTERNATIONAL MONETARY FUND

IMF Country Report No. 24/253

THE FEDERAL DEMOCRATIC REPUBLIC OF ETHIOPIA

July 2024

REQUEST FOR AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR THE FEDERAL DEMOCRATIC REPUBLIC OF ETHIOPIA

In the context of the Request of an Arrangement Under the Extended Credit Facility, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Acting Chair of the Executive Board.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on July 29, 2024, following the discussions that ended on April 2, 2024, with the officials of The Federal Democratic Republic of Ethiopia on economic developments and policies underpinning the IMF Arrangements under the Extended Credit Facility program. Based on information available at the time of these discussions, the Staff Report was completed on July 12, 2024.
- A **Debt Sustainability Analysis** prepared by the staffs of the IMF and World Bank.
- A **Staff Supplement** updating information on recent developments.
- **Statement by the Executive Director** for The Federal Democratic Republic of Ethiopia.

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International Monetary Fund
Washington, D.C.

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PRESS RELEASE

PR 24/291

IMF Executive Board Approves Four-Year US$3.4 billion Extended Credit Facility Arrangement for The Federal Democratic Republic of Ethiopia

FOR IMMEDIATE RELEASE

- The IMF Board approved an SDR 2.556 billion (about US$3.4 billion) ECF arrangement for Ethiopia. This decision will enable an immediate disbursement equivalent to SDR 766.75 million (about US$1 billion).
- The four-year financing package will support the authorities' Homegrown Economic Reform (HGER) Agenda to address macroeconomic imbalances, restore external debt sustainability, and lay the foundations for higher, inclusive, and private sector-led growth.
- The ECF arrangement is expected to catalyze additional external financing from development partners and creditors.

Washington, DC – **July 29, 2024:** The Executive Board of the International Monetary Fund (IMF) approved a four-year arrangement under the Extended Credit Facility (ECF)[1] for Ethiopia in an amount equivalent to SDR 2.556 billion (850 percent of quota or about US$3.4 billion) to support the authorities' implementation of their Homegrown Economic Reform (HGER) Agenda aimed at addressing macroeconomic imbalances and laying the foundations for private-sector led growth. The Executive Board's decision will enable an immediate disbursement of SDR 766.75 million (equivalent to about US$1 billion), which will help Ethiopia meet its balance of payments needs and provide support to the budget.

The authorities' economic program, supported by the four-year ECF arrangement, envisages a comprehensive policy package to stimulate private sector activity and increase economic openness to promote higher and more inclusive growth. Strengthening social safety nets to mitigate the impact of reforms on vulnerable households is a critical component of the authorities' reform program. Key policies include: (i) moving to a market-determined exchange rate to help address external imbalances and relieve FX shortages; (ii) combating inflation through modernizing the monetary policy framework, eliminating monetary financing of the budget, and reducing financial repression; (iii) creating space for priority public spending through mobilizing domestic revenues; (iv) restoring debt sustainability, including through securing timely debt restructuring agreements with external creditors; and (v) strengthening the financial position of state-owned enterprises to tackle critical macro-financial vulnerabilities.

"This is a landmark moment for Ethiopia," said IMF Managing Director Kristalina Georgieva. "The approval of the ECF is a testament to Ethiopia's strong commitment to transformative

[1] The Extended Credit Facility (ECF) provides medium-term financial assistance to low-income countries (LICs) with protracted balance of payments problems. The ECF is one of the facilities under the Poverty Reduction and Growth Trust (PRGT). https://www.imf.org/en/About/Factsheets/Sheets/2023/Extended-Credit-Facility-ECF

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reforms. The IMF looks forward to supporting these efforts to help make the economy more vibrant, stable, and inclusive for all Ethiopians."

The program is expected to help catalyze additional external financing from development partners and provide a framework for the successful completion of the ongoing debt restructuring.

Following the Executive Board discussion, Ms. Antoinette Sayeh, Deputy Managing Director, and Acting Chair, made the following statement:

“Ethiopia has been facing significant economic pressures amid a series of large shocks, high inflation, low international reserves, and unsustainable debt. In response, the authorities have launched a comprehensive reform program, to be supported by the ECF-arrangement. It is focused on addressing macroeconomic imbalances, restoring external debt sustainability, and implementing wide-ranging reforms to promote a robust, inclusive, and sustainable economy.

“The recent measures to decisively tackle macroeconomic imbalances, including moving to a market-determined exchange rate, removing current account restrictions, and modernizing the monetary policy framework to control inflation, are critical steps forward. Supportive macroeconomic policies, including the elimination of monetary financing of government deficits, monetary policy tightening, and prudent fiscal management, will need to be sustained to keep inflation in check, ensure a successful implementation of the market-determined exchange rate, and durably address exchange rate shortages.

“The authorities’ policies are well calibrated to protect the vulnerable and mitigate the socio-economic impacts of the reforms. They will significantly increase the budget allocation to the targeted cash transfer program (PSNP). Temporary subsidies on fuel and fertilizers are also part of the fiscal package, and will need to be unwound gradually over time. Continuing to widen the reach and impact of the social safety-net programs will be important.

“The authorities are advancing reforms to ensure the sustainability of public finances. Raising fiscal revenues and reaching a comprehensive external debt treatment, including of official debt under the G20 Common Framework, are crucial in this regard. The first use of the ‘credible official creditor process’ under the recent IMF policy reform has successfully allowed the Official Creditor Committee under the G20 Common Framework to provide financing assurances for this ECF-supported program in a short period of time.

“Strengthening public investment management, including spending related to climate change and post-conflict reconstruction, is also important. Transparency and the management of fiscal risks, particularly those related to extrabudgetary units and large state-owned enterprises, should be enhanced. Power sector reforms including tariff adjustment are also vital.

“The recent recapitalization of Commercial Bank of Ethiopia tackles a key macro-financial vulnerability. Reforms to improve financial sector governance and steadily reduce financial repression will be essential. Strengthening the NBE’s mandate and governance arrangements will help build the NBE’s credibility and capacity to fulfill its mandates.

“The authorities’ ambitious and comprehensive home-grown structural reform agenda will focus on better governance and public service delivery, competitiveness, and the business climate, to stimulate private sector-led growth and contribute to poverty reduction and raising living standards.

"The IMF extends its deepest sympathies to the Ethiopian people regarding the recent landslide that occurred in the Gofa Zone in the south of the country that led to tragic loss of life, and wishes the authorities the best in their response and recovery efforts.

Annex

After decades of rapid growth and improvements in living standards in Ethiopia, a series of shocks led to severe economic pressures, and the public investment-led growth model has reached its limits. Recognizing the urgent need for reform, the authorities have requested a four-year arrangement under the ECF with the Fund to help meet balance of payments needs and provide support to the budget and the implementation of the Homegrown Economic Reform Agenda (HGER).

Program Summary

The economic program envisages a comprehensive policy package to stimulate private sector activity and increase economic openness to promote higher and more inclusive growth. Strengthening social safety nets to mitigate the impact of reforms on vulnerable households is critical component of the authorities' reform program. Key policies include:

- Moving to a market-determined exchange rate to help address external imbalances and relieve FX shortages.
- Combating inflation through modernizing the monetary policy framework, eliminating monetary financing of the budget, and reducing financial repression.
- Creating space for priority public spending and addressing debt vulnerabilities through mobilizing domestic revenues.
- Restoring debt sustainability, including through securing timely debt restructuring agreements with external creditors.
- Strengthening the financial position of state-owned enterprises to tackle critical macro-financial vulnerabilities.

Table 1. The Federal Democratic Republic of Ethiopia: Selected Economic Indicators, 2021/22–2028/29

	2021/22	2022/23	2023/24 Proj.	2024/25 Proj.	2025/26 Proj.	2026/27 Proj.	2027/28 Proj.	2028/29 Proj.
Output								
Real GDP growth (%)	6.4	7.2	6.1	6.5	7.1	7.7	8.0	7.8
Prices								
Inflation - average (%)	33.9	32.5	26.9	30.1	16.2	12.2	10.4	9.6
General government finances								
Revenue (% GDP)	8.1	7.9	7.3	8.3	9.8	10.8	11.2	11.4
Expenditure (% GDP)	12.7	10.8	9.4	11.3	12.4	13.3	13.6	13.9
Fiscal balance, including grants (% GDP)	-4.2	-2.6	-1.7	-1.7	-2.1	-2.0	-2.0	-2.0
Public debt (% GDP)[1]	48.9	40.2	34.4	42.9	38.8	35.8	33.6	31.5
Money and Credit								
Broad money (% change)	27.2	26.6	14.4	30.3	25.1	26.6	23.5	21.7
Credit to private sector and state-owned enterprises (% change)	18.9	24.1	12.0	21.2	25.5	31.3	20.1	18.2
Balance of payments								
Current account (% GDP)	-4.0	-2.8	-2.6	-4.3	-3.2	-2.5	-2.0	-1.9
FDI (%GDP)	2.6	2.1	1.6	2.7	3.2	2.9	3.0	3.0
Reserves (in months of imports)	0.8	0.5	0.5	1.2	2.0	2.5	3.5	3.6
External debt (% GDP)	24.0	18.1	15.4	28.3	26.6	24.5	22.6	19.8
Exchange rate								
Real effective exchange rate (% change, end of period, depreciation –)	10.1	24.0	…	…	…	…	…	…

[1/] Public and publicly guaranteed external debt, which includes long-term foreign liabilities of NBE and external debt of Ethio-Telecom. Does not include expected debt relief.

INTERNATIONAL MONETARY FUND

THE FEDERAL DEMOCRATIC REPUBLIC OF ETHIOPIA

REQUEST FOR AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY

July 12, 2024

EXECUTIVE SUMMARY

Context. After decades of rapid growth and improvements in living standards, a series of shocks led to severe economic pressures, and the public investment-led growth model has reached its limits. Domestic conflict, the pandemic, droughts, and spillovers from Russia's war in Ukraine, as well as significant exchange rate overvaluation and insufficient macroeconomic policy adjustment, compounded building vulnerabilities resulting in high inflation, falling exports, foreign exchange shortages, erosion of international reserves, and unsustainable external debt. Reflecting their ambition to transform the economic model towards private sector-led development, and recognizing the urgent need for reform, the authorities developed the Home-Grown Economic Reform Agenda. This ambitious plan aims at tackling the drivers of economic imbalances including through moving to a market-determined exchange rate, modernizing the monetary policy framework, tackling fiscal revenues, and reforming state-owned enterprises.

Extended Credit Facility (ECF arrangement). The authorities have requested a four-year arrangement under the ECF for SDR 2,555.95 million (850 percent of quota or about US$3.4 billion) to help address protracted balance of payments needs related to structural external imbalances.

Outlook and risks. While growth is expected to decline in 2023/24 owing to tightening macroeconomic policies, FX shortages, lower agricultural output and policy uncertainty, reform policies are expected to support higher growth and easing inflation over the medium term. Temporary fiscal measures will cushion the socioeconomic impact of reform. Key downside risks include persistent inflation or depreciation expectations, security risks or social unrest, policy slippages, and commodity price volatility.

Program policies and objectives. The authorities' program aims to build economic resilience, laying the foundations for inclusive and private sector-led growth. Key policies include:

- Implementation of a market-based exchange rate, unifying official and parallel foreign exchange (FX) markets, to help address external imbalances and relieve FX shortages.
- Developing an interest-rate based monetary policy framework while eliminating monetary financing and reducing financial repression to combat inflation.
- Domestic revenue mobilization to create space for priority spending and addressing debt vulnerabilities.
- Strengthening social safety nets to help mitigate the impact of exchange rate reforms on vulnerable households.
- Strengthening the Commercial Bank of Ethiopia's (CBE) balance sheet and the financial position of state-owned enterprises (SOEs), addressing key macro-financial vulnerabilities.
- Promoting a robust, inclusive, and sustainable economy, through improving governance, financial inclusion, public service delivery and bolstering climate resilience and food security.

Approved By
Ms. Annalisa Fedelino (AFR) and Mr. Bjoern Rother (SPR)

Discussions took place in Addis Ababa in March-April and September-October 2023; and March-April 2024. The mission held discussions with Minister of Finance Ahmed Shide, Governor of the National Bank of Ethiopia Mamo E. Mihretu, and other senior officials. The staff team comprised of Messrs. Piris Chavarri (Head), Dalmau, Lee, Tulin; Mses. Böhme, Daly, Muehlschlegel, (all AFR); Messrs. Giri (now APD), Hegab (FAD), Gurhy, Mulema (both MCM), Pondi (SPR), and Rasmussen (IMF Resident Representative in Addis Ababa) and Abiy Hailu (local economist in Addis Ababa Office). Mr. Mengistu (OED:AE) participated in key policy meetings. Mr. Morán Arce and Ms. Nsanzimana assisted with the preparation of this report.

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CONTEXT

1. **Significant development progress was made in the years up to 2020.** During 2004–19, Ethiopia reported real GDP growth averaging over 10 percent per year, and rapidly rising per capita incomes. Development indicators saw remarkable improvement: life expectancy rose by about 10 years while infant mortality was halved. While the structure of the economy did not evolve radically, with a still large contribution from smallholder agriculture, Ethiopia maintained a relatively equitable income distribution.

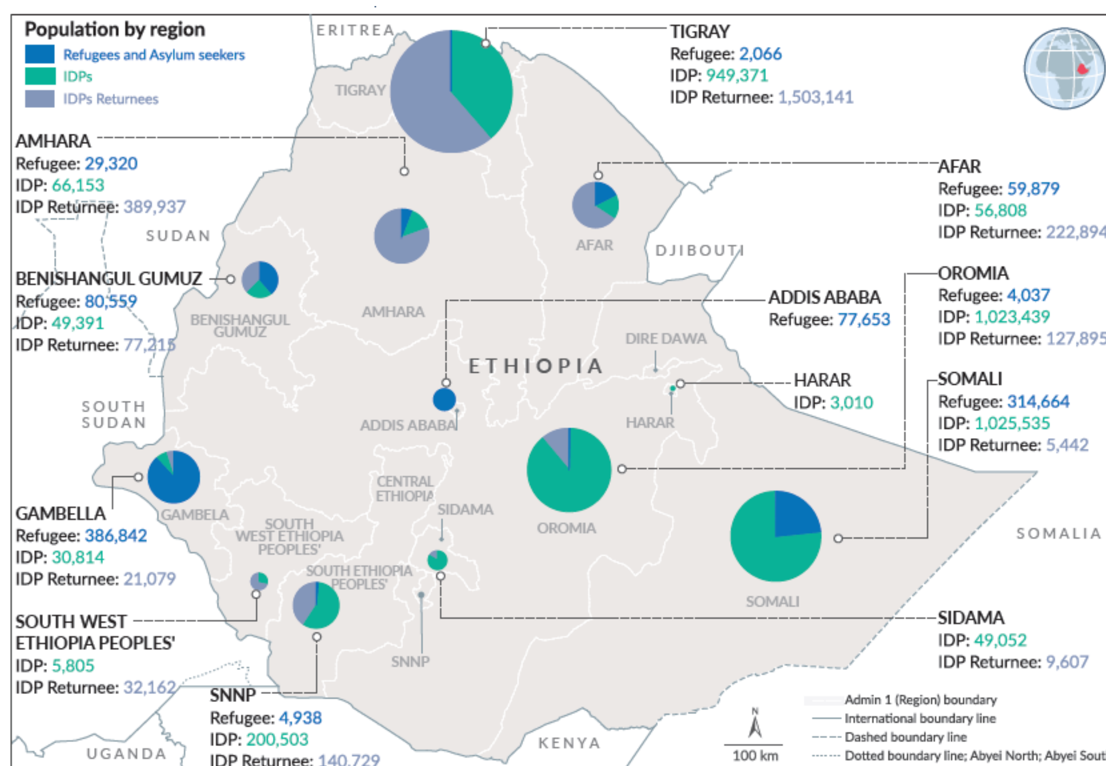
2. **Macroeconomic imbalances left the economy vulnerable to shocks.** Economic growth was propelled by public investment, driven by external borrowing and diversion of domestic resources to infrastructure projects through exchange rate distortions and financial repression. Significant exchange rate overvaluation contributed to weak export growth and current account deficits, and insufficient macroeconomic policy adjustment culminated in severe shortages of foreign exchange (FX), high inflation, and a high and rising parallel market exchange rate premium. The impact of the COVID-19 pandemic, domestic conflict, Russia's war in Ukraine, and tightening external financial conditions contributed to unsustainable external debt and mounting financial stability risks. The authorities requested official bilateral debt treatment under the G-20 Common Framework (CF) in February 2021, agreed a debt service standstill with the Official Creditor Committee (OCC) of the CF in November 2023, and defaulted on a Eurobond coupon payment in December-2023.

3. **Reviews under the 2019 ECF-EFF arrangements could not be completed absent financing assurances from creditors for debt treatment.** The Fund-supported program was built on the authorities' Home-Grown Economic Reform Agenda that aimed to address economic imbalances and revitalize the growth model. The start of the conflict and the COVID pandemic stalled progress, and the ECF and EFF expired in September 2021 and December 2022, respectively, without concluding any reviews and with limited overall progress on macroeconomic reforms.

4. **The end of the large-scale conflict in Tigray was a significant step towards lasting peace and stability.** The Cessation of Hostilities Agreement (November 2, 2022) has been followed with progress on providing humanitarian aid and restoring basic services, and the formation of an interim regional administration in Tigray. However, persistent security problems in some regions and food insecurity worsened by prolonged droughts and a suspension of donor supplies for Tigray following a corruption scandal in 2023 (since lifted), represent significant challenges. The war in Tigray also caused substantial destruction of infrastructure and private property. Reconstruction costs, estimated at US$20 billion, have so far received little international funding. Driven by domestic and regional conflicts, climatic shocks, and economic challenges, there are four million internally displaced people and close to a million refugees (Text Figure 1), and an estimated 21.4 million people need humanitarian assistance (UN OCHA). Ethiopia is classified as a Fragile and Conflict Affected state by the IMF and World Bank.

5. The authorities are redoubling ambitious and urgent reform efforts. The government headed by Prime Minister Abiy Ahmed has been in office since April 2018, launching the Homegrown Economic Reform Agenda (HGER) to modernize the macroeconomic policy framework, boost competitiveness, and lay the foundations for private sector-led growth. The government's reform mandate was reaffirmed in the 2021 elections, with the next general elections expected in 2026. Despite the challenges, the government has renewed its reform efforts, moving ahead with HGER2.0 in 2024.

Text Figure 1. The Federal Democratic Republic of Ethiopia: Refugees and Internally Displaced Persons



Source: UNHCR Refugees and Internally Displaced Persons bulletin, March 2024 (citing UNCS, UNHCR, IOM, CSA Ethiopia).

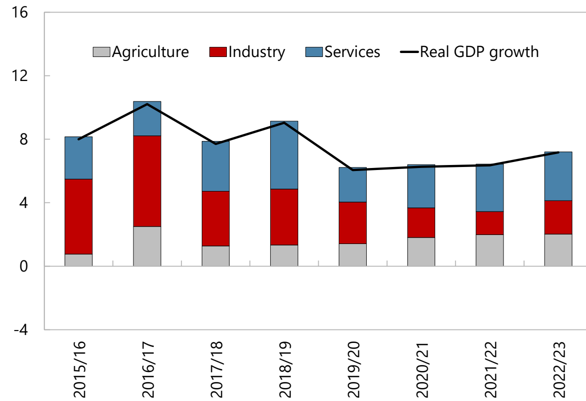
RECENT DEVELOPMENTS

6. Post-conflict recovery sustained GDP growth in fiscal year 2022/23. Following the Cessation of Hostilities Agreement in November 2022, growth rose to 7.2 percent from 6.4 percent in 2021/22, with double-digit growth in transport, communications and hospitality sectors, and favorable rainfall and expansion of irrigated crop production supporting agriculture. Inflation has started to decline but remains above 20 percent in annual terms with more persistence in food inflation (Text Figure 2).

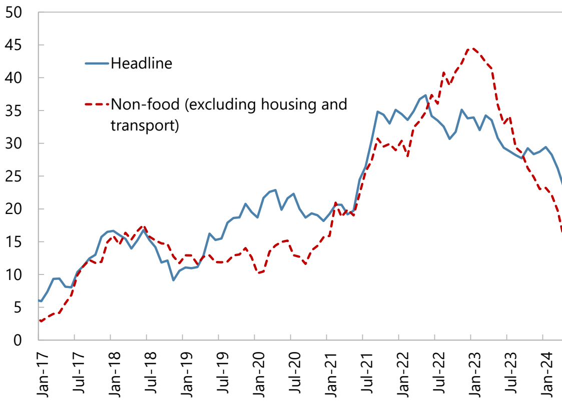
7. Foreign exchange pressures remain acute. Despite the debt service standstill and deposits made by foreign partners at the National Bank of Ethiopia (NBE) that relieved FX liquidity pressures in 2023/24, weak export and remittances contributed to persistent FX shortages. The parallel market exchange rate premium rose to over 100 percent. A US$33 million Eurobond coupon payment was missed on December 11, 2023, triggering default. Gross international reserves stood at US$1.5 billion at end-March 2024, covering less than one month of prospective imports. Real exchange rate overvaluation was estimated at 52 percent in 2022/23 based on the medium-term concept of an estimated norm, mainly reflecting inflation differentials with trade partners and the slow rate of crawl of the official rate (Text Figure 3, Annex I).

Text Figure 2. The Federal Democratic Republic of Ethiopia: Growth Contribution and Inflation

Growth Contributions
(In percentage points)



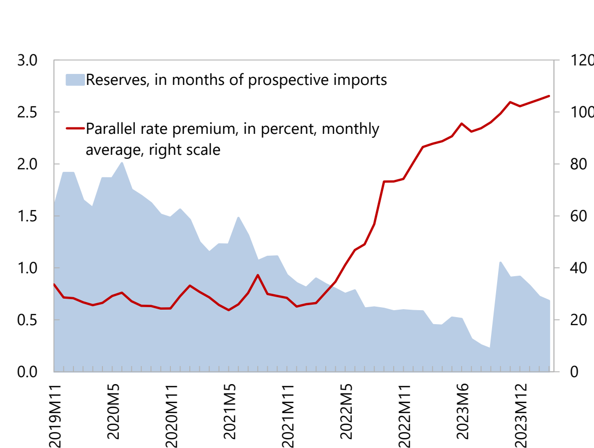
Inflation
(CPI, year-on-year percent change)



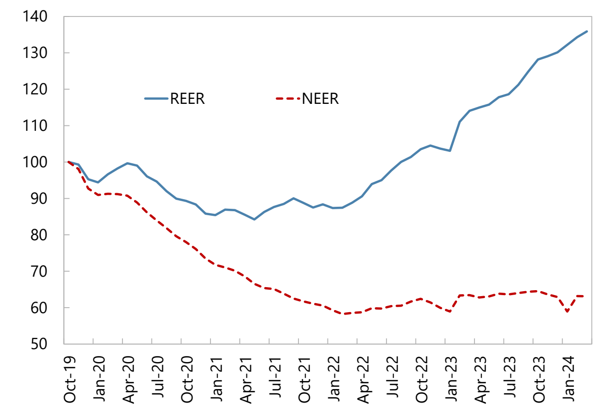
Sources: Ethiopian authorities; IMF staff calculations.

Text Figure 3. The Federal Democratic Republic of Ethiopia: Real Sector and BOP Stress

Reserve Adequacy and Parallel Market Exchange Rate Premium, 2019-24



Real and Nominal Effective Exchange Rate
(December 2019 = 100, Index based on Consumer Price Index)

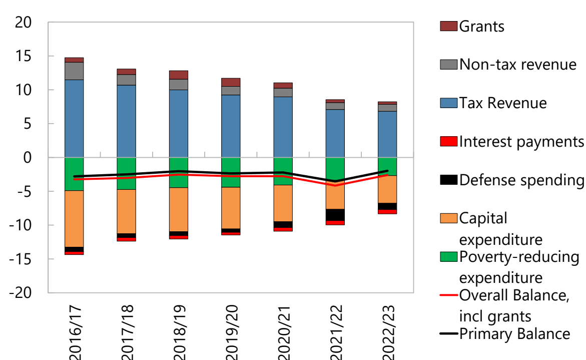


Sources: Ethiopian authorities; World Economic Outlook; IMF Information Notice System database; and IMF staff estimates.

8. A substantial fiscal tightening is underway. Fiscal outturns for 10 months of 2023/24 show the general government primary deficit is on track to decline by 0.9 percent of GDP to 1.1 percent, a significant effort in the post-conflict context (Text Figure 4). General government tax collection has consistently underperformed over the last years, falling to 6.8 percent of GDP in 2022/23 and is expected to drop further to 6.3 percent of GDP in 2023/24. New tax policy measures (a surtax on imports, excise on telecom) have not succeeded in reversing the trend decline in the tax-to-GDP ratio, as FX distortions have eroded corporate profits and the tax base. With constrained external and domestic financing, the authorities have implemented an expenditure-driven consolidation, sharply reducing reliance on monetary financing, and keeping non-interest expenditure unchanged in nominal terms, despite expected average inflation of 28 percent in 2023/24. Current spending pressures have been accommodated through cuts in capital expenditure. Over the last two years, fuel subsidies (that are off budget) have been phased out and fuel prices have risen above cost recovery level at the official exchange rate. The end of the armed conflict in Tigray has allowed a reduction of federal defense spending to near pre-conflict levels.

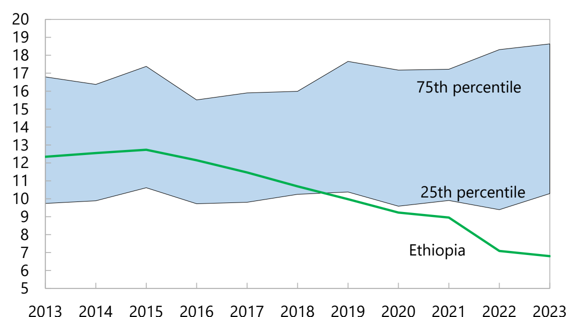
Text Figure 4. The Federal Democratic Republic of Ethiopia: Fiscal Developments

General Government
(In percent of GDP)



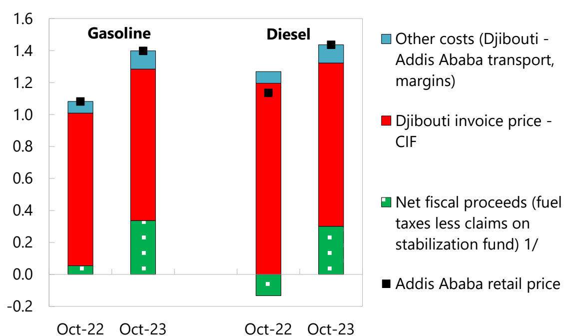
Sources: Ministry of Finance and IMF staff calculations

Sub-Saharan Africa: Tax Revenue, General Government (In percent of GDP)



Sources: World Economic Outlook and IMF staff calculations

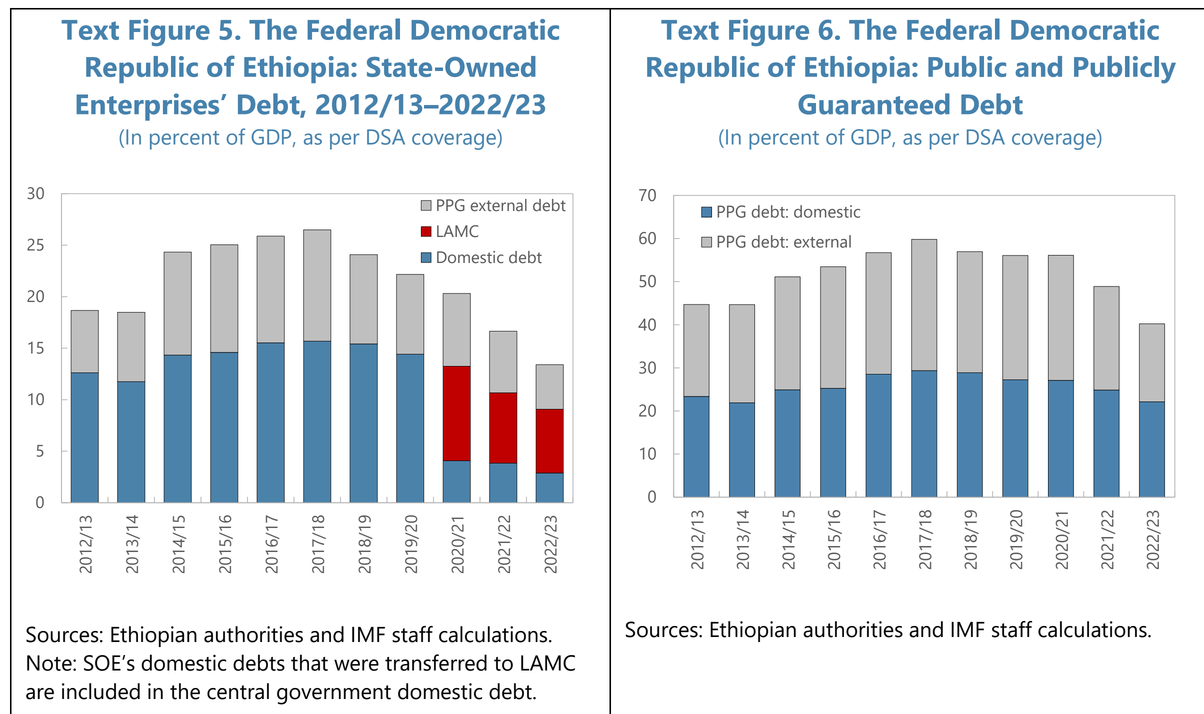
Fuel Price Structure
(In US dollars per liter, converted at the official exchange rate)



Sources: Ethiopian authorities; IMF staff estimates.

[1] Net fiscal proceeds are calculated as the difference between fuel taxes included in the pump price and retained by EPSE, and EPSE claims on the Fuel Price Stabilization Fund. Negative values indicate a fuel subsidy, while positive values indicate that pump prices are above cost recovery levels.

9. SOE debt has declined with controls on borrowing, but progress on reforms has lagged (Text Figure 5, Annex II). Non-concessional external borrowing has been reduced to zero, though reduced SOE borrowing from the state-owned Commercial Bank of Ethiopia (CBE) has continued. The Liability and Asset Management Corporation (LAMC) was established in 2021 to improve balance sheets of indebted SOEs by taking over the bulk of their domestic debt: 9.3 percent of 2020/21 GDP was transferred to LAMC initially, and a further one percent of GDP in loans and accumulated interest of financially weak SOEs was transferred in May 2023.[1] LAMC used privatization proceeds from the a telecom license sale (0.6 percent of GDP in 2021/22) and a mobile payments license (0.1 percent of GDP in 2022/23) to make debt service payments to CBE, but has not made any further payments subsequently.



Text Figure 5. The Federal Democratic Republic of Ethiopia: State-Owned Enterprises' Debt, 2012/13–2022/23
(In percent of GDP, as per DSA coverage)

Sources: Ethiopian authorities and IMF staff calculations.
Note: SOE's domestic debts that were transferred to LAMC are included in the central government domestic debt.

Text Figure 6. The Federal Democratic Republic of Ethiopia: Public and Publicly Guaranteed Debt
(In percent of GDP, as per DSA coverage)

Sources: Ethiopian authorities and IMF staff calculations.

10. Debt risks have materialized despite declines in debt-to-GDP ratios. Total public and publicly guaranteed debt declined by 9 percentage points to 40 percent of GDP in 2022/23 (Text Figure 6). External debt declined by 6 percent of GDP to 18 percent of GDP. Nonetheless, prior to the standstill agreement, external arrears to official creditors accumulated from early 2023 amid acute FX shortages reaching about US$1.2 billion by end-September 2023. The authorities have begun restructuring negotiations with representatives of holders of the Eurobond (for US$1 billion).

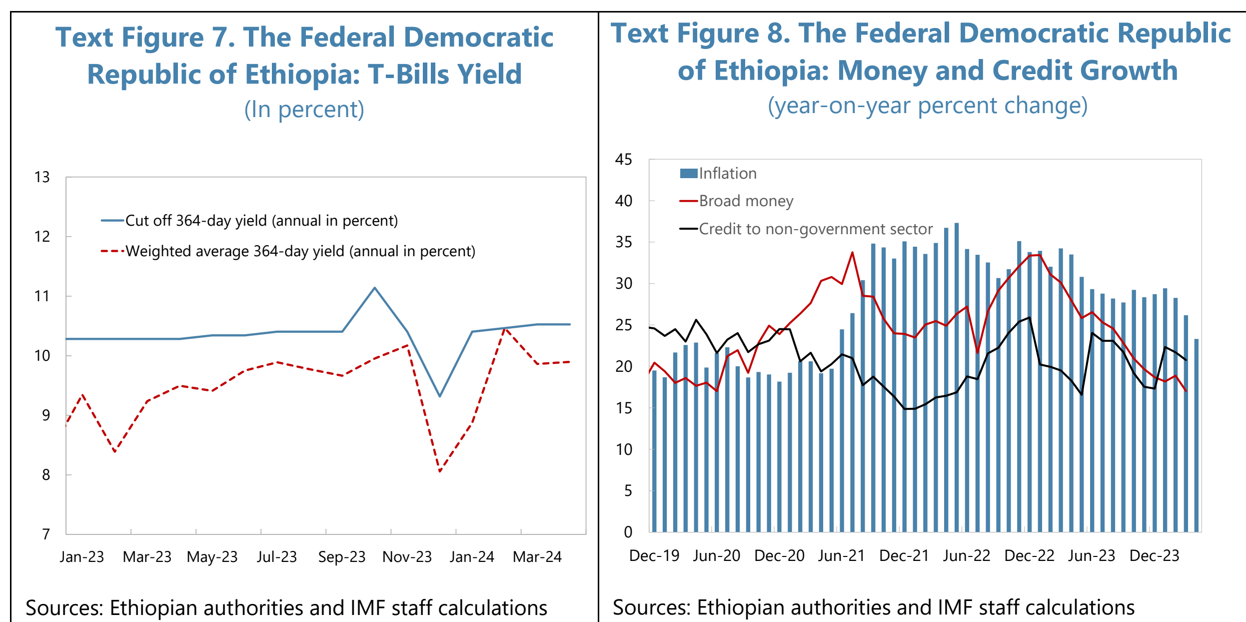
11. In June 2024, the NBE established an interest-rate based monetary framework and announced a target policy rate of 15 percent (prior action), an initial step toward positive real interest rates. To achieve the desired policy stance, the NBE introduced two-week open market

[1] Ethiopian Electric Power (EEP), Ethiopian Sugar Corporation (ESC), Ethiopian Railways Corporation (ERC), Ethio Engineering Group (EEG), and Ethiopian Construction Works Corporation (ECWC).

operations (OMOs) to remove excess liquidity from the banking system and to begin a process of aligning interbank lending rates to the policy rate. To promote monetary policy transmission, the NBE will absorb the full amount banks offer at the policy rate.

12. Demand for T-bills has been muted. The stock of outstanding T-bills has fluctuated around 4 percent of GDP this fiscal year. Tenors are up to one year maturity and with interest rates around 10 percent, well below inflation and private lending rates, auctions have often been undersubscribed (Text Figure 7). Banks report purchasing T-bills only up to the minimum level that enables compliance with regulatory liquidity ratios, while state-managed pension funds with few investment options are the largest holders (with about 65 percent of the total). Banks were also required to purchase 0.4 percent of GDP of 5-year government bonds at 9 percent this fiscal year. In line with the transition to an interest rate based monetary policy framework, T-bill rates will be allowed to move towards the clearing rate set in auctions, and publication of auction results resumed, having been suspended since November 2023.

13. Monetary conditions are tightening in response to policy. NBE advances to the government in the nine months of this fiscal year stand at 0.6 percent of GDP, a significant reduction from 2.4 percent of GDP in 2022/23. In the absence of effective price-based monetary policy tools, the NBE imposed a 14 percent cap on growth in commercial bank lending in August 2023, and tight controls on SOE borrowing continue. Broad money growth slowed to 17.0 percent y/y at end March 2024, well below inflation (Text Figure 8, Figure 1). Liquid assets-to-total liabilities of the banking system was 15.4 percent at end-March, above the minimum requirement, although the ratio of excess reserves or cash to deposits are tight at below 1.0 percent (end-March 2024).



OUTLOOK AND RISKS

14. In the coming years, growth will gradually strengthen and inflation moderate as the gains from macroeconomic reforms firm up. Tightening policies and adjustment will constrain economic activity in the near term (Text Table 1). The benefits of comprehensive reforms, external debt treatment, resumption of external financing, and greater domestic stability will raise growth towards 7.5–8 percent in the medium term. Following the adoption of a market-determined exchange rate, inflation is expected to peak around 30–35 percent in early 2025, but moderate to about 16 percent by 2025/26. The first-round impact of devaluation on consumer price inflation is expected to be relatively limited, given the low share of imports occurring at the official exchange rate in private consumption expenditure, and evidence that consumer prices track the parallel market exchange rate. Implementation of an interest-rate based monetary policy framework and monetary tightening will provide the basis for reducing inflation (domestic credit is expected to decline relative to GDP terms, Table 3b), while a large, temporary fiscal package will help cushion the socio-economic and inflationary impact of the upfront exchange rate reform. Revenue mobilization and reforms strengthening SOE financial health address structural weaknesses that also contribute to BOP vulnerabilities and create space for sustainable priority public expenditure in future.

Text Table 1. The Federal Democratic Republic of Ethiopia: Selected Economic Indicators

	2020/21	2021/22	2022/23	2023/24 IMF Staff Proj.	2024/25 IMF Staff Proj.	2025/26 IMF Staff Proj.	2026/27 IMF Staff Proj.	2027/28 IMF Staff Proj.	2028/29 IMF Staff Proj.
				In percent change, unless otherwise mentioned					
GDP at constant prices (at factor cost)	6.3	6.4	7.2	6.1	6.5	7.1	7.7	8.0	7.8
Consumer prices (period average) [1]	20.2	33.9	32.5	26.9	30.1	16.2	12.2	10.4	9.6
Consumer prices (end of period) [1]	24.5	34.2	29.3	22.9	31.1	13.5	10.9	9.7	9.4
External sector									
Exports of goods and services (U.S. dollars, f.o.b.)	10.9	22.8	3.3	3.9	7.9	15.0	17.3	17.0	7.1
Imports of goods and services (U.S. dollars, c.i.f.)	2.3	24.9	-1.4	1.9	8.7	5.9	10.6	11.8	6.8
				In percent of GDP, unless otherwise mentioned					
External current account balance, including official transfers	-2.8	-4.0	-2.8	-2.6	-4.3	-3.2	-2.5	-2.0	-1.9
Government finances									
Overall fiscal balance, including grants (cash basis)	-2.8	-4.2	-2.6	-1.7	-1.7	-2.1	-2.0	-2.0	-2.0
Total financing (including residuals and excluding net acqusition of assets)	2.8	4.2	2.6	1.7	1.7	2.1	2.0	2.0	2.0
External financing	0.7	0.1	0.3	0.2	1.3	-0.2	0.3	0.3	-0.4
Domestic financing	2.1	4.3	2.5	1.5	0.8	1.5	1.7	1.7	2.4
Primary fiscal balance, including grants	-3.5	-3.5	-2.0	-1.1	-0.6	-0.9	-0.8	-0.7	-0.7
Public debt [2]	56.1	48.9	40.2	34.4	42.9	38.8	35.8	33.6	31.5
Domestic debt	27.1	24.8	22.1	19.1	14.5	12.2	11.4	11.0	11.8
External debt (including to the IMF)	29.0	24.0	18.1	15.4	28.3	26.6	24.5	22.6	19.8
Gross official reserves (in millions of U.S. dollars)	2,866	1,495	1,026	1,011	2,793	5,067	7,012	10,205	11,543
(months of prospective imports of goods and nonfactor services)	1.5	0.8	0.5	0.5	1.2	2.0	2.5	3.5	3.6

Sources: Ethiopian authorities and IMF staff estimates and projections.

[1] The base is December 2016.

[2] Public and publicly guaranteed external debt, which includes long-term foreign liabilities of NBE and external debt of Ethio-Telecom.

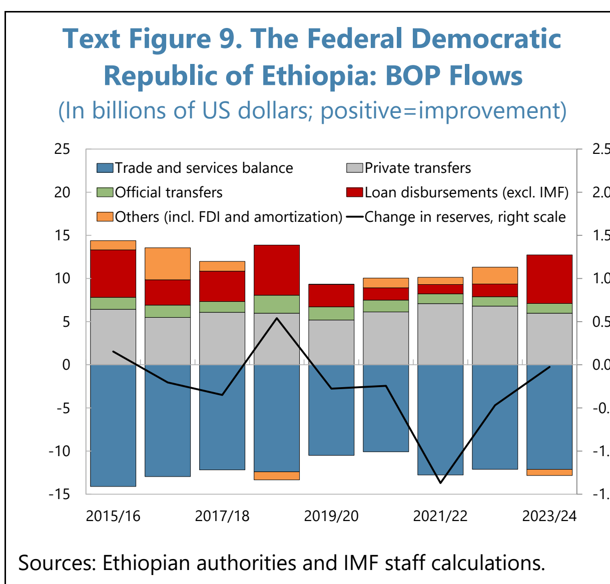
15. The current account deficit is projected to rise as FX availability improves, before stabilizing at around 2 percent of GDP in 2027/28.

- From 10.5 percent of GDP in 2022/23, goods imports are forecast to decline to 8.2 percent of GDP in 2023/24 due to FX shortages (Text Figure 9). Exchange rate reform and increased development partner support will alleviate shortages, leading to decompression in imports after years of restrictions, to a projected 13.6 percent of GDP in 2024/25. Capital goods and "big ticket" inputs for manufacturing and construction that cannot be imported through the parallel market can be expected to rise, and increased externally financed project support will also contribute. Price and substitution effects are expected to lead to a decline in the ratio in the medium term.

- Exports of goods are forecast to decline to 1.7 percent of GDP in 2023/24 (from 2.2), given lower-than-expected coffee and flower exports. Moving to a market-determined exchange rate will reduce incentives for exporters to avoid the official market, and increase investment in export industries, underpinning goods and services exports conservatively forecast at around 10 percent of GDP in the medium term. The outlook for services exports is positive, with strong expected global travel and cargo boosting Ethiopian Airlines.

Text Figure 9. The Federal Democratic Republic of Ethiopia: BOP Flows

(In billions of US dollars; positive=improvement)



Sources: Ethiopian authorities and IMF staff calculations.

- Reserves are expected to fall to 0.5 months of imports by end-June 2024 (US$1.0 billion), before rising to 1.2 months of imports by end-June 2025 (US$2.8 billion). External support, policy adjustment and structural reforms will help bring reserve adequacy to over 3 months of imports by 2027/28.

16. The outlook is subject to significant downside risks, stemming from potential social discontent, security challenges, and global commodity price volatility (Annex III). The baseline scenario is predicated on successful program execution and swift progress in implementing the external debt treatment. Potential exchange rate pressures in the initial stage of adopting a market-clearing exchange rate regime (e.g., driven by the materialization of backlogged FX demand) could generate volatility and impact volumes and market development. Persistent inflation and depreciation expectations could require a stronger policy reaction, while social pressures, policy slippages, or delays in reform implementation are downside risks. Inconsistent implementation or reversal of key fiscal or exchange rate reforms could result in larger financing gaps or withdrawal of development partner or creditor support. Deterioration in the domestic security situation could renew economic disruption and derail international support. Commodity price volatility and intensifying spillovers from regional conflicts also pose downside risks to the outlook.

PROGRAM OBJECTIVES AND POLICIES

17. The authorities' program is based on the HGER and aims to address macroeconomic imbalances, restore external debt sustainability, and lay the foundation for high, private sector-led growth. Comprehensive macroeconomic, structural, and sectoral reforms will stimulate private sector activity and increase the external openness of the economy with a view to promoting higher and more inclusive growth. Key objectives are:

- **Correcting external imbalances.** Moving to a market clearing exchange rate and removing current account restrictions will eliminate exchange rate overvaluation, alleviate acute FX shortages, and remove the key relative price distortion holding back development and causing protracted BOP vulnerabilities. Increased spending on social protection and temporary subsidies will help mitigate the impact on vulnerable households.
- **Developing the monetary policy framework and reducing inflation.** The authorities are adopting an interest-rate based framework and aim to bring inflation down to single digits. Ending monetary financing and financial repression as well as strengthening the role of market forces in the allocation of financial resources are key reforms.
- **Rebuilding revenues and anchoring debt sustainability.** Mobilizing fiscal revenues is critical to sustainably financing social and long-term development spending and will underpin maintenance of low deficits. A CF debt treatment will relieve external liquidity and solvency pressures.
- **Strengthening SOE's financial positions.** SOE reform will remove a key structural driver of BOP debt and fiscal vulnerabilities and strengthen long-term growth prospects. Financial strengthening of CBE has tackled a key macro-financial vulnerability, while governance reforms underpin longer-term financial stability and benefits from financial sector opening. The authorities' privatization plans complement SOE sector reform objectives and contribute, in combination with more focused public investment, exchange rate and fiscal reforms, to the transition to private sector-led growth.
- **Promoting a robust, inclusive, and sustainable economy**, through improving governance, financial inclusion, public service delivery and bolstering climate resilience and food security.

18. The program addresses urgent macroeconomic imbalances and longer-term BOP vulnerabilities. The program and the World Bank's policy agenda complement each other, with World Bank's Development Policy Operations focused on advancing the sustainable transition to a market-based economy, fiscal sustainability, and supporting social resilience and climate action as well as its Financial Sector Strengthening Project, which addresses CBE's governance, role, and long-term viability. The authorities have already taken important steps to tighten the macroeconomic policy stance to contain inflation; the program also envisages terminating monetary financing and interest rates increases. Structural drivers of long-term BOP vulnerabilities will take time to resolve supported by the four-year ECF arrangement.

19. Program preparation has been supported by extensive technical assistance. Fund TA has centered on domestic revenue mobilization and on modernization of central bank operations and structures, including support for the National Medium-Term Revenue Strategy (NMTRS) and the revised NBE Establishment Proclamation (central bank law). TA was also provided to support the adoption of the market-clearing exchange rate regime and the operationalization of NBE's new monetary policy framework. There has also been active engagement in public financial management, including a recent PIMA/C-PIMA, and in most areas of economic statistics.

A. Exchange Rate Policy

20. The authorities are adopting a market-clearing exchange rate regime. Steps taken include: (i) revision of FX regulations consistent with a market-determined exchange rate regime; (ii) preparation of a code of conduct for FX transactions; (iii) determination of a methodology to calculate the reference exchange rate; (iv) development of a communications strategy to support the process of exchange rate unification; (v) implementation of a system to receive real-time data on foreign exchange transactions from market participants (commercial banks and foreign exchange bureaus) to compute the market-determined daily exchange rate; (vi) adoption of a foreign exchange intervention (FXI) strategy; and (vii) development of measures to mitigate the social impact of exchange rate unification (see section C, and Annex IV) (MEFP ¶16). The authorities have not yet announced the move to a market-determined rate or removed critical current account restrictions to unify the exchange rate but will do so as a prior action (MEFP ¶17). Staff will issue a supplement before the Board meeting to provide an update on:

- Publication of a directive announcing that authorized dealers can buy and sell FX from their clients and among themselves at freely negotiated exchange rates. The benchmark exchange rate will be computed as the daily weighted average rate of transactions between authorized dealers and their clients, as well as transactions between authorized dealers themselves. This benchmark will be published daily at the close of the market.
- Removal of current account restrictions, specifically the (i) rationing of FX for imports, and the three-tier priority list of imports; (ii) the minimum import price requirement by the customs authorities for certain imported goods; and (iii) the security deposit requirement of 50 percent when queuing for FX for import payments. Current account restrictions on the outstanding stock of dividends and supplier's credits will be retained temporarily, given the potential to exert sudden pressure on FX demand. The authorities commit to an Article VIII assessment by the Fund before the first review.

21. Surrender requirements for foreign exchange earners will be switched from the NBE to the commercial banks. This is to support efficient foreign exchange pricing by providing liquidity to the interbank market and creating counter incentives to hoarding FX. The surrender rate to the commercial banks is 50 percent, while foreign exchange earners retain the rest. As a transitional measure, foreign exchange earners have one month to use non-surrendered FX before it must be surrendered. This measure will be reconsidered at the first program review with a view to its removal. The exchange rate applicable to the surrender requirement is the prevailing market

exchange rate. The authorities commit to fully eliminating surrender requirements by the end of the program, linked to the development of FX market liquidity (MEFP ¶18).[2]

22. The exchange commission will be reviewed. The authorities maintain an exchange restriction and a multiple currency practice (MCP) subject to Article VIII, Sections 2(a) and 3 arising from a 2.5 percent commission that the NBE requires banks to charge on exchange transactions since May 2, 2022. The NBE requires that the commission be levied on most sales of FX by authorized banks and then transferred to the NBE. Purchase of FX by authorized banks is not subject to the commission. The measure gives rise to an MCP and an exchange restriction.[3] Staff assesses that the commission accounts for a large portion of NBE's operating income and any recalibration should be aligned to NBE's attaining an adequate capital position to ensure that it can meet its policy objectives and ensure its independence. While difficult to ascertain, the economic impact of the commission on FX transactions appears to be limited given the dearth of FX in the market with recent parallel market premiums reported at around 100 percent, although the magnitude of the commission is likely to limit FX market liquidity and development. The authorities will review the commission charged by NBE following the full Art. VIII assessment and take steps to eliminate the exchange restriction and MCP during the program period.

23. NBE will strengthen monitoring and enforcement of banks' daily Net Open Position (NOP) limits to ensure that banks effectively manage FX risks and support inter-bank FX market liquidity (MEFP ¶19). An assessment of all banks' NOPs was completed, and banks will have until June 2025 to eliminate policy-induced, legacy open positions (end-September 2024, structural benchmark). If needed, an additional extension of up to one year will be provided to CBE. To strengthen daily enforcement of NOP limits, NBE will improve the measurement of NOPs, revise the NOP prudential regulation, and redesign the call report to collect more data on banks' FX positions.

24. The NBE adopted a foreign exchange intervention (FXI) strategy (MEFP ¶20). Under the FXI strategy, the NBE can, but is not obliged to, intervene to stem disorderly market conditions. Any FX intervention will be conducted via public auction that satisfy three criteria: (i) all authorized dealers have access to the auction; (ii) no constraints should be placed on bid prices; (iii) and the NBE should make FX allotments solely on the basis of bid prices. During the two-month period immediately after the change of FX regime, the NBE may conduct a limited number of low value FX sale auctions to support price-discovery consistent with the framework. The NBE may also settle letters of credit for fuel imports that fall due in July and August 2024 at the previous day's daily reference exchange rate to facilitate clearance of pre-existing obligations (up to US$670 million).

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[2] The surrender requirement was implemented before the Institutional View took effect. Changes going forward will be assessed by staff.

[3] Under the Fund's new MCP policy, an MCP arose on February 1, 2024, as official action (i.e. the exchange commission) gave rise to an impermissible exchange rate spread as defined in Paragraph 2.g. of Decision No. 17292-(22/63), adopted July 1, 2022).

B. Monetary Policy

25. Monetary policy will anchor inflation and exchange rate expectations with the objective of ensuring price stability over the medium term. Monetary financing of fiscal deficits through direct advances by the NBE (a significant driver of inflation) has been eliminated (quantitative performance criterion, QPC). Regular open market operations (OMO) have begun, at an initial monetary policy rate of 15 percent (prior action), a first step towards reducing the level of financial repression in the economy, and consistent with macro-financial stability. The authorities are committed to further tighten monetary policy as needed to anchor inflation and exchange rate expectations, and to reach a positive real policy interest rate by the first quarter of 2025 (MEFP ¶23), implying further rises will be needed. They will maintain a close dialogue with the IMF on monetary policy, consulting as necessary if inflation deviates substantially from the baseline or in case of unexpectedly large exchange rate movements. Considering transmission may be weak during the initial phase of the new monetary policy regime, additional policy measures (e.g., raising reserve requirements) may be implemented to manage inflation expectations if needed. Fiscal policy and containing SOE borrowing (both large sources of credit demand) will also support tighter monetary conditions.

26. The authorities established a monetary policy committee to recommend the policy stance to the Board of the NBE in June 2024. The committee's formal role will be included in the amendments to the NBE proclamation (discussed below). An emergency liquidity assistance framework will be put in place (structural benchmark, SB, end-September 2024) and a central securities depository will be deployed by end-December 2024 (MEFP ¶22). A review of the reserve requirement framework with a view to simplifying it to improve banking sector liquidity management and improvements to monetary policy analytical capacity will also support the implementation of the new framework.

27. Progressively moving to market-based financing of the government is a critical reform. Steadily reducing financial repression is essential to supporting efficient resource allocation and adequate financing for the private sector, and to containing inflationary pressures. T-bill rates have been allowed to adjust towards market clearing rates set in the auctions, complemented by efforts to promote better market functioning and price discovery through improved auction procedures (MEFP ¶24). Continuing to allow T-bill rates to rise gradually to positive levels in real terms will be an essential signal to reduce financial repression, build policy credibility, attract demand, develop the local currency bond market, and ensure market discipline in public finances.

C. Fiscal Policy

28. The program seeks to strengthen fiscal sustainability and increase space for social and capital expenditure. Over the program period, revenue mobilization will provide resources for raising pro-poor and capital expenditure by about 2 and 1 percent of GDP. To mitigate the impact of the reform program on the vulnerable, a fiscal package of 1½ percent of GDP in 2024/25 will support exchange rate unification (¶31, and Annex IV).

29. Domestic revenue mobilization is a key program objective. The tax-to-GDP ratio will increase by about 4 percentage points by 2027/28. Revenue yields will come primarily from tax reforms with gains from tax administration reforms accruing over time (Text Table 2). Adoption of the NMTRS by the Council of Ministers (SB, end-September 2024) will anchor tax reforms over the course of the program.

Text Table 2. The Federal Democratic Republic of Ethiopia: Revenue Measures in the Program Baseline
(In percent of GDP)

	2024/25	2025/26	2026/27	2027/28
Cumulative tax-to-GDP ratio increase since FY2023/24	**1.0**	**2.5**	**3.5**	**4.0**
XR reform and economic recovery	**0.2**	**0.4**	**0.8**	**1.0**
Tax policies	**0.8**	**2.2**	**2.7**	**3.0**
Direct Taxes	**0.0**	**0.7**	**1.1**	**1.1**
Rationalizing income tax exemptions and holidays (e.g. minimum alternative tax)		0.4	0.6	0.6
Rationalizing PIT regime (increasing exemption threshold)	-0.1	-0.1	-0.1	-0.1
Offsetting measures (witholding rate on interest income, taxes on inheritances and gifts)		0.1	0.1	0.1
New property tax regime	0.1	0.2	0.3	0.3
Motor vehicle circulation tax	0.0	0.1	0.2	0.2
Indirect Taxes	**0.8**	**1.5**	**1.7**	**1.9**
VAT	**0.3**	**1.0**	**1.0**	**1.2**
VAT: base broadening under 2024 VAT Proclamation and removal of exemptions		0.5	0.5	0.7
VAT on fuel		0.5	0.5	0.5
Excise	**0.4**	**0.4**	**0.9**	**0.9**
Excise stamp	0.3	0.3	0.3	0.3
Revision of excise rates		0.1	0.2	0.2
Telecom	0.1	0.1	0.1	0.1
Fuel			0.3	0.3
Social welfare duty	0.1	0.1	0.1	0.1
Surtax on imports			-0.3	-0.3

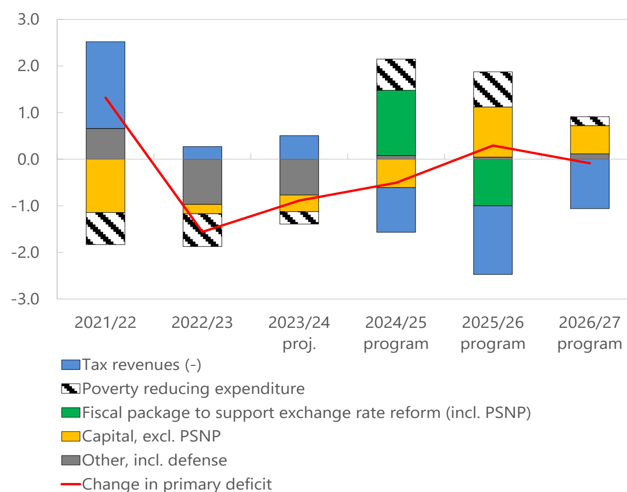
30. Introduction of an excise stamp and modernized VAT regimes (prior actions), together with windfall tax revenue gains from exchange rate will raise tax-to-GDP ratio by 1 percentage point in 2024/25 (**MEFP ¶33).** Rollout of the excise stamp and adjustment of specific rates on alcohol and tobacco will improve revenue tracing and compliance. The new VAT Proclamation, recently tabled for discussion in Parliament, maintains a uniform 15 percent tax rate and removes wide-ranging exemptions on products that are not heavily consumed by low-income groups. The authorities are advancing the rollout of the new Real Estate Tax Proclamation, that they expect will yield an additional 0.1 percent of GDP starting in 2024/25.

31. Policy changes to increase revenues from income taxes, VAT, and excise will sustain revenue mobilization during the program. These will include: (i) introducing a minimum alternative tax to help address gaps in the corporate tax base, while streamlining and reducing revenue losses from exemptions and tax holidays; (ii) reform of the presumptive tax regime, (iii) nationwide rollout of the real estate property tax and introduction of motor vehicle circulation tax; and (iv) full implementation and inclusion in budget revenues of the fuel excise and VAT regime following unwinding of the temporary fuel subsidy. Personal income tax thresholds will be updated (the lower threshold has fallen below the poverty line) and the bracket structure streamlined, complemented by compensatory measures increasing withholding rates and new taxes on nonwage incomes. The authorities have requested capacity development support to design policies to: (i) raise revenues from agricultural taxation while protecting low-income farmers; (ii) strengthen the income tax regime, in line with NMTRS; and (iii) develop tax rules for capital market operations (MEFP ¶34). The authorities intend to reduce reliance on trade tariffs as a source of tax revenue over the medium term. The next TADAT Assessment, currently planned for 2025, will assist in identifying the gaps and facilitate the designing and prioritization of tax administration reforms.

32. A fiscal package will mitigate the inflationary and socio-economic impact of the exchange rate reform. A total spending package of about 1½ percent of GDP will be implemented in 2024/25 (Annex IV; MEFP ¶35). Expanding the targeted cash-transfer program (the Productive Safety Net Program, PSNP) by 0.4 percent of GDP will ensure expansion in the most cost-effective and efficient way to support vulnerable people. Additional resources for PSNP will be provided by World Bank social safety net project financing (0.2 percent of GDP) and help cover the gaps in donor financing for the next 18 months. This will be complemented with a package of temporary subsidies that will be phased out during FY2024/25 and will include subsidies on: (i) fuel (0.5 percent of GDP); (ii) select food items and medicines to allow for lags in the adequate expansion of PSNP (up to 0.2 percent of GDP); and (iii) higher fertilizer subsidies (an increase of 0.2 percent of GDP) to limit the impact on smallholders. In public transport, the current scheme of targeted interventions based on rebates through mobile payments will be preserved. The authorities also intend to increase public sector wages within the current spending envelope to partly offset significant erosion in purchasing power over the last years that have left the lowest earning public servants below the poverty line.

Text Figure 10. The Federal Democratic Republic of Ethiopia: General Government Fiscal Impulse

(In percent of GDP, contribution to fiscal impulse)



Sources: Ethiopian authorities; IMF staff estimates.

Note: FY2024/25 primary balance includes 0.7 percent of GDP DPO grant.

33. Pro-poor spending will grow over time.[4] The program envisages a near doubling of pro-poor spending from 2½ to 4 percent of GDP over the program, bridging part of the gap with peers (MEFP ¶37). In addition, a large and durable expansion of the safety net is envisaged through the government's contribution to the PSNP increasing from 0.1 to 0.4 percent of GDP starting in 2024/25 (indicative target, floor). As the cost-of-living shock abates, PSNP will concentrate on poverty reduction.

34. A gradual general government primary deficit reduction of 0.4 percentage points of GDP during the program period will reinforce the significant consolidation already underway. The package of measures to mitigate the impact of exchange rate reform temporarily widens the

[4] For the purposes of the program, pro-poor spending will be defined as the sum of federal government recurrent spending in basic services (education, health, agriculture, water, and roads), federal government capital spending in education and health, and general-purpose grants from the federal government to regions. The latter is included as sub-national levels of government have committed to allocate at least 60 percent of their spending to basic services in the context of the World Bank ESPES Program. The authorities' federal budget presentation includes PSNP under capital spending, as it was designed primarily as a public works scheme.

overall deficit, excluding budget grants, by 0.7 percent of GDP in 2024/25 (half of the fiscal package cost). An increase in domestic interest payments from 0.5 to over 1 percent of GDP over the program is driven by (i) gradually rising effective interest rates for domestic public borrowing as market-based financing becomes more predominant; and (ii) the costs of debt issued for recapitalization of CBE. Removing exchange rate distortions and gradually reducing financial repression will lead to additional consolidation of off budget and net quasi-fiscal operations estimated at about 2⅓ percentage points of GDP (Annex V).

35. Public investment reforms will focus on strengthening institutional frameworks, including for climate change. Promoting sustainably financed investment in public infrastructure will build on addressing institutional gaps to enhance efficiency and the growth impact of capital budgets, which will remain lower than in previous decades. This will entail a thorough review of the existing public investment pipeline, identifying low value projects to be canceled, and the room for new, higher priority projects in the future. The recent PIMA/C-PIMA will guide comprehensive reforms to close institutional gaps in (climate-aware) public investment planning, allocation, and implementation. The findings will, for example, help clarify the allocation of public investment-related responsibilities within the PIM framework, including project appraisal, selection and maintenance practices, medium-term planning and budgeting, and implementation. The authorities plan to strengthen public-private partnership risk oversight in anticipation of an expanding portfolio of these projects; improve climate hazard identification and preparedness for public infrastructure management; and ensure coordination in the development of information management system. With limited fiscal space to meet post-conflict recovery and reconstruction needs, the authorities are seeking to mobilize resources from developmental partners and the private sector and have set up a multi-donor trust fund with World Bank support.

36. Fiscal transparency and monitoring of fiscal risks will be improved. Guided by Fund TA, the authorities intend to prioritize compilation, reconciliation, and reporting practices to improve compliance with GFSM2001/2014 (MEFP ¶39). Implementation of the 2019 Public Expenditure and Financial Accountability recommendations will strengthen transparency of public finances, which will include publication of monthly budget execution and mid-year review reports, and disclosure of extrabudgetary unit operations. The introduction of a public sector obligations framework for SOEs, supported by the World Bank, is an important step toward a comprehensive disclosure of quasi-fiscal activities and fiscal risk management (see below). Starting in 2024/25, fuel subsidies will be fully reflected as budgetary spending (MEFP ¶36). The authorities will settle legacy liabilities of the Fuel Price Stabilization Fund, and guided by future Fund TA, develop a strategy to rebuild buffers in the Fuel Price Stabilization Fund.

37. If fiscal risks materialize, authorities will sustain the primacy of the program's macroeconomic stabilization objective. If tax revenue targets fall out of reach, the authorities intend to step up efforts to broaden the tax base, identify new policy measures, and accelerate administration reforms. The authorities will safeguard social safety net spending. Higher interest cost from T-bills resulting from a tighter-than-expected monetary stance or market-determined rates may require further prioritization in spending. Margins of adjustment will include containing capital

and recurrent spending in lower-priority categories, and some room to accommodate higher deficits if financing is available, observing program commitments on ending monetary financing.

D. State-Owned Enterprise Reform

38. Institutional reform and financial strengthening of SOEs are a key focus of the authorities. The new Public Enterprise Law (January 2024) lays out comprehensive legal foundations for strengthening SOE oversight, professionalization of corporate governance, financial reporting, state-ownership, and SOE public service obligations. The Ethiopia Investment Holdings (EIH) and Public Enterprises Holding and Administration Agency (PEHAA), in their roles as commercially oriented shareholders on behalf of the state, are mandated to drive reforms to ensure cost efficiency, good corporate governance, and transparency across the SOE sector.

39. Financial reporting and SOE fiscal risk management and oversight will be strengthened (MEFP ¶46). PEHAA and EIH have made progress in addressing delays in preparing SOE audited accounts and improving IFRS compliance. The authorities aim to promptly publish 2022/23 IFRS-based and audited financial statement for critical SOEs (SB, end-September 2024). To ensure robust centralized fiscal oversight, the Ministry of Finance SOE Unit is developing comprehensive digital reporting systems to monitor SOE sector financial flows, quasi-fiscal operations, contingent liabilities, and fiscal risk management. PEHAA and EIH will implement centralized investment planning and dividend policy oversight, while maintaining tight limits on SOE borrowing, which occurs with state guarantees (indicative target). Borrowing limits are reinforced by stronger prudential regulation and CBE governance reform (supported by the World Bank), will enhance SOE financial discipline, and prevent the reemergence of SOE-driven financial fragilities.

40. Power sector reforms will restore financial sustainability, reduce fiscal costs, and improve efficiency and access to electricity over the course of the program (**MEFP ¶48).** Achieving cost recovery in the power sector will reduce a key fiscal, financial stability, and growth risk. Adoption by the Council of Ministers of a four-year electricity tariff adjustment plan is the first step to reaching cost recovery within the program horizon, and the first tariff increase is expected by end-September 2024 (SB). The authorities are committed to power sector reforms backed by US$1.6 billion World Bank project lending for transmission and distribution investment to improve access to electricity.

41. The authorities will develop a strategy to address financial vulnerabilities and fiscal risks emanating from the Ethiopian Railway Corporation (MEFP ¶48). The reforms include streamlining fragmented infrastructure management and operations and allowing private sector participation in management and operations. The legal framework for the liberalization of key logistics sub-sectors (dry port, freight, and logistics services) will be finalized by 2026.

42. The sugar sector privatization process has been relaunched. The authorities intend to finalize the bid process and transfer ownership in 2025, to attract private sector investment to the sugar industry and help recoup the large public investments in the sector (MEFP ¶48).

E. Financial Sector

43. Strengthening of CBE's capital has addressed an important macro-financial vulnerability. CBE is the largest bank (58 percent of banking system assets) and was historically heavily exposed to non-performing SOE debt. With World Bank support, the authorities have taken decisive steps to financially strengthen CBE and address legacy issues related to its role in SOE lending, including FX exposures (MEFP ¶49). A capital injection of 870 billion Birr (using government securities) has enabled CBE to write off all claims on LAMC, fully provision claims on EEP, and bring CBE's capital adequacy ratio up to the regulatory minimum (prior action). The World Bank's Financial Sector Strengthening Project (FSSP, US$700 million) will be used for recapitalization and continued support of the reform and restructuring of the bank. This will include a focus on governance and risk management, including CBEs ownership policy, mandate, and business plan to ensure CBE can compete as a sound, viable, and commercially oriented bank at arms-length from the government as the financial sector is opened. The FSSP also includes conditionality on strengthening banking supervision and key regulations, including asset classification, the treatment of non-performing government guaranteed claims, and foreign exchange exposures.

44. Continued strengthening of banking regulation and supervisory capacity are important for financial sector stability and development. Fund TA has focused on implementing risk-based supervision, supervisory manuals and processes, upgrading the capital framework to Basel II/III, enhancing asset classification, and provisioning requirements, and increasing supervisory capacity on IFRS 9. Continued efforts toward improving the measurement of FX exposures and priorities related to financial sector opening, including stress testing, licensing, and the regulatory framework for mobile money institutions are also needed.

45. Developing a sustainable funding model for the Development Bank of Ethiopia (DBE) and unwinding of financial repression will support financial sector growth and efficiency. Phasing out mandatory purchase of DBE and five-year government bonds will remove a significant distortion in the allocation of financial resources (MEFP ¶44). DBE will continue to rely on development partner funding for on-lending to small and medium enterprises, complemented with market-based bond financing as domestic capital markets develop. The preferential inclusion of T-bills in CBE's reserve requirement calculation will also be phased out.

F. Debt

46. Ethiopia's debt is unsustainable and in distress. Debt sustainability will be restored with the successful completion of debt treatment and reform agenda. Debt carrying capacity (DCC) is classified as weak (see Debt Sustainability Analysis). In relation to the debt thresholds for weak DCC, there are protracted breaches of the exports-related indicators (PV of external debt-to-exports and external debt service-to-exports ratios) and the external debt service to revenue ratio. The PV of external debt to GDP ratio remains below the threshold for the entire projection period. All the external debt risk indicators exceed their thresholds for a protracted period under the most extreme shock scenario. The combination of prudent macroeconomic policies, fiscal and debt conditionality,

improved SOE governance, and the debt treatment would all contribute towards reducing debt vulnerabilities. There is a risk that a drawn-out debt restructuring process slows the reduction of debt vulnerabilities.

47. The debt treatment will help bring the risk of debt distress rating to moderate by the end of the program. Restoring debt sustainability would entail: (i) reducing external debt service to 14 percent of revenues and 10 percent of exports, and the present value of external debt to 140 percent of exports by program end; and (ii) maintaining these indicators at or below these thresholds in the post-program period. The debt treatment will contribute US$3.5 billion to covering the financing gap through lower debt service during the program. Debt treatment will be achieved through the CF arrangement with official creditors and through an agreement on comparable terms with external commercial creditors.

48. The standstill agreement with the OCC members provides significant temporary relief. Staff forecasts incorporate reprofiling of debt payment of US$2.5 billion due to all the official bilateral creditors in 2023 and 2024, following the term sheet of the standstill.

49. The authorities will limit the accumulation of new debt vulnerabilities (MEFP ¶42). New external borrowing will be limited to concessional debt, with a zero ceiling on contracting and guaranteeing new non-concessional debt (continuous performance criterion). The pace of contracting new public and publicly guaranteed (PPG) concessional debt will be underpinned by a ceiling on the present value of new external borrowing (indicative target). The authorities requested one exemption from the zero-limit on new non-concessional borrowing for the completion of the final phase of Koysha Hydroelectric Dam project (US$950 million), for which concessional financing is not available (Box 1). The project is integral to the authorities' development program given its potential to generate export revenues, support rural electrification, and contribute to climate change mitigation.

50. Non-market-based financing of the public sector is being phased out gradually, while considering fiscal sustainability (MEFP ¶44). Besides the elimination of monetary financing of fiscal deficits, the mandatory purchase of 5-year treasury bonds at a fixed interest rate of 9 percent by commercial banks will be phased out by end-June 2025, with an intention to develop the market for longer-dated government securities. Mandatory purchase of DBE bonds by financial institutions will be phased out before the fifth review of the program. The authorities conducted a voluntary exchange of the current stock of T-bills held by Public Servants Social Security Agency and the Private Organizations Employees' Social Security Administration for long-term securities. The exchange provides the pension funds with assets that better match the duration of their liabilities and provide a return expected to keep pace with medium-term inflation, while providing debt service relief to the Treasury in the near term. Going forward, the pension funds will participate freely in T-bill and bond auctions helping determine market-based interest rates; the authorities will inform Fund staff before taking any action to roll over or restructure public sector liabilities at rates below contemporaneous T-bill rates, including the T-bill exchange noted above.

51. The strengthening of debt management and transparency is underway. A medium-term debt management strategy will be developed by the end of 2024/25 with TA support from the Fund (MEFP ¶45). The public debt bulletin now includes government guaranteed DBE bonds.

G. Safeguards and Business Environment

52. The program will support the authorities' efforts to reform, modernize, and strengthen NBE. Based on recent TA, NBE is preparing comprehensive amendments to the NBE Proclamation, with respect to mandate, decision-making structure (internal checks and balances and collegial decision-making), accountability, external audit, transparency, and autonomy, and will submit draft legal amendments to Parliament (SB, end-December 2024) with a view to parliamentary approval by end-March 2025 (MEFP ¶26). To strengthen financial autonomy and capacity to implement policy, the next step will be to conduct an assessment of the balance and the appropriate level of "policy capital" required to conduct monetary policy and successfully maintain low inflation (MEFP ¶27).

53. Building on progress in strengthening the AML/CFT legal framework, the authorities will intensify efforts to improve its effectiveness to tackle and deter financial crimes. In collaboration with the Fund, they plan to integrate AML/CFT measures into capacity development initiatives. In preparation for the upcoming FATF 5th round assessment, they have requested Fund TA to help strengthen supervision of both financial and nonfinancial sectors and enhance timeliness and quality of financial intelligence.

54. Addressing safeguards assessment recommendations is a priority. To advance long-overdue recommendations of the 2020 safeguards assessment in a very constraining legal environment, NBE will adopt a selection and rotation policy for an external auditor, the Federal Auditor General has authorized NBE to be audited by a suitably qualified external audit firm, and NBE will float competitive bid to conduct audits starting with the 2022/23 financial statements (prior action). NBE's audited financial statements for 2020/21–2022/23 will be finalized and published (SB, end-December 2024). An update safeguards assessment will be undertaken before the first review.

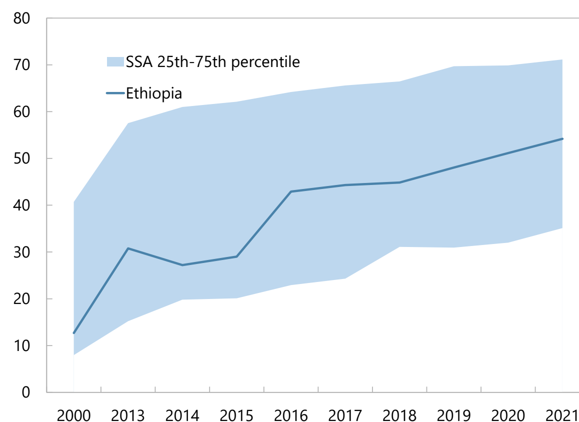
55. The broader agenda for private sector development is advancing. Homegrown Economic Reform Agenda 2, about to be launched, retains the objective of enabling private sector-led development, with reforms in the following areas:

- *Opening of the economy to private investment.* The draft of a new banking law allowing foreign banks to operate was submitted to the Council of Ministers in June, a securities exchange is set to be launched by the end of 2024, and a range of sectors including retail and wholesale trade, logistics, energy, and mobile financial services are being opened to domestic and/or foreign investment.
- *Removing barriers to international trade.* Ethiopia is preparing to apply to join the WTO and is implementing steps for full participation in the African Continental Free Trade Area and other regional trade arrangements, including by an overhaul of tariff lines.

Box 1. The Koysha Hydroelectric Project

The Koysha project will generate 1,800 MW of power, equivalent to 40 percent of the current capacity. The project commenced in 2016 with non-concessional financing secured through loans totaling approximately 340 million Euros from three banks, backed by the Italian export credit guarantee agency, SACE. After reaching 66 percent completion, a lack of external financing has led to delays. The estimated shortfall is 879 million Euros, and the authorities have not succeeded in securing concessional loans. Completion is projected to require an additional 3–6 years.

Koysha aims to improve access to electricity and support rural electrification. Per capita electricity consumption is 140 kWh per year, only 5 percent of the global average of 33,131 kWh. As of 2020, only 51 percent of Ethiopians have access to electricity, leaving nearly 57 million people, primarily in rural areas, without this essential service. The project is a critical part of the National Electrification Program that aims to provide adequate, affordable, and reliable electricity to all.



Source: World Bank.

Koysha is expected to generate export revenues. In FY2021/22, Ethiopia exported electricity valued at US$93 million to Sudan and Djibouti (2.3 percent of total goods exports, while the volume of electricity exports represents 11 percent of total generation). A 25-year power purchase agreement with Kenya to export up to 600 MW of electricity, which Koysha is intended to supply, will earn around about US$100 million annually. The increase in electricity exports has the potential to improve the debt outlook, as the narrow export base and low overall exports currently constrain debt service capacity. Existing transmission lines can accommodate increased exports, including a World Bank-funded 2,000 MW Ethiopia-Kenya line. Ethiopia is the center of the East Africa power pool and exports are critical for the regional demand-supply balance, meeting growing demand with clean energy, and adapting to climate-induced hydrology variations.

Koysha will strengthen climate resilience by reducing use of biomass fuels. Biomass is the main source of energy in much of rural Ethiopia, resulting in deforestation, soil erosion, land degradation, adverse changes in natural habitats, and loss of biodiversity. Increasing access to electricity for rural households can help stop environmental degradation through deforestation and conserve the fertility of soils.

Securing external financing and resuming construction are crucial to avoid incurring contractual penalties due to delays, potential termination, and overall construction cost increases. The contractor of the project has claimed prolongation costs. These continue to escalate until construction resumes. The contractor can also terminate the contract, underscoring the urgency of securing necessary funding to prevent major setbacks. World Bank supported reforms to the electricity tariff framework and a new four-year tariff plan are expected to support the financial viability of Koysha through achieving cost recovery tariff levels across the industry.

The government has approached bilateral and multilateral partners to fill the financing gap, but no concessional finance has yet been mobilized. The government has also tried directly negotiating with equipment suppliers to provide concessional discounts, but this has also been unsuccessful.

- *Improving the regulatory environment and supporting competition.* The trade registration and licensing system will be fully digitalized, the trade and consumer protection law will be revised, and a framework for public-private dialogue will be institutionalized.

56. Strengthening the quality and frequency of economic statistics is a priority. The Ethiopian Statistical Development Program adopted in December 2023 aims to strengthen data collection and processing to improve economic data available to the public. The need to address shortcomings in national accounts statistics is particularly pressing, given poor source data, an outdated base year, and lack of expenditure in volumes. Ethiopia has not been compiling quarterly GDP, which is critical for policy making. The diagnostic of national account statistics planned to be completed by December 2024, with the support of IMF TA, will be a first step, helping to develop a timeline to produce and publish quarterly and annual GDP by production and expenditure and conduct a rebasing (MEFP ¶56). In addition, addressing shortcomings in external sector statistics, particularly aligning with BPM6 methodology and collecting data on foreign direct investment is important. IMF TA is ongoing with the first mission in over five years recently underway, and implementing its recommendations will be crucial to closing data gaps and improving the quality of BOP data and compiling international investment position (IIP data) and external debt statistics for the first time.

PROGRAM DESIGN

57. The ECF arrangement is expected to catalyze external financing from multilateral and official bilateral partners and creditors and increase reserves to an adequate level. The program envisages ambitious FX, monetary, and fiscal measures, which, with prospective donor financing and debt treatment, will help close the BOP gap. The residual external financing gap, anchored on bringing reserve adequacy to 3.5 months of import coverage by the end of the program period, is estimated at US$10.7 billion until 2027/28, of which about US$4.4 billion in 2024/25 (Text Table 3). A portion of the Fund disbursements in the first year of the program (30 percent or 16 percent of the total program disbursement, SDR 421.73 million) would be used for budget support to ensure non-inflationary financing of the budget, including social spending in the context of exchange rate reform.

58. The program envisages equal burden sharing of the financing required from the Fund, development partners and the Common Framework debt treatment (Text Table 3). The estimation assumes that the Eurobond will be restructured. Privatization proceeds are assumed at US$650 million in 2025/26. Expected privatization proceeds are in line with the authorities' privatization agenda and assumed amounts are conservative compared to the asset valuations. Official transfers are projected to gradually rise to US$1.7 billion over the medium term, from US$1.1 billion in 2023/24, with continuous support from multilateral creditors. US$2.5 billion of financial support is envisaged around program approval, with Fund contributing US$1 billion and the Bank providing US$1.5 billion. The Bank has provided firm commitments for Development Policy

Operations totaling US$2.5 billion between July 2024 and July 2025. With this commitment, as well as the progress towards debt restructuring through Credible Official Creditor Process under the CF, there are firm commitments of financing for next 12 months and good prospects for financing the remainder of the program.

Text Table 3. The Federal Democratic Republic of Ethiopia: External Financing Requirements, 2023/24–2027/28

(In USD millions)

	2023/24	2024/25	2025/26	2026/27	2027/28	Cumulative
External financing requirement	9,692	13,146	10,646	9,594	10,373	53,450
External financing sources	6,417	6,469	6,180	6,576	7,460	33,102
Financing gap (need for financing +)	3,275	6,676	4,466	3,018	2,913	20,347
Expected financing	3,275	2,257	2,309	1,314	536	9,691
Official transfers	1,139	1,401	1,567	1,653	1,701	7,462
Privatization proceeds	0	0	650	0	0	650
Reprofiling of external sovereign deposits at NBE, 2020[1]	*288*	*0*	*0*	*0*	*0*	288
Standstill agreement with Official Bilateral Creditors [2]	*1,815*	*856*	*92*	*-339*	*-1,165*	1,258
Accumulation of arrears	*33*	*0*	*0*	*0*	*0*	33
Residual gap	**0**	**4,419**	**2,157**	**1,704**	**2,376**	**10,656**
IMF	0	1,870	511	512	513	3,406
Disbursements	0	1,870	511	512	513	3,406
Prospective debt restructuring	*0*	*1,050*	*646*	*491*	*1,313*	3,500
Prospective budget support	0	1,500	1,000	700	550	3,750

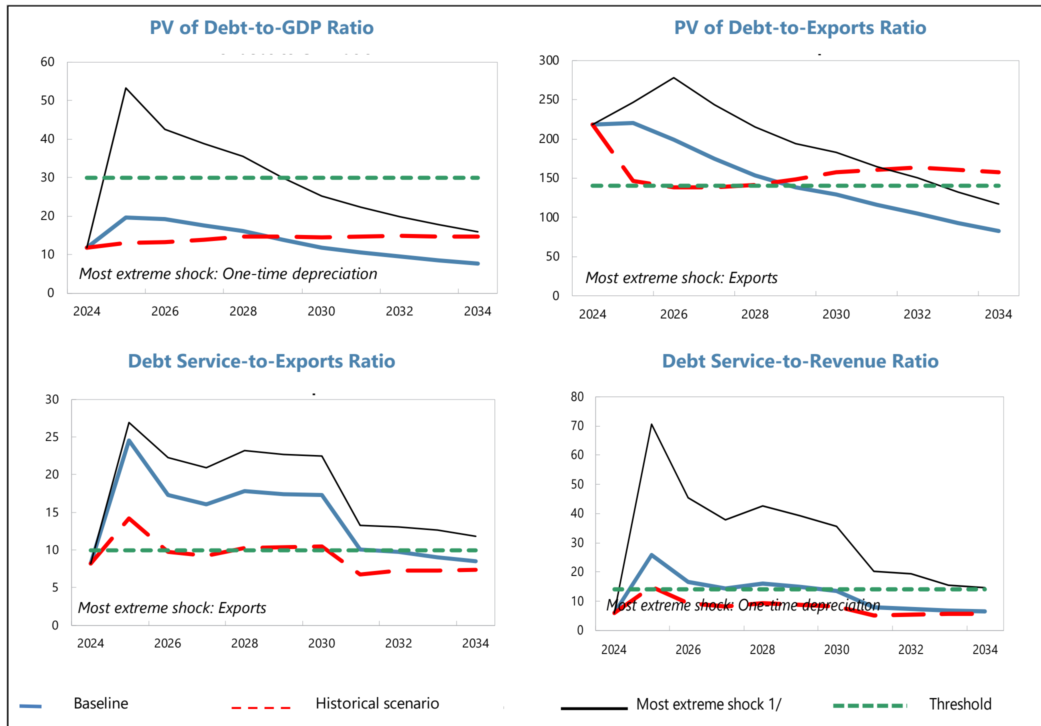
Sources: IMF staff projections and estimates.

1. Represents reprofiling that was finalized under the previous ECF/EFF program and through recent negotiation.
2. Represents standstill agreement with official bilateral creditors as for debt service falling due in CY2023 and CY2024 (staff estimate).

59. Total access requested is SDR 2,555.95 million (850 percent of quota). The authorities request a front-loaded disbursement of 30 percent of the total at program approval to support upfront exchange rate unification by strengthening the NBE's credibility and providing an adequate cushion to manage exchange rate volatility. A well-designed FXI strategy will avoid Fund resources financing capital flight. The provision of budget support will support the elimination of monetary financing and the transition to positive real interest rates.

60. The authorities are seeking a debt restructuring to ensure the program is fully financed and to improve the risk of debt distress to "moderate" by the end of the program. Debt relief is needed during both the program and post-program periods, mainly to eliminate protracted breaches in the exports-related debt vulnerabilities indicators. The illustrative debt restructuring scenario incorporates the temporary debt service suspension granted by all official bilateral creditors (Text Figure 11). Debt service relief of US$2.4 billion is assumed in 2023 and 2024 through the debt service suspension, to be succeeded by the full debt treatment consistent with Fund program parameters. Suspended debt service will be repaid between 2027/28 and 2029/30, in line with the term sheet of the standstill. Deposits made at NBE by foreign partners have been used to support the BOP and are categorized as debt, in line with the treatment of similar deposits in the past.

Text Figure 11. The Federal Democratic Republic of Ethiopia: Illustrative Debt Restructuring Scenario–Indicators of PPG Debt, 2023/24–2033/34



1/ The most extreme stress test is the test that yields the highest ratio in or before 2034.
Source: IMF staff projections based on LIC DSF.

61. The authorities have engaged actively with Eurobond holders on the need for debt restructuring on comparable terms to the official creditors. Ethiopia has outstanding arrears to Eurobond holders of US$33 million as of end-May 2024. The authorities have appointed legal and financial advisors and have opened negotiations with representatives of Eurobond holders. During a meeting with bondholders in December 2023, the authorities conveyed their commitment to acting transparently and in good faith. Staff assess that the authorities are making good faith efforts to agree terms with Eurobond holders, as required under the Fund's lending into arrears policy in case of arrears to private creditors. Staff will continue to monitor evolving relations with these creditors. Staff also assesses that adequate safeguards remain in place for the use of Fund resources, and Ethiopia's adjustment efforts are not undermined by developments in creditor-debtor relations.

62. The OCC debt service suspension resolves external arrears to official creditors accumulated from early 2023, with the suspension retroactive to January 1, 2023. Ethiopia has pre-HIPC era arrears to Libya, Russia, and the former Republic of Yugoslavia, totaling about US$525 million as of June 2023, which are deemed away. Furthermore, there are about US$15 million in external arrears to commercial creditors from the former Czechoslovakia, India, Italy, and the former Yugoslavia, all pre-dating the 1990s, and authorities are making good faith efforts to resolve these arrears.

63. Staff assesses that there are sufficient assurances regarding the debt restructuring needed to restore debt sustainability. This judgement is based on the key milestone reached under the Common Framework process involving the Paris Club, a credible official creditor process.[5] In particular, the OCC (co-chaired by China and France) meeting on July 11 confirmed a common understanding (on the basis of a working paper) on Ethiopia's macroeconomic challenges, its current debt situation, and the scale of debt relief that will be needed to restore debt sustainability and fill the financing gap, providing the necessary financing assurances.[6] The authorities are committed to reaching an agreement with official creditors on a debt treatment in line with program parameters and to making progress toward reaching agreement on comparable terms with other creditors by the time of the second review.

64. Financing assurances reviews will continue to be conducted at each review of the ECF arrangement until all external arrears are cleared.

65. Staff assesses all Poverty Reduction and Growth Trust (PRGT) exceptional access criteria to be met based on financing assurances from development partners, and from official bilateral creditors for a debt treatment under the CF, an assessment of moderate risk of debt distress by the end of the program, and the authorities' commitment to the program.

- *Criterion 1 (exceptional BOP pressures):* Ethiopia is experiencing exceptional BOP pressures, with extremely low reserves, widespread FX shortages, exchange rate overvaluation, and is in external debt distress.
- *Criterion 2 (debt sustainability with high probability):* A combination of strong policies and financing from sources other than the Fund, including via the treatment of official bilateral debt under the CF and application of comparability of treatment to non-official debt, would secure sustainability with high probability by improving the debt distress rating to moderate by the end of the program. There are good prospects for a successful debt restructuring in line with program parameters. The OCC signaled commitment to providing an appropriate debt treatment in accordance with the G20 CF.
- *Criterion 3 (income criterion for presumed blending):* At about 74 percent of the IDA Operational Cut-off, Ethiopia does not meet the income criterion for presumed blending and is thus eligible for PRGT exceptional access.
- *Criterion 4 (reasonably strong prospect of program success):* The envisaged frontloaded policy adjustments, including a strong set of prior actions, and the authorities' established commitment to program implementation would provide a sufficient basis for a favorable assessment of a strong prospect of success. The implementation of prior actions demonstrates strong program ownership.

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[5] As established in the recently adopted "Policy Reform Proposals to Promote the Fund's Capacity to Support Countries Undertaking Debt Restructuring", April 2024. See in particular paragraph 31.

[6] Going forward, this key milestone would satisfy as an indication that financing assurances have been received under the Common Framework (when it involves the Paris Club). The track record of the Paris Club, including when it is involved in the Common Framework, supports such an approach.

66. Staff assesses that the criteria under the Policy Safeguards on High Combined Credit (PS-HCC) are also met. Because Ethiopia has outstanding obligations to the GRA, the proposed access will entail levels of combined PRGT and GRA credit above the applicable limits, thereby triggering the PS-HCC. In line with staff's judgment on PRGT exceptional access criteria 1, 2 and 4, staff assesses that the three criteria under the PS-HCC are also met.

67. The program will be monitored via quantitative targets and structural benchmarks, with seven prior actions (Tables 9–10). The program will be monitored on a quarterly basis for the first and second review to maintain close engagement during heightened uncertainty, after which reviews would be semi-annual with end-June and end-December test dates, consistent with the authorities' budget cycle.

68. Ethiopia's capacity to repay is considered adequate, predicated on successful program implementation, securing financing assurances and debt restructuring, but substantial downside risks remain. The program request triggers enhanced safeguards for capacity to repay.

- The outstanding stock of Fund credit would peak at 18.8 percent of exports, 76.4 percent of FX reserves, and 1.9 percent of GDP. Debt service to the Fund is projected to peak at 2.5 percent of exports, 8.3 percent of FX reserves, and 0.2 percent of GDP. Most capacity to repay indicators remain within the range of past PRGT UCT-quality arrangements (Figure 2). However, as a percent of international reserves, total Fund credit will be above the 75th percentile due to the initially low level of reserves. Reserve accumulation during the program will put the ratio on a firm downward path. Risks to CtR rise towards the end of the ten-year horizon when repayments to the Fund peak and rescheduled debt service payments recommence. Reflecting Ethiopia's low quota, access—at around 2.0 percent of GDP—is similar to that at the time of the 2019 ECF/EFF and lower than that of all the other PRGT exceptional access cases except one.
- Downside risks include derailment of international financial support due to the security situation, failure of exchange rate reform, further falls in international reserves, and protracted debt negotiations. Risks are mitigated by the authorities' commitment to reforms, their track record of servicing debt obligations to the Fund, and measures under the program including the CF debt treatment along with adequate reserve accumulation.

69. Ethiopia's debt owed to international financial institutions represents about 54 percent of total external PPG debt as of end-June 2023. This is below the average ratio of multilateral to total external PPG debt in LICs. The World Bank alone represents about 76 percent of multilateral debt (41 percent of external PPG debt), reflecting uninterrupted project financing through IDA.

70. The Fund faces significant enterprise risks.

- Credit risks arise as capacity to repay is subject to substantial downside risks. Obligations to the Fund, as percent of reserves, peak at 8.3 percent of gross international reserves at the onset of the program reflecting repayment of existing credit. Reserve accumulation under

the program would clear this risk after just one year. Short-term risks stem from frontloaded disbursements, low international reserves, the risk of policy reversals and possibly protracted negotiations with creditors. These risks are mitigated by the authorities' commitment to reforms, strength of program design including through prior actions, and an already established and active OCC under the CF that has already agreed to a debt-service suspension. Risks due to prospective credit under the program will rise towards the end of the ten-year horizon.

- The access under the program is expected to have significant impact on PRGT finances. The proposed access will be the largest under the PRGT to date in terms of quota and in nominal terms. It will account for about half of current PRGT reserves, cost significant subsidy resources and increase credit concentration. An underfunded program, on the other hand, would compromise chances of program success.

The Federal Democratic Republic of Ethiopia: Debt Composition

(In millions of US dollars, unless otherwise specified)

Creditor Profile	**At end-June 2023**
Total debt	64,274
External	28,930
Multilateral Creditors	15,269
IMF	709
World Bank	11,589
AfDB/AfDF	2,198
Others	773
o/w IFAD	410
Bilateral official creditors 1/ 2/	12,406
Paris Club	1,853
Non-Paris Club	10,553
Eurobond	1,033
Commercial creditors 3/	222
Domestic	35,343
Memo Items:	
Collateralized debt	0
Nominal GDP (in ETB millions)	8,722,308
End-of-period exchange rate (ETB per US$)	55
Multilateral and Collateralized debt	
Multilateral Creditors	15,269
Percent of external debt	53
Percent of GDP	9.6
IMF and WB	12,298
Percent of external debt	43
Percent of GDP	7.7
AfDB/AfDF	2,198
Percent of external debt	8
Percent of GDP	1.4
Others	773
Percent of external debt	2.7
Percent of GDP	0.5
Collateralized debt	0
Percent of external debt	0
Percent of GDP	0

Sources: Ethiopian authorities; and IMF staff estimates and projections.
1/ Includes loans backed by export credit agencies.
2/ Includes pre-HIPC arrears waiting to receive HIPC comparable treatment.
3/ Loans from commercial banks and credit suppliers non-backed by ECAs

- Business risks are posed by data limitations, including lack of high frequency indicators and data quality concerns, which can affect estimates of the impact of reforms.

- Reputational risks could arise if the program goes off track shortly after inception due to insufficient upfront adjustment, or if the exchange rate unification leads to an inflation-depreciation spiral that is not addressed through a strong policy response and effective communication by the authorities. Program design aims to mitigate these risks (Box 2). The Fund could also face reputational risks from not supporting a member with large BOP needs in a fragile post-conflict socio-economic environment, considering efforts to consolidate peace and potential spillovers to neighboring countries in the Horn of Africa.

71. Staff and the authorities have identified key capacity development priorities to support program objectives. Areas covered include national accounts, external sector, and price statistics; NBE Proclamation; FX regulations; monetary operations; asset classification, provisioning, and capital framework for banks; fuel pricing mechanism; tax policy and administration; public financial management; government finance statistics; and debt management and reporting.

Box 2. Exchange Rate Reform and Program Design

The program includes measures to manage potential risks from the significant exchange rate reform envisaged by the authorities. Key risks that program design aims to address include:

- *Expectations:* Tightening of financial conditions through active monetary policy and keeping SOE lending in check along with good communication will underpin the credibility of the post-unification policy framework and help minimize exchange rate overshooting or risks of an inflation-depreciation spiral.
- *Uncertainty and hoarding:* Program monitoring (including quarterly monitoring in the early stages) and course correction as needed will help navigate uncertainty. As FX suppliers may face incentives to withhold FX from the market in the uncertain new environment, surrender requirements will be removed gradually to ensure a minimum market supply as confidence develops. Surrender will be to commercial banks subject to NOP requirements that will limit their ability to take long positions and limit supply of FX to market.
- *Welfare impacts:* Managing the impact of further price increases for food and essential commodities, particularly for the urban poor, will be critical for maintaining social cohesion. Strengthening social protection via the PSNP as well as potential temporary measures will help address this impact and ensure durable buy-in for the new exchange rate regime (Annex V)
- *Balance sheet risks:* Upfront recapitalization of CBE is important for financial sector stability given its central role in FX transactions as banker for SOEs. Risks in the rest of the banking sector are limited given manageable legacy NOPs, and little indirect credit risk as lending is not dollarized. Measures to improve the financial position of SOEs are also important for those previously importing essential commodities at the official exchange rate, and as the Birr costs of servicing foreign debt and capital goods imports rises.
- *Policy commitment:* The authorities may come under pressure to provide FX at favorable rates from vested interests—for example in SOEs—and CBE is a possible instrument to do so. Maintaining strong commitment to market determination of exchange rates and further liberalizing steps as the FX market deepens will be critical to avoid re-emergence of a parallel market spread, uncertainty and continued depreciation pressures.

STAFF APPRAISAL

72. After decades of rapid social and economic development, Ethiopia experienced a series of large shocks leading to acute economic pressures, while the public investment-led growth model has reached its limits. Combined with building vulnerabilities, domestic conflict, the pandemic, droughts, and spillovers from Russia's war in Ukraine led to foreign exchange shortages, high inflation, worsening export performance, an erosion of international reserves, and unsustainable external debt. The authorities recognize that comprehensive macroeconomic and structural reforms are needed to urgently address macroeconomic imbalances and lay the foundation for higher, inclusive, and private sector-led growth.

73. The authorities have embarked on an ambitious reform program under the HGER. Addressing the challenge of transforming the economy, already under way, has entailed extensive preparation including with capacity development from development partners, and will require continued support from many domestic and external stakeholders.

74. Moving to a market clearing exchange rate and removing current account restrictions will help address acute FX shortages and remove the key relative price distortion contributing to protracted BOP vulnerabilities. Any intervention in the FX market should be limited to stemming disorderly market conditions. Strengthened monitoring and enforcement of daily net open position limits will help ensure that banks manage FX risks well under the new regime.

75. The authorities are requesting temporary approval to retain an exchange transaction commission required by the NBE to be levied on sales of FX by authorized banks that gives rise to a multiple currency practice and an exchange restriction (see discussion in paragraph 22). Staff assesses that the criteria for approval are satisfied, as it is imposed for BOP reasons, does not give the member an unfair competitive advantage over other members and the measure is temporary as the authorities aim to eliminate it by the end of the Fund-supported program. Staff supports the authorities' request for approval.

76. Continuing to tighten monetary policy will be essential to supporting exchange rate reform and anchoring inflation. In addition to the elimination of monetary financing of fiscal deficits and moving to positive real interest rates, the authorities stand ready to take additional monetary policy measures (e.g., raising reserve requirements) if needed. Continued efforts to maximize market-based financing and allowing T-bill rates to rise gradually to positive levels in real terms, are important to reduce financial repression and contain inflation. Development of the governance and operational framework for interest rate-based monetary policy is critical to develop efficient transmission of policy signals to the wider economy and ensure NBE can control inflation over the medium and long term. Comprehensive revision of NBE's mandate, autonomy, governance, and transparency arrangements that are underway are likewise key elements to entrench price stability, a healthy financial system, and promote financial deepening.

77. Revenue mobilization is critical to realize the authorities' developmental objectives and the long-term sustainability of public finances. While a temporary widening of the fiscal deficit to accommodate spending to mitigate the impact of exchange rate reform on the most vulnerable is warranted, some gradual consolidation is also needed. Revenue mobilization will be anchored by the National Medium-Term Revenue Strategy and will be key to create space for priority social and capital expenditure. Expanding the targeted cash transfer program (PSNP) is the most cost effective and efficient way to support vulnerable people, and untargeted subsidies, e.g., on fuel, should be removed to ensure fiscal sustainability after the initial price impact of reform wanes. Strengthening the institutional framework for public investment will help enhance efficiency and the growth impact of capital spending in the context of large needs, including those related to climate change and reconstruction. Enhanced transparency and monitoring of extrabudgetary units will be important for managing fiscal risks.

78. The planned debt treatment under the CF will help restore debt sustainability. The authorities should also seek to avoid the accumulation of new debt vulnerabilities by limiting non-concessional borrowing and strengthening debt management and transparency.

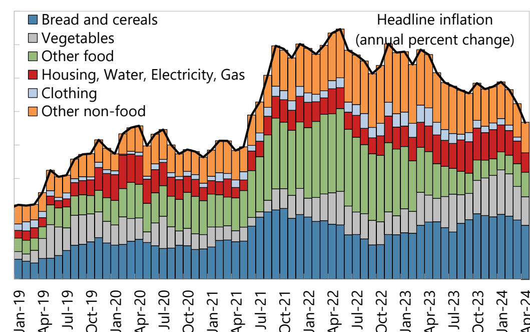
79. CBE's stronger balance sheet and improving the financial position of SOEs are key to bolstering financial stability and reducing vulnerabilities. Building on its recent recapitalization, the authorities should implement a reform program for CBE to ensure it can operate sustainably, at arm's length from the rest of the public sector as a fully commercially oriented bank. Tight limits on SOE borrowing reinforced by stronger prudential regulations and enhanced transparency (including audits) will be important to prevent the reemergence of SOE-driven financial fragilities. Proactive and sustained strengthening of banking regulation and supervision will be important for preserving financial sector stability and encouraging sound development as the sector opens up, new economic opportunities emerge from macroeconomic reform, and exchange rate and interest rate environments change fundamentally.

80. Further structural reforms will support growth and poverty reduction. This includes measures to improve governance, financial inclusion, public service delivery, and bolster climate resilience and food security. Improving economic statistics, starting with national accounts and fiscal and debt transparency, is also a priority to enable better policymaking and improve the investment environment.

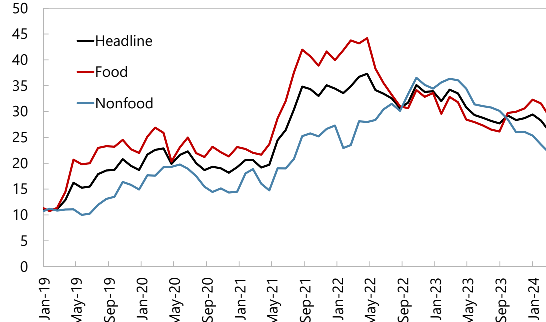
81. In view of Ethiopia's large balance of payments needs and based on the strength of the proposed program, the prior actions taken by the authorities, and given receipt of financing assurances from bilateral creditors, staff supports the authorities' request for a 48-month arrangement in the amount of SDR 2,555.95 million and for temporary approval of the exchange restriction and multiple currency practice.

Figure 1. The Federal Democratic Republic of Ethiopia: Inflation and Monetary Developments

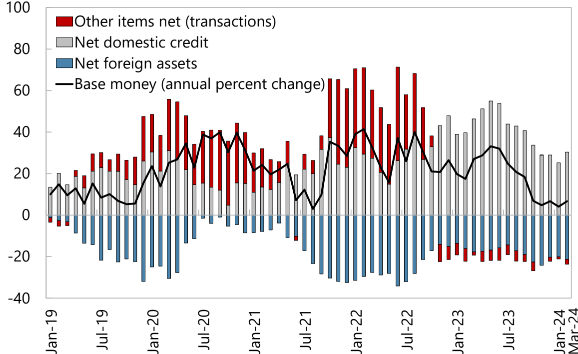
Contribution to Inflation
(Percentage points, unless otherwise specified)



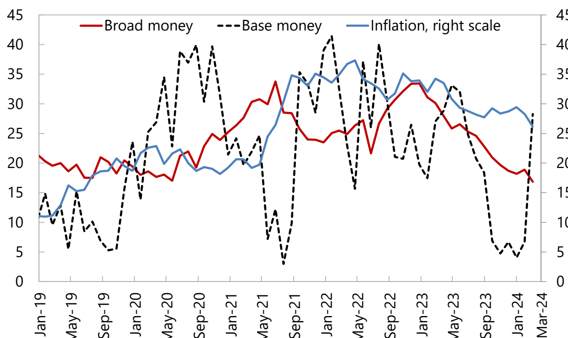
Inflation
(CPI, annual percentage change)



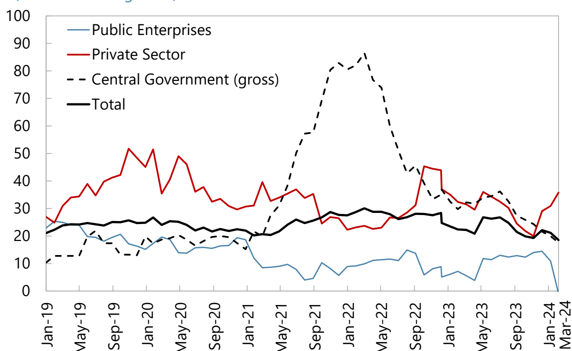
Contribution to Reserve Money Growth
(Percentage points)



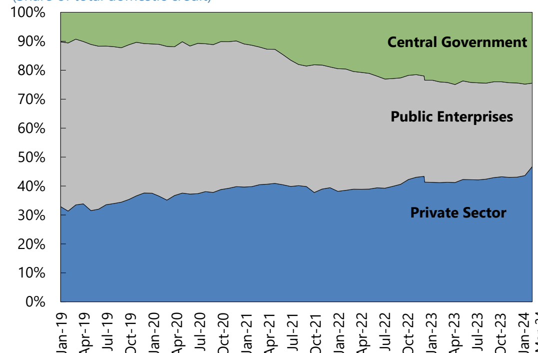
Monetary Aggregates and Inflation
(year-on-year percent change)



Credit to the Economy
(Percent annual growth)



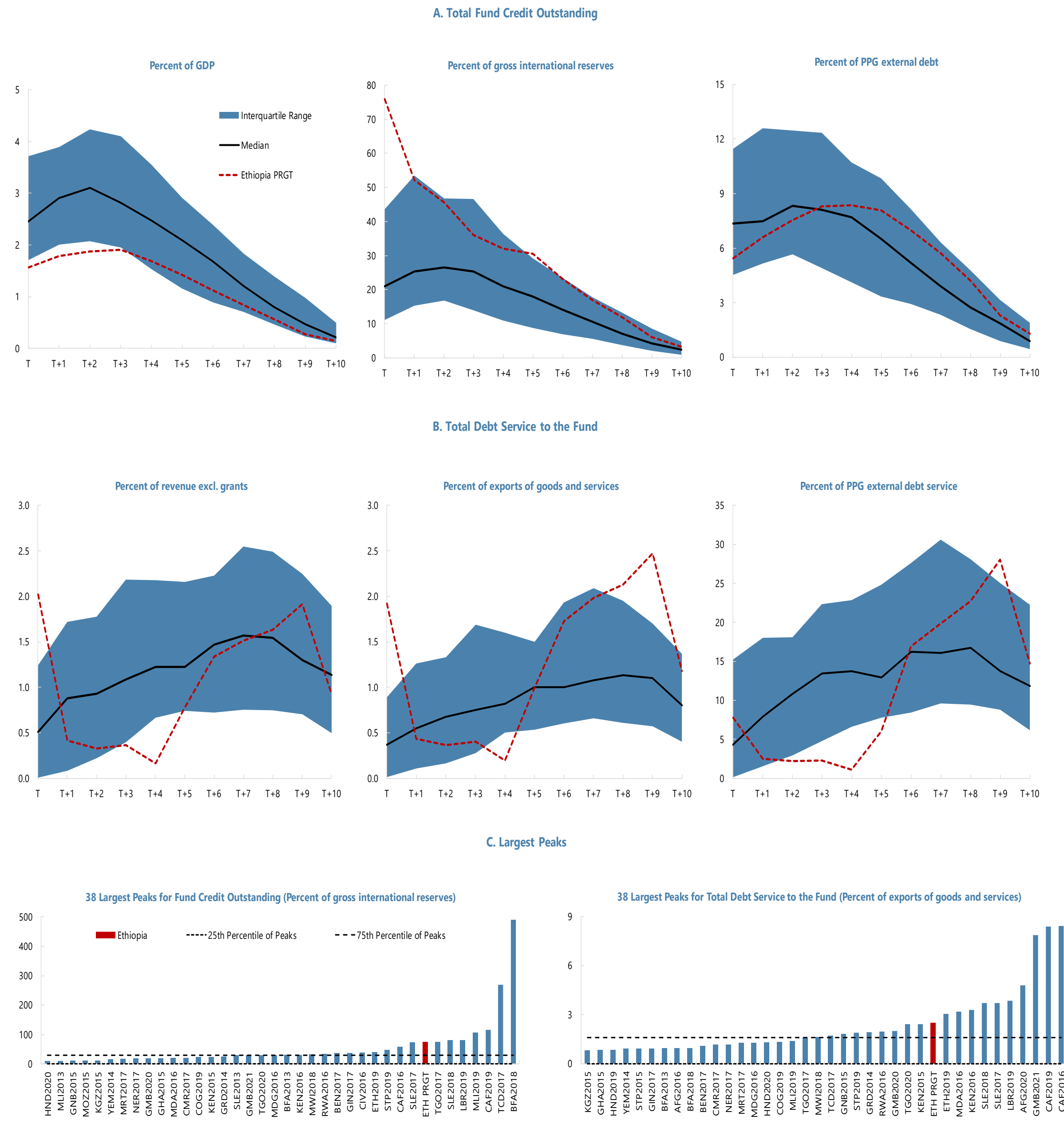
Credit to the Economy
(Share of total domestic credit)



Sources: Ethiopian authorities; Central Statistical Agency, Ethiopia; IMF staff calculations.

Figure 2. The Federal Democratic Republic of Ethiopia: Capacity to Repay Indicators Compared to UCT Arrangements for PRGT Countries

(In percent of the indicated variable)



Notes:
1) T = date of arrangement approval. PPG = public and publicly guaranteed.
2) Red lines/bars indicate the CtR indicator for the arrangement of interest.
3) The median, interquartile range, and comparator bars reflect all UCT arrangements (including blends) approved for PRGT countries between 2013 and 2023.
4) PRGT countries in the control group with multiple arrangements are entered as separate events in the database.
5) Comparator series is for PRGT arrangements only and runs up to T+10.
6) Debt service obligations to the Fund reflect prospective payments, including for the current year.
7) In the case of blenders, the red lines/ bars refer to PRGT+GRA. In the case of RST, the red lines/ bars refer to PRGT+GRA+RST.

Table 1. The Federal Democratic Republic of Ethiopia: Selected Economic Indicators, 2020/21–2028/29[1]

	2020/21 Act.	2021/22 Act.	2022/23 Prel.	2023/24 IMF Staff Proj.	2024/25 IMF Staff Proj.	2025/26 IMF Staff Proj.	2026/27 IMF Staff Proj.	2027/28 IMF Staff Proj.	2028/29 IMF Staff Proj.
	In percent change, unless otherwise mentioned								
National income and prices									
GDP at constant prices (at factor cost)	6.3	6.4	7.2	6.1	6.5	7.1	7.7	8.0	7.8
GDP deflator	21.8	34.7	32.9	26.7	25.8	16.1	12.2	10.4	9.6
Consumer prices (period average) [1]	20.2	33.9	32.5	26.9	30.1	16.2	12.2	10.4	9.6
Consumer prices (end period) [1]	24.5	34.2	29.3	22.9	31.1	13.5	10.9	9.7	9.4
External sector									
Exports of goods and services (f.o.b.)	10.9	22.8	3.3	3.9	7.9	15.0	17.3	17.0	7.1
Imports of goods and services (c.i.f.)	2.3	24.9	-1.4	1.9	8.7	5.9	10.6	11.8	6.8
Export volume (goods)	12.6	2.5	-17.3	2.0	1.7	22.8	21.6	18.4	11.3
Export volume (goods and services)	3.2	11.0	-3.2	7.7	7.3	13.6	11.1	9.7	5.7
Import price index (percent change)	3.7	16.4	4.0	-4.1	-0.2	-1.8	-1.4	-1.2	-1.2
Terms of trade (goods and services, deterioration –)	3.7	-4.9	2.5	0.6	0.7	3.0	7.1	8.0	2.6
Nominal effective exchange rate (end of period, depreciation –)	-24.1	-8.6	8.7	...	...	...	...	...	...
Real effective exchange rate (end of period, depreciation –)	-10.2	10.0	29.8	...	...	...	...	...	...
Money and credit									
Claims on nongovernment	21.9	18.9	24.1	12.0	21.2	25.5	31.3	20.1	18.2
Broad money	29.9	27.2	26.6	14.4	30.3	25.1	26.6	23.5	21.7
Base money	7.2	37.2	32.0	3.3	23.9	24.7	22.3	21.0	16.8
Velocity (GDP/broad money)	3.22	3.59	4.02	4.70	4.90	4.90	4.71	4.57	4.44
	In percent of GDP, unless otherwise mentioned								
Financial balances[2]									
Gross domestic savings	19.0	15.2	14.8	13.9	10.4	15.0	16.8	18.9	19.7
Public savings	1.6	-0.4	1.1	1.7	1.0	2.3	3.0	3.3	3.5
Private savings	17.4	15.6	13.7	12.2	9.4	12.7	13.8	15.6	16.2
Gross domestic investment	28.0	25.3	22.2	19.7	20.1	23.9	25.0	26.6	27.0
Public investment	7.5	6.4	5.6	4.2	3.7	5.7	6.2	6.6	6.3
Private investment	20.5	19.0	16.6	15.4	16.4	18.2	18.8	20.0	20.7
Resource gap	-9.1	-10.1	-7.4	-5.8	-9.7	-8.9	-8.2	-7.7	-7.3
External current account balance, including official transfers	-2.8	-4.0	-2.8	-2.6	-4.3	-3.2	-2.5	-2.0	-1.9
Government finances									
Revenue	10.2	8.1	7.9	7.3	8.3	9.8	10.8	11.2	11.4
Tax revenue	9.0	7.1	6.8	6.3	7.3	8.7	9.8	10.2	10.4
Nontax revenue	1.3	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
External grants	0.8	0.4	0.4	0.4	1.4	0.6	0.5	0.4	0.4
Expenditure and net lending	13.8	12.7	10.8	9.4	11.3	12.4	13.3	13.6	13.9
Fiscal balance, including grants (cash basis)	-2.8	-4.2	-2.6	-1.7	-1.7	-2.1	-2.0	-2.0	-2.0
Total financing (including residuals and excluding privatization)	2.8	4.2	2.6	1.7	1.7	2.1	2.0	2.0	2.0
External financing	0.7	0.1	0.3	0.2	1.3	-0.2	0.3	0.3	-0.4
Domestic financing	2.1	4.3	2.5	1.5	0.8	1.5	1.7	1.7	2.4
Public debt [3]	56.1	48.9	40.2	34.4	42.9	38.8	35.8	33.6	31.5
Domestic debt	27.1	24.8	22.1	19.1	14.5	12.2	11.4	11.0	11.8
External debt (including to the IMF)	29.0	24.0	18.1	15.4	28.3	26.6	24.5	22.6	19.8
Overall balance of payments (in millions of U.S. dollars)	-41	-2,639	-809	-91	-1,816	174	298	892	1,377
Gross official reserves (in millions of U.S. dollars)	2,866	1,495	1,026	1,011	2,793	5,067	7,012	10,205	11,543
(months of prospective imports of goods and nonfactor services)	1.5	0.8	0.5	0.5	1.2	2.0	2.5	3.5	3.6
Net international reserves (in millions of U.S. dollars, program definition)	1,922	271	-269	...	...	...	...	...	...
GDP at current market prices (billions of birr)	4,341	6,158	8,722	11,676	15,844	19,839	24,155	28,918	34,216.6

Sources: Ethiopian authorities and IMF staff estimates and projections.

[1] The base is December 2016.

[2] Based on data from Central Statistical Agency (CSA), except for the current account balance, which is based on balance of payments (BOP) data from National Bank of Ethiopia

[3] Public and publicly guaranteed external debt, which includes long-term foreign liabilities of NBE and external debt of Ethio-Telecom. Does not include expected debt relief.

Table 2a. The Federal Democratic Republic of Ethiopia: General Government Operations, 2020/21–2028/29[1]

(Millions of Ethiopian birr)

	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29
	Act.	Act.	Act.	IMF Staff	IMF Staff	IMF Staff	IMF Staff	IMF Staff	IMF Staff
				Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Total revenue and grants	478,888	525,736	717,149	901,105	1,525,795	2,044,069	2,730,394	3,367,675	4,063,614
Revenue	444,583	499,043	685,021	857,904	1,311,704	1,934,431	2,611,824	3,241,260	3,913,680
Tax revenue	388,763	436,753	595,135	737,578	1,152,827	1,735,498	2,369,614	2,951,292	3,570,580
Direct taxes	173,965	206,825	265,385	355,331	443,378	720,163	964,845	1,173,922	1,410,727
Indirect taxes	214,798	229,927	329,749	382,247	709,449	1,015,335	1,404,769	1,777,370	2,159,853
Domestic indirect taxes	108,160	98,617	161,197	210,076	362,044	535,307	756,434	1,002,307	1,246,769
Import duties and taxes	106,638	131,310	168,553	172,171	347,405	480,028	648,335	775,063	913,084
Nontax revenue	55,819	62,290	89,887	120,326	158,877	198,933	242,210	289,968	343,100
Grants	34,305	26,693	32,128	43,201	214,091	109,638	118,570	126,415	149,934
Program grants	10,747	0	2,426	0	130,260	13,047	15,140	16,430	17,662
Project grants	23,558	26,693	29,701	43,201	83,831	96,591	103,430	109,985	132,272
Total expenditure and net lending (cash basis)	599,007	781,789	943,881	1,099,597	1,795,116	2,450,770	3,213,497	3,946,033	4,747,946
Recurrent expenditure [2]	363,597	518,302	588,122	664,815	1,238,198	1,560,169	1,982,709	2,419,534	2,882,651
Defense spending	37,092	102,617	82,825	50,000	80,430	109,678	133,538	159,869	189,162
Poverty-reducing expenditure [3]	176,979	208,540	234,055	281,983	488,766	761,744	973,835	1,189,167	1,421,132
Education	107,513	127,506	145,117	174,833	296,563	445,597	569,664	695,627	831,320
Health	40,665	47,267	53,596	64,571	116,540	196,994	251,843	307,529	367,518
Agriculture	21,850	23,282	26,288	31,671	57,160	90,180	115,288	140,780	168,242
Natural resources	5,051	7,779	6,928	8,347	14,158	22,337	28,556	34,871	41,673
Roads	1,899	2,706	2,126	2,561	4,344	6,636	8,484	10,359	12,380
Interest payments	24,001	38,513	54,544	71,759	177,469	233,309	293,092	373,451	447,587
Domestic interest and charges	16,563	26,602	41,557	61,406	149,814	189,769	238,905	306,045	367,653
External interest payments [4]	7,438	11,911	12,987	10,353	27,654	43,540	54,187	67,406	79,934
Other recurrent expenditure	125,525	168,632	216,699	261,073	491,533	455,437	582,244	697,048	824,770
Capital expenditure	235,410	263,488	355,759	434,782	556,918	890,602	1,230,788	1,526,499	1,865,295
Central treasury	186,923	216,570	284,022	356,486	409,066	717,159	1,033,010	1,315,916	1,620,084
External project grants	23,558	26,693	29,701	43,201	83,831	96,591	103,430	109,985	132,272
External project loans	24,929	20,224	42,036	35,095	64,022	76,852	94,348	100,598	112,939
Overall balance									
Including grants	-120,119	-256,054	-226,733	-198,492	-269,320	-406,702	-483,103	-578,358	-684,332
Excluding grants	-154,424	-282,747	-258,860	-241,693	-483,412	-516,340	-601,672	-704,773	-834,266
Financing	142,064	265,726	243,253	198,492	269,320	406,702	483,103	578,358	684,332
Net external financing	29,818	3,295	29,010	18,665	204,293	-39,925	77,409	81,067	-122,765
Gross borrowing [5]	26,804	20,224	51,843	35,095	303,770	76,852	197,681	187,050	112,939
IMF budget support	0	0	0	0	65,256	0	0	0	0
Project loans	24,929	20,224	42,036	35,095	64,022	76,852	94,348	100,598	112,939
Budget support	1,875	0	9,807	0	174,493	0	103,333	86,452	0
G20 Debt Service Suspension Initiative	8,009	0	0	0	0	0	0	0	0
Amortization, due	-4,995	-16,929	-22,833	-16,430	-207,538	-122,185	-141,505	-203,142	-235,705
Net domestic financing [6]	89,426	262,431	214,243	179,828	127,260	295,661	405,694	497,291	807,098
Banking system	34,862	206,614	141,729	89,914	29,260	144,384	202,847	248,645	403,549
Nonbanking system	54,564	55,817	72,514	89,914	98,000	151,277	202,847	248,645	403,549
o/w gross advances from NBE	51,625	61,201	189,543	95,000	0	0	0	0	0
o/w T-bills and T-bonds	88,378	201,230	24,700	84,828	127,260	295,661	405,694	497,291	807,098
o/w Other (incl. net deposit withdrawal)	-50,577	0	0	0	0	0	0	0	0
Privatization proceeds	22,820	0	0	0	0	88,733	0	0	0
Other below-the-line operations [7]	-21,945	-9,673	-16,521	0	-62,233	62,233	0	0	0
Residual gap	0	0	0	0	108,061	5,407	21,233	97,160	0
CBE recapitalization									
Total debt outstanding				870,000	870,000	870,000	870,000	745,714	621,429
Debt service				0	78,300	78,300	78,300	229,628	202,702
Amortization				0	0	0	0	124,286	124,286
Interest (included in the budgetary central government)				0	78,300	78,300	78,300	105,342	78,416
Total net financing (budgetary plus CBE recap. amortization)	142,064	265,726	243,253	198,492	269,320	406,702	483,103	702,644	808,618

Sources: Ethiopian authorities and IMF staff estimates and projections.

[1] Government financial statistics are reported by the authorities based on GFSM 1986.

[2] Excluding special programs (demobilization and reconstruction).

[3] Poverty-reducing spending is defined to include total spending on health, education, agriculture, roads, and food security.

[4] External interest and amortization are presented after HIPC debt relief from the World Bank and the African Development Bank.

[5] Includes prospective donor financing to close the financing gap.

[6] Net domestic financing is derived as a residual financing source in projection years.

[7] Negative amounts signify overfinancing. Net FY2024/25 overfinancing reflects expected timeline of DPO2 disbursement.

Table 2b. The Federal Democratic Republic of Ethiopia: General Government Financial Operations, 2020/21-2028/29[1]

(Percent of GDP)

	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29
	Act.	Act.	Act.	IMF Staff	IMF Staff	IMF Staff	IMF Staff	IMF Staff	IMF Staff
				Proj.	Proj.	Proj.	Proj.	Proj.	Proj.
Total revenue and grants	11.0	8.5	8.2	7.7	9.6	10.3	11.3	11.6	11.9
Revenue	10.2	8.1	7.9	7.3	8.3	9.8	10.8	11.2	11.4
Tax revenue	9.0	7.1	6.8	6.3	7.3	8.7	9.8	10.2	10.4
Direct taxes	4.0	3.4	3.0	3.0	2.8	3.6	4.0	4.1	4.1
Indirect taxes	4.9	3.7	3.8	3.3	4.5	5.1	5.8	6.1	6.3
Domestic indirect taxes	2.5	1.6	1.8	1.8	2.3	2.7	3.1	3.5	3.6
Import duties and taxes	2.5	2.1	1.9	1.5	2.2	2.4	2.7	2.7	2.7
Nontax revenue	1.3	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Grants	0.8	0.4	0.4	0.4	1.4	0.6	0.5	0.4	0.4
Program grants	0.2	0.0	0.0	0.0	0.8	0.1	0.1	0.1	0.1
Project grants	0.5	0.4	0.3	0.4	0.5	0.5	0.4	0.4	0.4
Total expenditure and net lending (cash basis)	13.8	12.7	10.8	9.4	11.3	12.4	13.3	13.6	13.9
Recurrent expenditure [2]	8.4	8.4	6.7	5.7	7.8	7.9	8.2	8.4	8.4
Defense spending	0.9	1.7	0.9	0.4	0.5	0.6	0.6	0.6	0.6
Poverty-reducing expenditure [3]	4.1	3.4	2.7	2.4	3.1	3.8	4.0	4.1	4.2
Education	2.5	2.1	1.7	1.5	1.9	2.2	2.4	2.4	2.4
Health	0.9	0.8	0.6	0.6	0.7	1.0	1.0	1.1	1.1
Agriculture	0.5	0.4	0.3	0.3	0.4	0.5	0.5	0.5	0.5
Natural resources	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Roads	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Interest payments	0.6	0.6	0.6	0.6	1.1	1.2	1.2	1.3	1.3
Domestic interest and charges	0.4	0.4	0.5	0.5	0.9	1.0	1.0	1.1	1.1
External interest payments [4]	0.2	0.2	0.1	0.1	0.2	0.2	0.2	0.2	0.2
Other recurrent expenditure	2.9	2.7	2.5	2.2	3.1	2.3	2.4	2.4	2.4
Capital expenditure	5.4	4.3	4.1	3.7	3.5	4.5	5.1	5.3	5.5
Central treasury	4.3	3.5	3.3	3.1	2.6	3.6	4.3	4.6	4.7
External project grants	0.5	0.4	0.3	0.4	0.5	0.5	0.4	0.4	0.4
External project loans	0.6	0.3	0.5	0.3	0.4	0.4	0.4	0.3	0.3
Overall balance									
Including grants	-2.8	-4.2	-2.6	-1.7	-1.7	-2.1	-2.0	-2.0	-2.0
Excluding grants	-3.6	-4.6	-3.0	-2.1	-3.1	-2.6	-2.5	-2.4	-2.4
Financing	3.3	4.3	2.8	1.7	1.7	2.1	2.0	2.0	2.0
Net external financing	0.7	0.1	0.3	0.2	1.3	-0.2	0.3	0.3	-0.4
Gross borrowing [5]	0.6	0.3	0.6	0.3	1.9	0.4	0.8	0.6	0.3
IMF budget support	0.0	0.0	0.0	0.0	0.4	0.0	0.0	0.0	0.0
Project loans	0.6	0.3	0.5	0.3	0.4	0.4	0.4	0.3	0.3
Budget support	0.0	0.0	0.1	0.0	1.1	0.0	0.4	0.3	0.0
G20 Debt Service Suspension Initiative	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Amortization, due	-0.1	-0.3	-0.3	-0.1	-1.3	-0.6	-0.6	-0.7	-0.7
Net domestic financing [6]	2.1	4.3	2.5	1.5	0.8	1.5	1.7	1.7	2.4
o/w gross advances from NBE	1.2	1.0	2.2	0.8	0.0	0.0	0.0	0.0	0.0
o/w T-bills and T-bonds	2.0	3.3	0.3	0.7	0.8	1.5	1.7	1.7	2.4
o/w Other (incl. net deposit withdrawal)	-1.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Privatization	0.5	0.0	0.0	0.0	0.0	0.4	0.0	0.0	0.0
Other below-the-line operations [7]	-0.5	-0.2	-0.2	0.0	-0.4	0.3	0.0	0.0	0.0
Residual gap	0.0	0.0	0.0	0.0	0.7	0.0	0.1	0.3	0.0
CBE recapitalization									
Total debt outstanding				7.5	5.5	4.4	3.6	2.6	1.8
Debt service				0.0	0.5	0.4	0.3	0.8	0.6
Amortization				0.0	0.0	0.0	0.0	0.4	0.4
Interest (included in the budgetary central government)				0.0	0.5	0.4	0.3	0.4	0.2
Total net financing (budgetary plus CBE recap. amortization)	3.3	4.3	2.8	1.7	1.7	2.1	2.0	2.4	2.4
Memorandum items :									
Primary fiscal balance, including grants	-2.2	-3.5	-2.0	-1.1	-0.6	-0.9	-0.8	-0.7	-0.7

Sources: Ethiopian authorities and IMF staff estimates and projections. The Ethiopian fiscal year ends July 7.

[1] Government financial statistics are reported by the authorities based on GFSM 1986.

[2] Excluding special programs (demobilization and reconstruction).

[3] Poverty-reducing spending is defined to include total spending on health, education, agriculture, roads, and food security.

[4] External interest and amortization are presented after HIPC debt relief from the World Bank and the African Development Bank.

[5] Includes prospective donor financing to close the financing gap.

[6] Net domestic financing is derived as a residual financing source in projection years.

[7] FY2024/25 overfinancing reflects expected timeline of DPO2 disbursement.

Table 3a. The Federal Democratic Republic of Ethiopia: Monetary Survey, 2020/21–2028/29

(Millions of birrs)

	2020/21 Act.	2021/22 Act.	2022/23 Prel.	2023/24 IMF Staff Proj.	2024/25 IMF Staff Proj.	2025/26 IMF Staff Proj.	2026/27 IMF Staff Proj.	2027/28 IMF Staff Proj.	2028/29 IMF Staff Proj.
				I. Depository Corporation Survey					
Monetary survey									
Net foreign assets	-812	-111,428	-160,098	-262,628	-410,162	-194,175	1,078	416,780	623,036
Central bank	-43,907	-134,219	-191,423	-295,505	-563,258	-361,757	-178,011	226,759	422,865
Commercial banks	43,095	22,791	31,325	32,877	153,096	167,582	179,088	190,021	200,172
Net domestic assets	1,349,078	1,826,738	2,330,946	2,746,639	3,646,467	4,242,904	5,125,958	5,916,699	7,082,022
Domestic credit	1,481,844	1,930,622	2,444,436	2,758,665	3,232,045	4,024,611	5,229,695	6,318,695	7,636,457
Claims on government (net) [1]	214,269	422,864	573,676	663,686	692,946	837,330	1,044,853	1,292,949	1,695,943
Claims on nongovernment	1,267,575	1,507,758	1,870,760	2,094,978	2,539,099	3,187,281	4,184,843	5,025,746	5,940,515
Public enterprises	603,517	692,126	779,194	849,502	982,253	1,163,381	1,351,383	1,625,594	1,860,333
Private sector	664,059	815,631	1,091,566	1,245,477	1,556,846	2,023,900	2,833,460	3,400,152	4,080,182
Broad money	1,348,266	1,715,310	2,170,848	2,484,011	3,236,305	4,048,730	5,127,036	6,333,479	7,705,059
Money	437,392	588,016	706,142	812,640	1,032,661	1,275,794	1,589,658	1,946,470	2,349,571
Currency outside banks	133,621	173,383	211,637	255,097	297,559	350,786	409,643	483,031	563,062
Demand deposits	303,771	414,633	494,505	557,543	735,102	925,009	1,180,015	1,463,439	1,786,508
Quasi money	910,874	1,127,294	1,464,706	1,671,370	2,203,644	2,772,935	3,537,378	4,387,009	5,355,488
Savings deposits	816,380	1,016,049	1,315,260	1,499,114	1,976,531	2,487,149	3,172,807	3,934,872	4,803,537
Time deposits	94,494	111,245	149,446	172,256	227,113	285,786	364,572	452,137	551,951
Central bank									
Net foreign assets	-43,907	-134,219	-191,423	-295,505	-563,258	-361,757	-178,011	226,759	422,865
Foreign assets	125,860	79,820	56,154	57,481	365,203	689,705	983,543	1,496,595	1,720,068
Foreign liabilities	169,767	214,038	247,577	352,986	928,462	1,051,462	1,161,554	1,269,836	1,297,204
Net domestic assets	308,209	496,717	669,895	789,656	1,175,317	1,125,133	1,111,662	903,068	896,437
Domestic credit	301,662	371,039	566,123	661,123	573,598	432,304	417,980	209,227	410,382
Government (net)	245,019	326,216	521,300	616,300	616,300	616,300	616,300	616,300	616,300
Other items (net)	6,547	125,678	103,772	128,533	601,719	692,829	693,682	693,841	486,055
Reserve money	264,302	362,499	478,472	494,151	612,059	763,376	933,651	1,129,827	1,319,302
Currency outside banks	133,621	173,383	211,637	255,097	297,559	350,786	409,643	483,031	563,062
Commercial bank reserves	130,681	189,116	266,835	239,054	314,500	412,590	524,008	646,796	756,240
Cash in vault	30,088	34,828	42,679	45,420	59,755	78,392	99,562	122,891	143,686
Reserve deposit	100,593	111,346	127,177	143,739	162,397	182,696	205,534	231,011	289,978
				(Annual percentage change, unless otherwise indicated)					
Monetary survey									
Net foreign assets	-90.2	13617.2	43.7	64.0	56.2	-52.7	-100.6	38578.8	49.5
Net domestic assets	29.0	35.4	27.6	17.8	32.8	16.4	20.8	15.4	19.7
Domestic credit	25.9	30.3	26.6	12.9	17.2	24.5	29.9	20.8	20.9
Claims on government (net) [1]	56.3	97.4	35.7	15.7	4.4	20.8	24.8	23.7	31.2
Claims on nongovernment	21.9	18.9	24.1	12.0	21.2	25.5	31.3	20.1	18.2
Public enterprises	11.0	14.7	12.6	9.0	15.6	18.4	16.2	20.3	14.4
Private sector	33.8	22.8	33.8	14.1	25.0	30.0	40.0	20.0	20.0
Broad money	29.9	27.2	26.6	14.4	30.3	25.1	26.6	23.5	21.7
Money	21.3	34.4	20.1	15.1	27.1	23.5	24.6	22.4	20.7
Quasi money	34.5	23.8	29.9	14.1	31.8	25.8	27.6	24.0	22.1
Memorandum items:									
Base money growth	7.2	37.2	32.0	3.3	23.9	24.7	22.3	21.0	16.8
Nominal GDP growth	28.7	41.8	41.7	33.9	35.7	25.2	21.8	19.7	18.3
Excess reserve deposit (billions of birr)	31,976	22,206	66,804	37,609	49,033	75,342	94,229	114,373	112,614
Percent of deposits	2.6	2.1	3.4	1.7	1.7	2.0	2.0	2.0	1.6
Money multiplier (broad money/reserve money)	5.10	4.73	4.54	5.03	5.29	5.30	5.49	5.61	5.84
Velocity (GDP/broad money)	3.05	3.59	4.02	4.70	4.90	4.90	4.71	4.57	4.44
Currency-deposit ratio	0.110	0.112	0.108	0.114	0.101	0.095	0.087	0.083	0.079
Birr per U.S. dollar (end of period)	43.7	…	…	…	…	…	…	…	…
Nominal GDP (millions of birr)	4,108,684	6,157,538	8,722,308	11,676,013	15,844,489	19,839,119	24,155,131	28,917,904	34,216,610

Sources: NBE and IMF staff estimates and projections.

[1] Claims on the general government by the banking system less deposits of the general government with the banking system.

Table 3b. The Federal Democratic Republic of Ethiopia: Monetary Survey and Central Bank Accounts, 2020/21–2028/29

(In percent of GDP)

	2020/21	2021/22	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29
	Act.	Act.	Prel.	IMF Staff Proj.	IMF Staff Proj.	IMF Staff Proj.	IMF Staff Proj.	IMF Staff Proj.	IMF Staff Proj.
			Percent of GDP						
Monetary survey									
Net foreign assets	0.0	-1.8	-1.8	-2.2	-2.6	-1.0	0.0	1.4	1.8
Central bank	-1.1	-2.2	-2.2	-2.5	-3.6	-1.8	-0.7	0.8	1.2
Commercial banks	1.0	0.4	0.4	0.3	1.0	0.8	0.7	0.7	0.6
Net domestic assets	32.8	29.7	26.7	23.5	23.0	21.4	21.2	20.5	20.7
Domestic credit	36.1	31.4	28.0	23.6	20.4	20.3	21.7	21.9	22.3
Claims on government (net) [1]	5.2	6.9	6.6	5.7	4.4	4.2	4.3	4.5	5.0
Claims on nongovernment	30.9	24.5	21.4	17.9	16.0	16.1	17.3	17.4	17.4
Public enterprises	14.7	11.2	8.9	7.3	6.2	5.9	5.6	5.6	5.4
Private sector	16.2	13.2	12.5	10.7	9.8	10.2	11.7	11.8	11.9
Broad money	32.8	27.9	24.9	21.3	20.4	20.4	21.2	21.9	22.5
Money	10.6	9.5	8.1	7.0	6.5	6.4	6.6	6.7	6.9
Currency outside banks	3.3	2.8	2.4	2.2	1.9	1.8	1.7	1.7	1.6
Demand deposits	7.4	6.7	5.7	4.8	4.6	4.7	4.9	5.1	5.2
Quasi money	22.2	18.3	16.8	14.3	13.9	14.0	14.6	15.2	15.7
Savings deposits	19.9	16.5	15.1	12.8	12.5	12.5	13.1	13.6	14.0
Time deposits	2.3	1.8	1.7	1.5	1.4	1.4	1.5	1.6	1.6
Central bank									
Net foreign assets	-1.1	-2.2	-2.2	-2.5	-3.6	-1.8	-0.7	0.8	1.2
Foreign assets	3.1	1.3	0.6	0.5	2.3	3.5	4.1	5.2	5.0
Foreign liabilities	4.1	3.5	2.8	3.0	5.9	5.3	4.8	4.4	3.8
Net domestic assets	7.5	8.1	7.7	6.8	7.4	5.7	4.6	3.1	2.6
Domestic credit	7.3	6.0	6.5	5.7	3.6	2.2	1.7	0.7	1.2
Government (net)	6.0	5.3	6.0	5.3	3.9	3.1	2.6	2.1	1.8
Other items (net)	0.2	2.0	1.2	1.1	3.8	3.5	2.9	2.4	1.4
Reserve money	6.4	5.9	5.5	4.2	3.9	3.8	3.9	3.9	3.9
Currency outside banks	3.3	2.8	2.4	2.2	1.9	1.8	1.7	1.7	1.6
Commercial bank reserves	3.2	3.1	3.1	2.0	2.0	2.1	2.2	2.2	2.2
Cash in vault	0.7	0.6	0.5	0.4	0.4	0.4	0.4	0.4	0.4
Reserve deposit	2.4	1.8	1.5	1.2	1.0	0.9	0.9	0.8	0.8
Nominal GDP (millions of birr)	4,108,684	6,157,538	8,722,308	11,676,013	15,844,489	19,839,119	24,155,131	28,917,904	34,216,610

Sources: NBE and IMF staff estimates and projections.

[1] Claims on the general government by the banking system less deposits of the general government with the banking system.

Table 4a. The Federal Democratic Republic of Ethiopia: Summary Balance of Payments, 2020/21–2028/29

(In millions of U.S. dollars, unless otherwise indicated)

	2020/21 Act.	2021/22 Act.	2022/23 Prel.	2023/24 IMF Staff Proj.	2024/25 IMF Staff Proj.	2025/26 IMF Staff Proj.	2026/27 IMF Staff Proj.	2027/28 IMF Staff Proj.	2028/29 IMF Staff Proj.
(Millions of U.S. dollars, unless otherwise indicated)									
Current account balance [1]	-3,169	-5,134	-4,635	-5,945	-6,078	-4,632	-4,040	-3,545	-3,695
Excl. official transfers [1]	-4,538	-6,270	-5,729	-7,084	-7,479	-6,199	-5,693	-5,246	-5,447
Trade balance	-10,671	-13,991	-13,512	-13,656	-15,127	-15,260	-15,808	-16,653	-17,569
Exports of goods	3,617	4,101	3,618	3,560	3,641	4,525	5,811	7,344	8,289
Coffee	909	1,431	1,340	1,248	1,500	1,591	1,945	2,315	2,464
Oil seeds	336	266	258	259	241	257	272	290	309
Gold	672	546	197	140	279	378	611	810	888
Other	1,700	1,859	1,823	1,913	1,621	2,298	2,983	3,929	4,629
Imports of goods	-14,288	-18,092	-17,130	-17,216	-18,768	-19,785	-21,619	-23,997	-25,858
Fuel	-1,941	-3,455	-4,031	-3,800	-3,700	-4,500	-4,807	-5,118	-5,435
Services (net)	587	1,213	1,399	1,535	1,850	2,300	2,400	2,521	2,537
Exports	4,895	6,350	7,174	7,650	8,450	9,380	10,505	11,750	12,166
Imports	-4,308	-5,137	-5,775	-6,115	-6,600	-7,080	-8,105	-9,229	-9,630
Income (net) [1]	-572	-574	-413	-934	-1,052	-864	-867	-853	-833
Private transfers (net)	6,118	7,082	6,798	5,971	6,850	7,626	8,582	9,738	10,418
Official transfers (net) [1]	1,369	1,136	1,093	1,139	1,401	1,567	1,653	1,701	1,752
Capital account balance [1]	3,467	1,975	2,929	4,040	3,407	4,715	4,677	5,602	6,207
Foreign direct investment (net, incl. privatization)	3,970	3,308	3,428	3,363	3,700	4,700	4,725	5,480	6,133
Other investment (net) [1]	-504	-1,333	-499	676	-293	15	-48	122	74
Federal government	706	274	1,944	405	137	940	612	353	687
Disbursements [1]	973	616	2,372	1,090	1,855	1,830	1,532	1,435	1,900
Amortization [1]	-267	-343	-429	-685	-1,718	-890	-920	-1,082	-1,214
Other public sector [1,2]	-1,070	-1,668	-860	844	-430	-925	-660	-230	-613
Disbursements	420	291	541	2,536	914	300	319	545	212
Amortization [1]	-1,490	-1,959	-1,401	-1,692	-1,345	-1,226	-979	-775	-825
Private sector borrowing (net)	153	0	0	0	0	0	0	0	0
Other (net)	-293	62	-1,583	-572	0	0	0	0	0
Errors and omissions	-339	520	897	0	0	0	0	0	0
Overall balance	-41	-2,639	-809	-1,906	-2,671	83	637	2,057	2,512
Financing	41	2,639	809	1,906	2,671	-83	-637	-2,057	-2,512
Central bank (net; increase –)	238	1,371	469	-197	-134	-1,820	-1,489	-2,756	-1,377
Reserves (increase –)	244	1,371	469	15	-1,781	-2,275	-1,945	-3,193	-1,338
Liabilities (increase +)	-6	0	0	-212	1,647	455	456	437	-39
IMF credit (net)	-6	0	0	-212	1,647	455	456	437	-39
of which: IMF Rapid Financing Instrument (RFI)	…	…	…	…	…	…	…	…	…
SDR allocation	0	397	0	0	0	0	0	0	0
Prospective donor financing	0	0	0	0	1,500	1,000	700	550	0
of which: grants	*0*	*0*	*0*	0	1,000	*0*	*0*	*0*	*0*
Exceptional Financing	488	720	475	2,103	1,905	737	152	149	-1,135
Debt service restructuring [3]	250	663	475	2,103	1,905	737	152	149	-1,135
Reprofiling of external sovereign deposits at NBE, 2020			*475*	*288*	*0*	*0*	*0*	*0*	*0*
first phase of reprofiling during the prev. prog. (UAE)	*250*	*250*	*250*	*125*	*0*	*0*	*0*	*0*	*0*
Reprofiling from Saudi	*0*	*413*	*225*	*163*	*0*	*0*	*0*	*0*	*0*
Standstill agreement with Official Bilateral Creditors [4]			*0*	*1,815*	*856*	*92*	*-339*	*-1,165*	*-1,135*
Other restructuring (incl. pros. G20 CF)	*0*	*0*	*0*	*0*	*1,050*	*646*	*491*	*1,313*	*0*
G20 Debt Service Suspension Initiative [3]	231	57	0	0	0	0	0	0	0
IMF CCR Trust debt relief [5]	7	1	0	0	0	0	0	0	0
Commercial banks (net; increase –)	-685	548	-135	0	-600	0	0	0	0
(Annual percentage change, unless otherwise indicated)									
Memorandum items :									
Exports of goods	21.1	13.4	-11.8	-1.6	2.3	24.3	28.4	26.4	12.9
Imports of goods	2.9	26.6	-5.3	0.5	9.0	5.4	9.3	11.0	7.8
Services exports	4.4	29.7	13.0	6.6	10.5	11.0	12.0	11.9	3.5
Services imports	0.4	19.2	12.4	5.9	7.9	7.3	14.5	13.9	4.3
Private transfers	18.0	15.7	-4.0	-12.2	14.7	11.3			
Exports of goods and services (percent of GDP)	7.6	8.2	6.6	5.4	8.9	9.6	10.0	10.4	9.9
Imports of goods and services (percent of GDP)	-16.7	-18.3	-14.0	-11.2	-18.6	-18.5	-18.2	-18.1	-17.2
Trade balance (percent of GDP)	-9.6	-11.0	-8.3	-6.5	-11.1	-10.5	-9.7	-9.1	-8.5
Private transfers (net, percent of GDP)	5.5	5.6	4.2	2.9	5.0	5.2	5.2	5.3	5.1
Gross official reserves (millions U.S. dollars)	2,866	1,495	1,026	1,011	2,793	5,067	7,012	10,205	11,543
(Months of following year's imports of goods and services)	1.5	0.8	0.5	0.5	1.2	2.0	2.5	3.5	3.6

Sources: Ethiopian authorities and IMF staff estimates and projections.

[1] Excludes prospective donor financing and/or exceptional financing.

[2] Includes net borrowing by state-owned enterprises and the central bank's long-term non-IMF liabilities.

[3] Staff estimates.

[4] Represents standstill agreement with official bilateral creditors as for debt service falling due in CY2023 and CY2024 (staff estimate).

[5] Currently available on debt service to the Fund falling due until January 10, 2022. Subsequent relief is contingent on availability of financing for the Trust.

Table 4b. The Federal Democratic Republic of Ethiopia: Summary Balance of Payments, 2020/21–2028/29

(In percent of GDP)

	2020/21 Act.	2021/22 Act.	2022/23 Prel.	2023/24 IMF Staff Proj.	2024/25 IMF Staff Proj.	2025/26 IMF Staff Proj.	2026/27 IMF Staff Proj.	2027/28 IMF Staff Proj.	2028/29 IMF Staff Proj.
	(Percent of GDP, unless otherwise indicated)								
Current account balance [1]	-2.8	-4.0	-2.8	-2.8	-4.5	-3.2	-2.5	-1.9	-1.8
Excl. official transfers [1]	-4.1	-4.9	-3.5	-3.4	-5.5	-4.3	-3.5	-2.9	-2.6
Trade balance	-9.6	-11.0	-8.3	-6.5	-11.1	-10.5	-9.7	-9.1	-8.5
Exports of goods	3.3	3.2	2.2	1.7	2.7	3.1	3.6	4.0	4.0
Coffee	0.8	1.1	0.8	0.6	1.1	1.1	1.2	1.3	1.2
Oil seeds	0.3	0.2	0.2	0.1	0.2	0.2	0.2	0.2	0.1
Gold	0.6	0.4	0.1	0.1	0.2	0.3	0.4	0.4	0.4
Other	1.5	1.5	1.1	0.9	1.2	1.6	1.8	2.1	2.2
Imports of goods	-12.8	-14.3	-10.5	-8.2	-13.8	-13.6	-13.2	-13.0	-12.6
Fuel	-1.7	-2.7	-2.5	-1.8	-2.7	-3.1	-2.9	-2.8	-2.6
Services (net)	0.5	1.0	0.9	0.7	1.4	1.6	1.5	1.4	1.2
Exports	4.4	5.0	4.4	3.7	6.2	6.5	6.4	6.4	5.9
Imports	-3.9	-4.1	-3.5	-2.9	-4.8	-4.9	-5.0	-5.0	-4.7
Income (net) [1]	-0.5	-0.5	-0.3	-0.4	-0.8	-0.6	-0.5	-0.5	-0.4
Private transfers (net)	5.5	5.6	4.2	2.9	5.0	5.2	5.2	5.3	5.1
Official transfers (net) [1]	1.2	0.9	0.7	0.5	1.0	1.1	1.0	0.9	0.9
Capital account balance [1]	3.1	1.6	1.8	1.9	2.5	3.2	2.9	3.0	3.0
Foreign direct investment (net, incl. privatization)	3.6	2.6	2.1	1.6	2.7	3.2	2.9	3.0	3.0
Other investment (net) [1,2]	-0.5	-1.1	-0.3	0.3	-0.2	0.0	0.0	0.1	0.0
Federal government	0.6	0.2	1.2	0.2	0.1	0.6	0.4	0.2	0.3
Disbursements [1]	0.9	0.5	1.4	0.5	1.4	1.3	0.9	0.8	0.9
Amortization [1]	-0.2	-0.3	-0.3	-0.3	-1.3	-0.6	-0.6	-0.6	-0.6
Other public sector [1]	-1.0	-1.3	-0.5	0.4	-0.3	-0.6	-0.4	-0.1	-0.3
Disbursements	0.3	0.2	0.3	1.9	0.6	0.2	0.2	0.3	
Amortization [1]	-1.2	-1.2	-0.7	-1.2	-0.9	-0.8	-0.6	-0.4	
Private sector borrowing (net)	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other (net)	-0.3	0.0	-1.0	-0.3	0.0	0.0	0.0	0.0	0.0
Errors and omissions	-0.3	0.4	0.5	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	0.0	-2.1	-0.5	-0.9	-2.0	0.1	0.4	1.1	1.2
Financing	0.0	2.1	0.5	0.9	2.0	-0.1	-0.4	-1.1	-1.2
Central bank (net; increase –)	0.2	1.1	0.3	-0.1	-0.1	-1.3	-0.9	-1.5	-0.7
Reserves (increase –)	0.2	1.1	0.3	0.0	-1.3	-1.6	-1.2	-1.7	-0.6
Liabilities (increase +)	0.0	0.0	0.0	-0.1	1.2	0.3	0.3	0.2	0.0
IMF credit (net)	0.0	0.0	0.0	-0.1	1.2	0.3	0.3	0.2	0.0
of which: IMF Rapid Financing Instrument (RFI)	...	...	...	...	...	...			
SDR allocation	0.0	0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Prospective donor financing	0.0	0.0	0.0	0.0	1.1	0.7	0.4	0.3	0.0
of which: grants	*0.0*	*0.0*	*0.0*	*0.0*	0.7	*0.0*	0.0	0.0	0.0
Exceptional Financing	0.4	0.6	0.3	1.0	1.4	0.5	0.1	0.1	-0.6
Debt service restructuring [3]	0.2	0.5	0.3	1.0	1.4	0.5	0.1	0.1	-0.6
Reprofiling of external sovereign deposits at NBE, 2020			*0.3*	*0.1*	*0.0*	*0.0*	0.0	0.0	0.0
Standstill agreement with Official Bilateral Creditors [4]		*0.0*	*0.0*	*0.9*	*0.6*	*0.1*	-0.2	-0.6	
Other restructuring (incl. pros. G20 CF)	*0.0*	*0.0*	*0.0*	*0.0*	*0.8*	*0.4*	0.3	0.7	0.0
G20 Debt Service Suspension Initiative (DSSI) [3]	*0.2*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*	0.0	0.0	0.0
IMF CCR Trust debt relief [5]	0.0	0.0	0.0	0.0	0.0	0.0	0.0	N.A.	N.A.
Commercial banks (net; increase –)	-0.6	0.4	-0.1	0.0	-0.4	0.0	0.0	0.0	0.0
Gross official reserves	2.6	1.2	0.6	0.5	2.1	3.5	4.3	5.5	5.6

Sources: Ethiopian authorities and IMF staff estimates and projections.

[1] Excludes prospective donor financing and/or exceptional financing.

[2] Includes net borrowing by state-owned enterprises and the central bank's long-term non-IMF liabilities.

[3] Staff estimates.

[4] Represents standstill agreement with official bilateral creditors as for debt service falling due in CY2023 and CY2024 (staff estimate).

[5] Currently available on debt service to the Fund falling due until January 10, 2022. Subsequent relief is contingent on availability of financing for the Trust.

Table 5. The Federal Democratic Republic of Ethiopia: Financial Soundness Indicators of the Banking Sector

	Jun-19	Jun-20	Jun-21	Jun-22	Jun-23
Capital adequacy					
Capital to Risk-Weighted Assets	19.9	18.4	15.2	16.3	14.7
Capital to Assets	8.0	7.6	6.9	7.5	7.8
Asset quality					
NPLs to Total Loans [1]	2.3	3.0	3.5	3.9	3.6
Earning and profitability					
Return on Assets	2.9	1.7	1.9	2.4	2.0
Return on Equity[2]	17.5	14.3	26.6	32.6	25.7
Liquidity					
Liquid Assets to Total Assets	13.0	13.4	15.5	21.0	19.3

Sources: National Bank of Ethiopia

[1]Reported NPLs exclude non-performing government-guaranteed SOE debts, and are not adjusted for the results of the CBE AQR.

[2]The average capital used to calculate the ROE execludes retained earning and profit & loss.

Table 6. The Federal Democratic Republic of Ethiopia: External Financing Requirements and Sources, 2023/24–2027/28

(In millions of U.S. dollars, unless otherwise indicated)

	2023/24	2024/25 Program	2025/26 Program	2026/27 Program	2027/28 Program	Cumulative (FY2024/25-2027/28)
External financing requirement	**9,692**	**13,146**	**10,646**	**9,594**	**10,373**	**43,758**
Current account deficit, excl. official transfers	7,117	7,479	6,199	5,693	5,246	24,618
Federal government amortization	685	1,718	890	920	1,082	4,610
Other public sector amortization[1]	1,692	1,345	1,226	979	775	4,325
Repayments to Fund	212	223	56	57	75	411
Change in gross reserves (increase +)	-15	1,781	2,275	1,945	3,193	9,194
Change in commercial bank reserves (increase +)	0	600	0	0	0	600
External financing sources	**6,417**	**6,469**	**6,180**	**6,576**	**7,460**	**26,685**
Foreign direct investment, excl. privatization	3,363	3,700	4,050	4,725	5,480	17,955
External loans to Federal government	1,090	1,855	1,830	1,532	1,435	6,652
Other public sector external borrowing	2,536	914	300	319	545	2,079
Other (net, incl. change in commercial banks' NFA)	-572	0	0	0	0	0
Financing gap (need for financing +)	**3,275**	**6,676**	**4,466**	**3,018**	**2,913**	**17,073**
Expected financing	**3,275**	**2,257**	**2,309**	**1,314**	**536**	**6,416**
Official transfers	1,139	1,401	1,567	1,653	1,701	6,323
Privatization proceeds	0	0	650	0	0	650
Reprofiling of external sovereign deposits at NBE, 2020 [2]	288	0	0	0	0	0
Standstill agreement with Official Bilateral Creditors [3]	1,815	856	92	-339	-1,165	-557
Accumulation of arrears	33					
Residual gap	**0**	**4,419**	**2,157**	**1,704**	**2,376**	**10,656**
IMF	0	1,870	511	512	513	3,406
Disbursements	*0*	*1,870*	*511*	*512*	*513*	3,406
Prospective debt restructuring	0	1,050	646	491	1,313	3,500
Prospective budget support	0	1,500	1,000	700	550	3,750
Memorandum items :						
Gross official reserves (millions U.S. dollars)	1,011	2,793	5,067	7,012	10,205	
(Months of following year's imports of goods and services)	0.5	1.2	2.0	2.5	3.5	

Sources: IMF staff projections and estimates.

[1] Includes guaranteed and non-guaranteed SOE loans and long-term debt of National Bank of Ethiopia (NBE).

[2] Represents reprofiling that was finalized under the previous ECF/EFF program and through recent negotiation.

[3] Represents standstill agreement with official bilateral creditors as for debt service falling due in CY2023 and CY2024 (staff estimate).

Table 7. The Federal Democratic Republic of Ethiopia: Proposed Access and Phasing Under the Extended Credit Facility

Date of availability	Condition for disbursement	Amount		Percent of quota[1]	
		SDR million	Percent share of total	Specific review	Cumulative
At Program Approval	Executive Board approval of the ECF arrangement	766.75	30.0	255.0	255.0
September 10, 2024	Observance of continuous performance criteria (PCs) and PCs for August 16, 2024 and completion of the first review	255.60	10.0	85.0	340.0
December 10, 2024	Observance of continuous PCs and PCs for end-September 2024 and completion of the second review	191.70	7.5	63.8	403.7
April 15, 2025	Observance of continuous PCs and PCs for end-December 2024 and completion of the third review	191.70	7.5	63.8	467.5
October 15, 2025	Observance of continuous PCs and PCs for end-June 2025 and completion of the fourth review	191.70	7.5	63.8	531.2
April 15, 2026	Observance of continuous PCs and PCs for end-December 2025 and completion of the fifth review	191.70	7.5	63.8	595.0
October 15, 2026	Observance of continuous PCs and PCs for end-June 2026 and completion of the sixth review	191.70	7.5	63.8	658.7
April 15, 2027	Observance of continuous PCs and PCs for end-December 2026 and completion of the seventh review	191.70	7.5	63.8	722.5
October 15, 2027	Observance of continuous PCs and PCs for end-June 2027 and completion of the eighth review	191.70	7.5	63.8	786.2
April 15, 2028	Observance of continuous PCs and PCs for end-December 2027 and completion of the ninth review	191.70	7.5	63.8	850.0
	Total	2555.95	100.0	850.0	

Source: IMF staff calculations.

[1] Ethiopia's quota is SDR 300.7 million.

Table 8. The Federal Democratic Republic of Ethiopia: Indicators of Fund Credit, 2023/24–2038/39[1,4]

(In millions of SDR, unless stated otherwise)

	2023/24	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30	2030/31	2031/32	2032/33	2033/34	2034/35	2035/36	2036/37	2037/38	2038/39
Fund obligations based on existing credit																
(In millions of SDR)																
Principal	7.5	165.4	41.8	41.8	55.1	28.4	34.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Charges and interest (excl. obligations to SDR department)	0.0	9.0	3.4	2.6	1.8	1.1	0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Fund obligations based on existing and prospective credit [2]																
(In millions of SDR)	7.5	174.4	45.1	44.4	57.0	29.5	156.0	300.3	377.0	453.7	587.9	313.1	210.9	134.2	57.5	0.0
Principal	7.5	165.4	41.8	41.8	55.1	28.4	155.7	300.3	377.0	453.7	587.9	313.1	210.9	134.2	57.5	0.0
PRGT	0.0	0.0	26.7	26.7	40.1	13.4	148.1	300.3	377.0	453.7	587.9	313.1	210.9	134.2	57.5	0.0
EFF	7.5	15.0	15.0	15.0	15.0	15.0	7.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
RFI	0.0	150.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Charges and interest (excl. obligations to SDR department)	0.0	9.0	3.4	2.6	1.8	1.1	0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total obligations based on existing and prospective credit [2]																
In millions of SDRs	7.5	174.4	45.1	44.4	57.0	29.5	156.0	300.3	377.0	453.7	587.9	313.1	210.9	134.2	57.5	0.0
In millions of U.S. dollars	10.0	231.9	60.2	59.3	76.3	39.5	209.0	402.4	505.1	607.9	787.7	419.5	282.5	179.8	77.1	0.0
In percent of general government revenue	0.1	2.1	0.4	0.3	0.4	0.2	0.8	1.4	1.5	1.7	1.9	0.9	0.6	0.3	0.1	0.0
In percent of exports of goods and services	0.1	1.9	0.4	0.4	0.4	0.2	1.0	1.7	2.0	2.1	2.5	1.2	0.7	0.4	0.2	0.0
In percent of total external debt service	0.7	6.7	2.0	1.9	1.9	1.0	5.1	14.3	17.2	20.1	27.3	14.4	10.6	7.3	3.1	0.0
In percent of gross international reserves	1.0	8.3	1.2	0.8	0.7	0.3	1.8	3.0	3.4	3.9	4.7	2.4	1.5	0.9	0.4	0.0
In percent of GDP	0.0	0.2	0.0	0.0	0.0	0.0	0.1	0.2	0.2	0.2	0.2	0.1	0.1	0.0	0.0	0.0
In percent of quota	2.5	58.0	15.0	14.8	18.9	9.8	51.9	99.9	125.4	150.9	195.5	104.1	70.1	44.6	19.1	0.0
Outstanding Fund credit (end of period)																
In millions of SDRs	366.7	1,607.1	1,948.7	2,290.4	2,618.6	2,590.2	2,434.6	2,134.3	1,757.2	1,303.6	715.7	402.6	191.7	57.5	0.0	0.0
In millions of U.S. dollars	488.2	2,137.7	2,598.3	3,061.1	3,508.5	3,470.5	3,261.9	2,859.5	2,354.4	1,746.5	958.9	539.4	256.8	77.1	0.0	0.0
In percent of general government revenue	3.3	21.3	19.2	17.9	17.5	15.1	12.6	9.9	7.3	4.9	2.4	1.2	0.5	0.1	0.0	0.0
In percent of exports of goods and services	4.4	17.7	18.7	18.8	18.4	17.0	15.6	12.2	9.2	6.1	3.0	1.5	0.7	0.2	0.0	0.0
In percent of total external debt	1.4	5.7	6.6	7.5	8.3	8.4	8.1	7.1	5.8	4.3	2.4	1.3	0.6	0.2	0.0	0.0
In percent of gross international reserves	48.3	76.5	51.3	43.7	34.4	30.1	27.9	21.4	15.7	11.2	5.7	3.0	1.3	0.4	0.0	0.0
In percent of GDP	0.2	1.6	1.8	1.9	1.9	1.7	1.4	1.1	0.8	0.6	0.3	0.1	0.1	0.0	0.0	0.0
In percent of quota	121.9	534.4	648.1	761.7	870.8	861.4	809.6	709.8	584.4	433.5	238.0	133.9	63.8	19.1	0.0	0.0
PRGT	44.4	511.9	630.6	749.2	863.3	858.9	809.6	709.8	584.4	433.5	238.0	133.9	63.8	19.1	0.0	0.0
EFF	27.5	22.5	17.5	12.5	7.5	2.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
RFI	50.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net use of Fund credit (millions of SDR)	-7.5	1,240.4	341.6	341.6	328.3	-28.4	-155.7	-300.3	-377.0	-453.7	-587.9	-313.1	-210.9	-134.2	-57.5	0.0
Disbursements	0.0	1,405.8	383.4	383.4	383.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repayments and repurchases	7.5	165.4	41.8	41.8	55.1	28.4	155.7	300.3	377.0	453.7	587.9	313.1	210.9	134.2	57.5	0.0
Debt relief under the CCRT [3]	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:																
General government revenue (billions of birr)	857.9	1,311.7	1,934.4	2,611.8	3,241.3	3,913.7	4,576.0	5,338.6	6,188.8	7,217.3	8,322.1	9,575.8	10,977.7	12,608.9	14,346.5	16,250.0
Exports of goods and services (billions of U.S. dollars)	11.2	12.1	13.9	16.3	19.1	20.5	21.0	23.4	25.5	28.6	31.9	35.5	38.8	42.7	46.9	51.2
Total debt service (millions of U.S. dollars)																
Gross international reserves (billions of U.S. dollars)	1.0	2.8	5.1	7.0	10.2	11.5	11.7	13.4	15.0	15.6	16.7	17.7	19.1	19.9	21.0	23.5
In months of prospective imports	0.5	1.2	2.0	2.5	3.5	3.6	3.4	3.6	3.6	3.4	3.4	3.3	3.2	3.1	3.1	3.2
Nominal GDP (billions of U.S. dollars)	208.7	136.2	145.3	163.6	184.0	205.9	229.0	255.1	282.0	312.1	344.0	378.8	415.9	456.1	499.2	544.7
SDR per U.S. dollar (period average)	0.8	0.8	0.8	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7
Quota (millions of SDR)	300.7	300.7	300.7	300.7	300.7	300.7	300.7	300.7	300.7	300.7	300.7	300.7	300.7	300.7	300.7	300.7

Source: IMF staff estimates and projections.

[1] Year ending in June.

[2] Including the proposed disbursements under the new ECF.

[3] Currently available on debt service to the Fund falling due until October 15, 2021. Subsequent relief is contingent on availability of financing for the Trust.

[4] Projected obligations and outstanding credit to IMF is as of June 2024.

Table 9. The Federal Democratic Republic of Ethiopia: Quantitative Performance Criteria and Indicative Targets, June 2024–June 2025

(In millions of Ethiopian birr, unless otherwise indicated)

	end-Jun 2024	Aug. 16, 2024	end-Sep 2024	end-Dec 2024	end-Mar 2025	end-Jun 2025
	Staff est. Initial level	Program target	Program target	Program target	Indicative target	Program target
Quantitative performance criteria						
Net financing of the general government primary balance (ceiling, cumulative change since previous June, includes grants and excludes interest payments) [1/, 2/]	146,000	N/A	42,000	69,000	95,000	106,000
Net international reserves (floor, cumulative change since previous June, US$ millions) (end-Jun 2024 is for initial level)	512	630	500	400	300	100
Tax revenue collected by the federal government (floor, cumulative sum of tax revenues collected since the beginning of the current fiscal year)	384,000	N/A	86,000	192,000	347,000	578,000
Net NBE claims on the general government (ceiling, cumulative change since previous June) (end-June 2024 for initial level)	616,300	0	0	0	0	0
Continuous performance criteria						
Contracting or guaranteeing of external non-concessional debt by the general government, the NBE and public enterprises (ceiling, US$ millions) [3/]		0	0	0	0	0
Accumulation of external payment arrears by the general government, the NBE and public enterprises (ceiling, US$ millions)		0	0	0	0	0
Indicative targets						
Gross claims on public enterprises by commercial banks (ceiling, cumulative change since previous June) (end-Jun 2024 is for initial level) [2/]	760,775	N/A	37,000	74,000	110,000	147,000
Government Contributions to Productive Safety Net Programme cash transfers (floor, cumulative sum of contributions since the beginning of the current fiscal year) [4/]	9,000	N/A	6,500	22,100	33,200	51,400
Present value of external new debt (excluding IMF credit) contracted or guaranteed by the general government, the NBE and public enterprises (ceiling for the fiscal year ending June, US$ millions)		N/A	2,000	2,500	2,750	3,000
Memorandum items:						
Official external grants disbursed to the government (US$ millions, cumulative since previous June)	791		210	420	630	840
Official external loans disbursed to the government (US$ millions, cumulative since previous June)	627		1638	1775	1913	2050
Gross privatization proceeds (US$ millions, cumulative since previous June)	0	0	0	0	0	0

Sources: Ethiopian authorities and IMF staff estimates and projections.

1/ Excluding on-lending from the general government.

2/ Excludes commercial banks' claims related to Addis Ababa Housing credit.

3/ The limit is a continuous target (ceiling) on the contracting of non-concessional debt for the fiscal year by the government including general government, NBE and public enterprises (see TMU). An exception is applied for new non-concessional external debt contracted or guaranteed by the general government for the Koysha dam project, which is capped at USD 950 over the duration of the program.

4/ Excludes in-kind benefits and donor contributions. Includes Government of Ethiopia contributions to cash transfers to beneficiaries under the rural Productive Safety Net Programme (PSNP) and Urban Productive Safety Net Programme (UPSNP).

Table 10. The Federal Democratic Republic of Ethiopia: Proposed Prior Actions

Measure	Rationale	Status
1. NBE to publish a directive announcing that Authorized Dealers can buy and sell FX from their clients and among themselves at freely negotiated rates, allowing market participants to determine a market-clearing exchange rate for current account transactions; and in consultation with Fund staff, eliminate the current account controls (the rationing of FX allocations for imports and the three-tier priority list of imports, the NBE import reference price system linked to minimum import prices by customs office, and the security deposit requirement of 50 percent when queuing for FX for import payments), removal of which is necessary for reaching market unification, with immediate effect, and publicly communicate the same.	Liberalization of foreign exchange market	To be completed
2. Introduction of an excise stamp regime, including finalizing the excise stamp tender, issuing excise stamp track and tracing directive, and issuing a circular on adjusting for inflation on specific excise rate on beer.	Tax revenue mobilization	Completed
3. Adoption by MoF of VAT directive to remove exemptions less targeted to the poor, to be specified in consultation with the Fund.	Tax revenue mobilization	Completed
4. The Federal Auditor General has authorized NBE to engage a new auditor; NBE to adopt a selection and rotation policy for an external auditor; and NBE to float a competitive bid for the audit starting with 2022/23 financial statements by a suitably qualified firm that includes international experts experienced in auditing central banks.	Update and modernize governance of the NBE and reduce vulnerability to corruption	Completed
5. The Federal Government to make a capital injection in the Commercial Bank of Ethiopia (CBE) with government securities in an amount equal to (i) CBE's claim on LAMC; (ii) the fully provisioned amount of CBE's claims on EEP; and (iii) the residual amount required to bring CBE's capital adequacy ratio up to the regulatory minimum.	Financial sector stability	Completed
6. Announcement of a target monetary policy rate of 15 percent, at the mid-point between the standing lending and deposit facility rates, set at ± 3 percent around the policy rate, with the interbank lending rate as an operational target	Reduce financial repression	Completed
7. NBE to begin conducting regular fixed rate (the policy rate) and full allotment open market operations before the move to a market-clearing exchange rate to manage banking sector liquidity, aligned to the monetary policy stance.	Strengthen monetary policy implementation	Completed

Table 11. The Federal Democratic Republic of Ethiopia: Proposed Structural Benchmarks

Measure	Rationale	Target Date
1. Council of Ministers to adopt and publish a medium-term revenue strategy (drawing on FAD TA) specifying tax policy and revenue administration compliance measures with a clear timeframe.	Tax revenue mobilization	End-September 2024
2. NBE to issue an order to all banks not in compliance with the regulatory threshold on net open position to develop plans to ensure full compliance with the regulation by end-June 2025.	Financial sector stability	End-September 2024
3. Publish IFRS-based and audited financial statements for 2022/23 for Ethiopian Electric Power (EEP), Ethiopian Electric Utility (EEU), and Ethiopia Petroleum Supply Enterprise (EPSE); and for 2021/22 for Ethiopian Sugar Corporation (ESC), Ethiopian Railway Corporation (ERC), Ethiopian Engineering Group (EEG), and Ethiopian Construction Works (ECW).	Strengthen SOE finances and reduce vulnerability to corruption	End-September 2024
4. NBE to implement an emergency liquidity assistance framework for financial stability purposes provided at the discretion of NBE to viable (solvent) banks with adequate collateral and a funding plan to recover the liquidity situation of the bank	Strengthen monetary policy implementation	End-September 2024
5. Implement the first quarterly electricity tariff increase under the multi-year plan as approved by the Council of Ministers in June 2024.	Strengthen SOE finances	End-September 2024
6. The NBE to finalize and publish audited financial statements for 2021/22-2022/23.	Update and modernize governance of the NBE	End-December 2024
7. NBE to submit to Parliament comprehensive draft legal amendments to the NBE Proclamation, to be prepared in consultation with IMF staff, with respect to the NBE's mandate, decision-making structure (internal check and balances and collegial implementation of decisions), accountability, transparency, and autonomy.	Update and modernize governance of the NBE	End-December 2024

Annex I. External Sector Assessment

Ethiopia's external position in 2022/23 is assessed to be substantially weaker than the level implied by medium-term fundamentals and desired macroeconomic policies. Significant policy adjustment is needed to address macroeconomic imbalances, including exchange rate and current account liberalization, and structural reforms. Tightening of monetary policy, coupled with reforms of SOEs to improve financial soundness, would help to support the exchange rate reform by lowering inflation and alleviating pressures on current account balance.

A. The Current Account

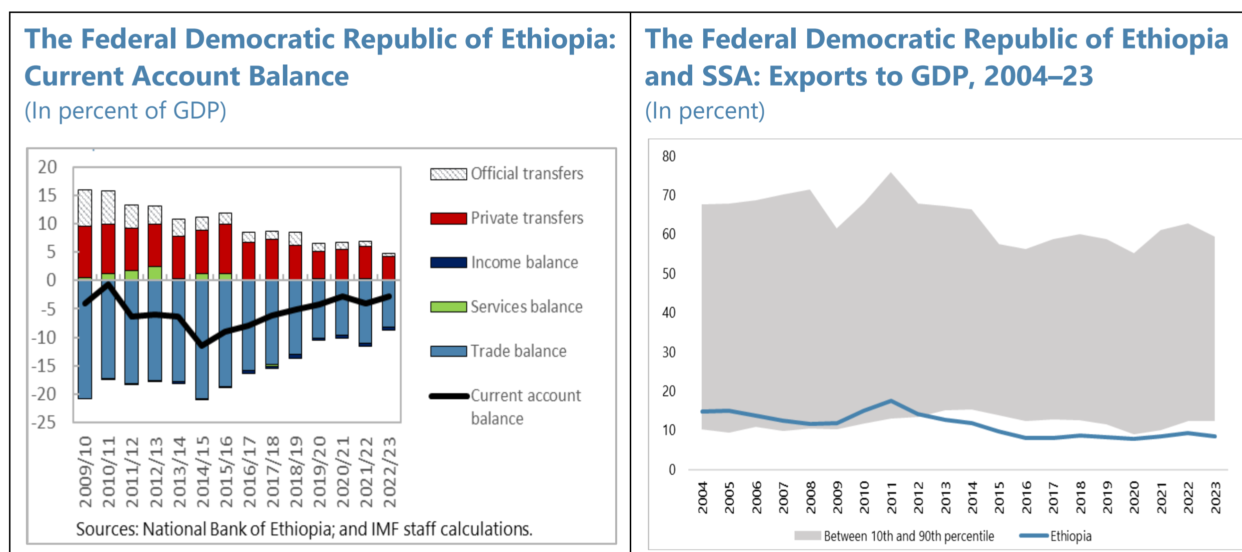
Background

1. **Ethiopia's current account (CA) deficit is driven by a large goods trade deficit.** The deficits reflect low and declining exports-to-GDP ratios and, historically, a debt-financed public sector investment-led growth model, which relied on imports. The trade deficit peaked in 2014/15 (20.8 percent of GDP) before declining due to stricter control of public investment and worsening foreign exchange (FX) shortages that constrained imports. The CA deficit shrank from 6.2 to 2.8 percent of GDP between 2017/18 and 2020/21, before widening to 4 percent of GDP in 2021/22 as import prices for fuel, fertilizer, and food rose. In 2022/23, the CA deficit declined to 2.8 percent of GDP, with a sharp import contraction due to acute FX shortages outweighing lower exports and private transfers.

- Goods exports declined by 12 percent in 2022/23 down from growth of 13 percent the year before. FX market distortions may have contributed to hoarding or smuggling of export items as well disincentives for production. The goods exports-to-GDP ratio, at 2.2 percent in 2022/23, is among the lowest in Sub-Saharan Africa (see chart, for total exports).
- Services exports growth moderated to 13 percent in 2022/23, after a sharp pick-up to 30 percent in 2021/22. Service exports are mainly driven by Ethiopian Airlines. The services exports-to-GDP ratio is 4.4 percent of GDP.
- Imports contracted in 2022/23, driven by goods imports as public sector investment was cut and constraints to private imports due to FX shortages and import bans on 38 items. Imports fell from 18.3 percent of GDP in 2021/22 to 14.0 percent in 2022/23.
- The goods trade deficit narrowed to 8.3 percent of GDP in 2022/23 from 11.0 percent in 2021/22 as the decline in the much larger imports more than offset the decline in exports.

2. **Goods exports are undiversified, concentrated in low value-added agricultural products (coffee, flowers, oil seeds, khat, and pulses).** The agricultural sector is characterized by low labor productivity and rain-fed production, making the export basket susceptible to shocks, climate disasters, and global price movements. Gold exports declined in 2022/23 after expanding during 2019/20–2020/21. The share of manufactured goods in total exports had grown to 13.5 percent in 2018/19, from a small base, but declined sharply thereafter to 7.1 percent in

2022/23, due to the pandemic, conflict, suspension from AGOA, and FX shortages that limited availability of intermediate imports.



The Federal Democratic Republic of Ethiopia: Current Account Balance
(In percent of GDP)

Sources: National Bank of Ethiopia; and IMF staff calculations.

The Federal Democratic Republic of Ethiopia and SSA: Exports to GDP, 2004–23
(In percent)

Assessment

3. **The EBA-lite model shows that in 2022/23 the CA balance was weaker than the level implied by medium-term fundamentals and desired policies.** Considering the sharp import contraction due to tight FX rationing (e.g., the ban on imports of 38 items) staff assesses that the CA balance is substantially weaker than the level implied by medium-term fundamentals and desired policies. The model-identified CA gap is about -2.2 percent of GDP, with a cyclically adjusted CA of -5.3 percent and CA norm of -3.1 percent of GDP.

- Model-estimated policy gaps contribute about 0.4 percent of GDP to the CA gap, where both external and domestic factors largely balance each other out.[1] The deviation in the fiscal deficit from its desired level is less significant compared to the rest of world, which aids in narrowing the CA gap. However, an increase in international reserves is needed to achieve adequate levels, contributing to the widening of the CA gap (given persistent CA deficits, Ethiopia is considered a net borrower economy).
- The current account norm is adjusted upwards by 1.0 percentage points, from -4.1 percent to -3.1 percent of GDP, to reflect the need to reach a moderate CA deficit to achieve medium-term external sustainability. The adjustment aligns the norm with the highest model estimated level of net international investment positions (IIP) to GDP in the past (around -28 percent of GDP).
- The cyclically adjusted CA balance is subject to additional model-based adjustment due to an impact of natural disasters and conflicts (2.4 percent of GDP).

[1] The overall policy gap, as a share of GDP, comprises fiscal policy 1.4 percent; public health expenditure 1.7 percent; changes in reserves –2.2 percent; private credit level 0.04 percent; private credit growth 0.5 percent; and capital controls -1.5 percent.

4. Staff considers the overall external sector assessment to be substantially weaker given the recent policy measures that have led to sharp FX rationing and import contraction in 2022/23. FX rationing was further tightened amid acute FX shortage including through an import ban of 38 items (including packaged foods, furniture, beauty products, automobiles, and alcoholic beverages). Consumer goods imports fell to 3.7 percent of GDP in 2022/23 from 6 percent in 2021/22, the lowest level in the past decade, matching those observed during the height of the COVID-19 pandemic. This contrasts sharply with the pre-COVID average of consumer goods imports to GDP, which stood at 6.9 percent. Over the last ten years, the average ratio of consumer goods imports to GDP has been 6.2 percent. REER overvaluation is estimated at 52 percent. To account for the contraction in imports due to shortages and policy measures, the actual CA balance is adjusted downward by 2.5 percentage points of GDP, widening the CA gap to -4.7 percent of GDP. This corresponds to 52 percent REER overvaluation using -0.09 elasticity of CA balance to REER.

Annex II. Table 1. The Federal Democratic Republic of Ethiopia: Assessment for 2022/23

(In percent of GDP)

	CA model [1/]	REER model [1/]
	(in percent of GDP)	
CA-Actual	**-2.8**	
Cyclical contributions (from model) (-)	0.1	
Additional temporary/statistical factors (-)	0.0	
Natural disasters and conflicts (-)	2.4	
Adjusted CA	**-5.3**	
CA Norm (from model)[2/]	**-4.1**	
Adjustments to the norm (-)	1.0	
Adjusted CA Norm	**-3.1**	
CA Gap	**-2.2**	**-4.0**
o/w Relative policy gap	0.4	
Elasticity	-0.1	
REER Gap (in percent)	**24.7**	**44.5**

Source: IMF staff estimates.

[1/] Based on the EBA-lite 3.0 methodology.

[2/] Cyclically adjusted, including multilateral consistency adjustments.

4. Measures to boost competitiveness, resolve FX shortages, diversify the export basket, and improve the business climate are needed to durably reduce external imbalances. Addressing the increasingly overvalued exchange rate is urgently needed to improve external competitiveness. Comprehensive reforms are needed to improve the business environment to facilitate private investment and diversify the export base, boost export competitiveness, and increase resilience to exogenous shocks. Sufficient and reliable access to credit and imported

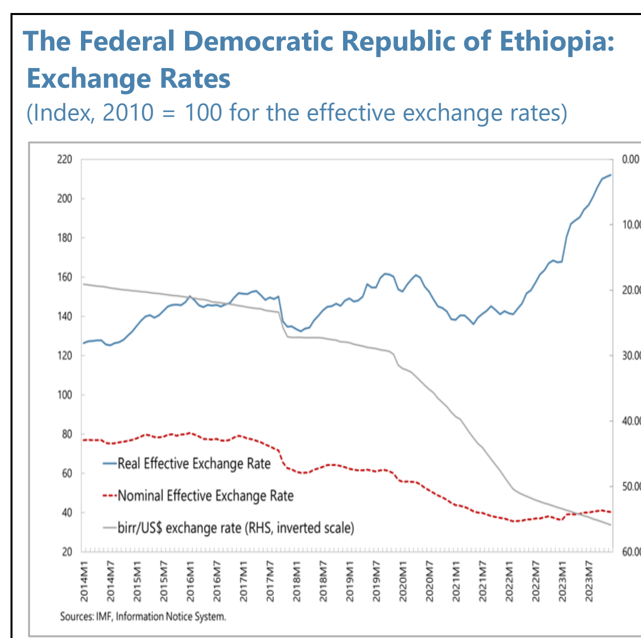
intermediate inputs is important for supporting exports, especially higher value-added manufactured goods that are part of global and regional supply chains. Improving the efficiency of trade and border logistics is important to lower trade costs. Reform of SOEs to improve their operational performance and finance investment needs sustainably would help support an improvement in the CA balance over the medium term.

B. Real Exchange Rate

Background

5. The real effective exchange rate (REER) has appreciated steadily, as inflation differentials have more than offset trend depreciation in the nominal effective exchange rate (NEER). The REER appreciated by around 70 percent between January 2014 and March 2024. The nominal value of the Birr has been managed to depreciate slowly against the US dollar, except for a step devaluation in October 2017. The pace of depreciation was moderately faster under the 2019 ECF-EFF, but the weaker NEER has been offset by the inflation differential with the trading partners. Inflation has risen sharply from an average of 8 percent in 2013/14 to 28 percent in 2022/23.

The Federal Democratic Republic of Ethiopia: Exchange Rates
(Index, 2010 = 100 for the effective exchange rates)



Sources: IMF, Information Notice System.

Assessment

6. The EBA-lite REER model estimates a REER gap of 44.5 percent in 2022/23. Adjusting the model-based results of the estimated CA gap to account for the temporary factors discussed above, staff's final assessment of the REER overvaluation is 52 percent in 2022/23. The average parallel market premium rose to 78 percent in 2022/23 from 32 percent in 2021/22. With persistently high inflation continuing into 2023/24, overvaluation is estimated to have increased further. The parallel market premium had risen to more than 100 percent by the end of March 2024.

7. Exchange rate flexibility, combined with appropriately tight macroeconomic policies and a shift to a modern monetary policy framework and durably lower inflation, should support a correction of the REER. Market determination of the exchange rate and removal of most current account restrictions will address the overvaluation and FX shortages, supported by a tight and more active monetary policy. The fiscal stance will be constrained by availability of financing and tighter monetary policy. Revenue mobilization is needed to support longer-term development spending while reducing external sector pressures.

C. Capital and Financial Flows

Background

8. The capital and financial accounts are dominated by official flows to the public sector and foreign direct investment (FDI). After peaking in 2014/15, with an issuance of its first and only (10-year) Eurobond of US$1 billion, the surplus has declined consistently as official flows dwindled. Official flows recovered moderately in 2022/23 following as conflict in the North of the country ended. Net FDI inflows fell to 2.1 percent of GDP in 2022/23 down from 2.6 percent the previous year, comparable to the averages for the region and low-income developing countries. Ethiopia maintains certain exchange controls and capital flow management measures.

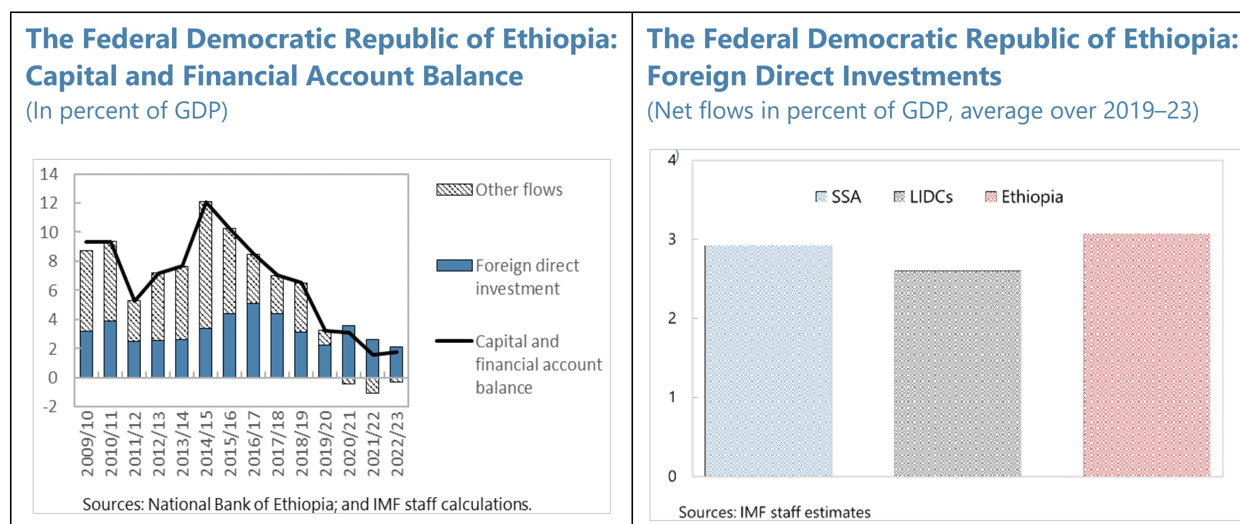
Assessment

9. Over the medium term, the external financing environment is expected to remain challenging. Low capacity to generate export earnings and low international reserves pose a risk to external debt servicing. FX market distortions dampen prospects for FDI due to restrictions on dividend payments and uncertainties surrounding FX availability. A full normalization of project financing and budget support will take time as Ethiopia applied for a debt treatment under the Common Framework in February 2021. A Fund program underpinned by strong reform measures and conclusion of debt treatment discussion could materially change the medium-term outlook by catalyzing FDI, private financial, official bilateral and multilateral flows.

D. FX Reserves

Background

10. Gross international reserves declined to US$1.0 billion (0.5 months of prospective imports coverage) at end-2022/23. Even with a decline in dollar amount of goods imports, lower



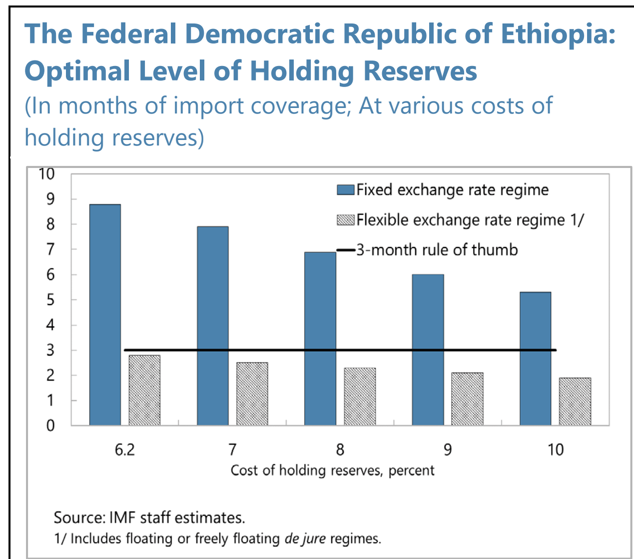
exports and private transfers led to declining FX reserves. Reserves rose to US$2.0 billion at end-December 2023 before declining to US$1.5 billion at end-March 2024.

Assessment

11. International reserves are significantly below the adequacy threshold commonly applied to low-income countries (3 months of prospective import coverage). Reserves have averaged only around 2 months of prospective import coverage over the past decade. The reserve adequacy template for low-income countries indicates that Ethiopia requires approximately 5 to 9 months of prospective import coverage, considering the country's current de facto crawling exchange rate regime and assuming a 6.2 percent cost of holding reserves (the recommended average value for LICs).[2] However, under a flexible exchange rate regime, this range would decrease to 2 to 3 months. Under the Fund-supported program reserves are projected to increase to 3.5 months of import coverage by the end of 2027/28. Higher reserves, complemented by policy adjustments and structural reforms, would provide an important buffer against shocks.

The Federal Democratic Republic of Ethiopia: Optimal Level of Holding Reserves

(In months of import coverage; At various costs of holding reserves)



Source: IMF staff estimates.

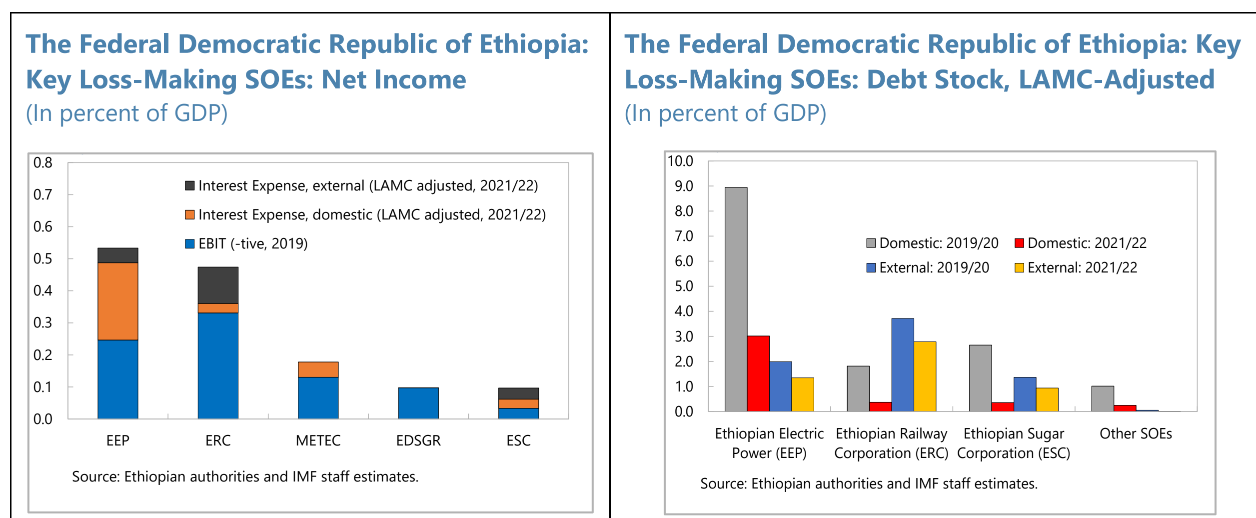
1/ Includes floating or freely floating *de jure* regimes.

[2] Ethiopia's de jure exchange rate regime is managed floating, but the de facto official exchange rate regime is classified as "crawl-like".

Annex II. The SOE-Bank-Sovereign Nexus

1. SOEs pose fiscal and debt risks and are a key macroeconomic vulnerability. Three loss-making, nonfinancial SOEs (Ethiopian Electric Power, EEP, Ethiopian Railway Corporation, ERC, and Ethiopian Sugar Corporation, ESC) accounted for 90 percent of birr-denominated SOE debt at end 2022/23. Transfer of their debts, totaling 9.3 percent of GDP, to LAMC in 2020/21 was not accompanied by improvements in operational viability, while LAMC was underfunded and unable to service the debt. In May 2023, LAMC assumed additional SOE debts to CBE (1 percent of GDP in loans and accumulated interest) of the financially weak and loss-making SOEs (with the bulk from ERC and ESC).

2. Fiscal risks from these SOEs are acute. The FAD SOE Health Check Tool classifies the largest of the LAMC-supported SOEs as overall high risk. Debt, inefficiencies, and fiscal risks are highly concentrated. Restoring the operational viability of EEP and ERC are priorities. In the electricity sector, the 2018 tariff reform helped halve the sector's net losses to about 0.5 percent of GDP while protecting the poorest households. However, tariffs remain below cost recovery and have not been adjusted for three years. In the railways sector, a comprehensive strategy to reduce large recurring losses is yet to be formulated. ERC announced losses of 9.7 billion birr (0.1 percent of GDP) for 2022/23, and the government authorized a capital increase of 221 billion birr. ESC is slated for privatization.



The Federal Democratic Republic of Ethiopia: Key Loss-Making SOEs: Net Income
(In percent of GDP)

Source: Ethiopian authorities and IMF staff estimates.

The Federal Democratic Republic of Ethiopia: Key Loss-Making SOEs: Debt Stock, LAMC-Adjusted
(In percent of GDP)

Source: Ethiopian authorities and IMF staff estimates.

3. CBE has written off claims on LAMC, fully provisioned non-performing loans to EEP, and has been recapitalized. CBE (58 percent of banking system assets) was the sole creditor of LAMC and EEP, which together accounted for over 90 percent of its loan book. Formerly, CBE did not provision or hold capital against these exposures, and government guarantees were not called. Recapitalization of CBE eliminates a significant macro-financial vulnerability, while reform of the SOE's and CBE's governance will avoid a similar practice reemerging, as will strengthened banking supervision and regulation. While the full extent of restructuring of SOE debts to CBE has not yet

been finalized, the effective alleviation of debt pressures on the SOEs also provides time for their operational restructuring.

4. The authorities are taking steps to address SOE vulnerabilities. The new Public Enterprise Law passed in 2023 applies to all SOEs and sets out grounds for public service obligation costing, funding, and accountability, and hence better fiscal risk and public investment management. Improvements in SOE performance have been achieved through subsidy reforms, budgetary controls, and tightened borrowing limits. Notably, fuel subsidy reform has lowered extrabudgetary costs by about 1 percent of GDP over the last three years. In the electricity sector, tariff adjustment plans (supported by the World Bank) are expected to restore operating balance within the program period, after several years during which tariff increases have lagged inflation and costs. In the railway sector, reforms will aim to address sector's fragmented corporate governance and reinforce efficiency through liberalization of key logistics sub-sectors.

Annex III. Risk Assessment Matrix[1]

Source of Risk	Relative Likelihood	Impact if Realized	Policy Response
Domestic Risks			
Further intensification of conflict in Amhara and Oromia regions or escalation of tension between Amhara and Tigray.	**M**	M. Economic disruption, increased humanitarian needs, and increase in prices of staples as Amhara and Oromia encompass the country's main crop producing areas.	Ensure clear communication, facilitate humanitarian aid, and accelerate peace talks. Ethiopian National Dialogue Commission already established.
Worsening of drought in the northern part of the country.	**M/L**	M. Further increase in food insecurity.	Scaling up humanitarian assistance to affected areas in coordination with international relief agencies.
Fallout from dispute with Somalia over status of Somaliland and Ethiopia's quest for sea access.	**L**	M. Regional instability, resurgence of Al-Shabab terrorism.	Resolving differences through peaceful negotiation.
Domestic resistance delays implementation of planned economic reforms.	**L**	M. Economic distortions continue, difficulties accessing imported goods intensify, growth and investment weaken.	Forceful communication of reform benefits complemented by protection of vulnerable groups.
External Risks[1/]			
Intensifying spillovers from regional conflicts. Escalation or spread of regional conflict(s) or terrorism disrupt trade, remittances, tourism, FDI and financial flows, payment systems, and increase refugee flows.	**H**	M. Lower demand for Ethiopia's main exports, trade flow disruptions, and weaker debt sustainability. Financing from a major bilateral partner adversely affected.	Accelerate reforms enhancing export competitiveness. Adopt a market-clearing exchange rate policy. Accelerate the WTO accession process and implementation of trade agreements such as AfCFTA.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. "Short term" and "medium term" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively.

External Risks[1/]			
Source of Risk	**Relative Likelihood**	**Impact if Realized**	**Policy Response**
Commodity price volatility. A succession of supply disruptions and demand fluctuations causes recurrent commodity price volatility, external and fiscal pressures, and social and economic instability.	**H**	M/H. Higher import prices for import commodity, including food, fuel, and fertilizers. Wider trade and fiscal deficits. Negative impact on agriculture due to lower fertilizer imports.	Tighten monetary policy if second-round inflation effects are significant. Increase social spending.
Broader conflicts, inward-oriented policies, and weakened international cooperation result in less efficient configuration of trade and FDI, supply disruptions, protectionism, policy uncertainty, technological and payments systems fragmentation, rising shipping and input costs, financial instability, a fracturing of international monetary systems, and lower growth.	**H**	L/M. Lower demand for exports, weaker trade deficit and debt sustainability. Reduction in remittances from diaspora, FDI, creditor cooperation, and financial support from international community.	Accelerate reforms enhancing export competitiveness. Adopt and maintain a more flexible exchange rate policy.

[1/] Based on the February 7, 2024, update of the Global Risk Assessment Matrix.

Annex IV. Mitigating the Social Impact of Exchange Rate Unification

A spending package of about 1½ percent of GDP in the first year of the Fund-supported program will fund increases in targeted pro-poor programs and temporary subsidies for key imported goods affected by the FX reform. Expansion of the targeted Productive Safety Net Program (PSNP) will ensure the most cost-effective and efficient way of providing support to vulnerable people. Higher support through PSNP is a key medium-term objective under the program. Temporary fuel and top-ups to the fertilizer subsidy will further mitigate impacts on households and poor farmers. Temporary direct subsidies (select food items, medicines) will be considered to cushion the impact and potential delay in the timely expansion of the PSNP, despite the inefficiencies of untargeted schemes.

1. **PSNP reaches around 40 percent of rural and 20 percent of urban households.** The schemes are well targeted but cover only about half of rural administrative areas (woredas), precluding very quick scaling up. A near-term strategy to mitigate the impact of a large FX depreciation will encompass: (i) raising benefits for current coverage of the rural poor to counter erosion from inflation, and (ii) raising benefits and expanding coverage of the urban and rural poor. This will require raising the budgetary allocation for PSNP from about 0.1 to 0.4 percent of GDP per year. In the medium term, coverage in rural areas should be further expanded. These measures to expand PSNP are backed by the World Bank DPO social resilience pillar. Further DPO-supported reforms will modernize safety nets, including to (i) expand e-payments for rural safety nets, (ii) establish a digital ID system and data protection, (iii) enhance and update targeting of the rural poor, and (iv) establish a national social registry.

2. **Essential commodities subject to import price shocks are an important part of household consumption (Annex IV. Table 1).** A budgetary allocation of 0.2 percent of GDP to subsidize imported food and medicine prices will help mitigate direct welfare costs. In terms of direct expenditure, cereals accounts for about a third of food expenditure and a fifth of household consumption. However, about 80 percent of wheat supply is domestic, imports are mostly aid, and wholesale local wheat prices are reportedly close to international prices. Imports of edible oil (0.8 percent of GDP) could have a large direct impact on food expenditure, which presents a case for temporary subsidy. Imports of medical products are about 0.4 percent of GDP (60 percent are public sector imports of pharmaceuticals).

Annex IV. Table 1. The Democratic Republic of Ethiopia: Goods Imports by Public and Private Sector, 2022/23

	Public Sector		Private Sector	
	In millions of U.S. dollars	As percent of GDP	In millions of U.S. dollars	As percent of GDP
Semi-finished Goods	**1,147**	**0.7**	**2,509**	**1.6**
Fertilizers	1,049	0.6	169	0.1
Others	98	0.1	2,340	1.4
Fuel	**3,992**	**2.5**	**38**	**0.0**
Petroleum Products	3,829	2.4	0	0.0
Others	163	0.1	38	0.0
Capital Goods	**1,021**	**0.6**	**2,121**	**1.3**
Transport	27	0.0	204	0.1
Agricultural	14	0.0	52	0.0
Industrial	981	0.6	1,865	1.2
Consumer Goods	**666**	**0.4**	**5,362**	**3.3**
Durables	212	0.1	664	0.4
Non-durables	455	0.3	4,698	2.9
Cereals	40	0.0	1,336	0.8
Other Food	28	0.0	1,223	0.8
Medical & Pharmaceuticals	307	0.2	290	0.2
Others	79	0.0	1,849	1.1
Total Imports	**6,838**	**4.2**	**10,293**	**6.4**

Source: National Bank of Ethiopia and Fund staff calculation.

3. Indirect effects on households would manifest primarily through public sector imports of petroleum products. Direct fuel subsidies to private households are small due to low motor vehicle ownership and low volumes of kerosene consumed but are inefficient (only 15 percent of benefits accrue to households in the two poorest income quintiles). Indirect effects of increased transportation costs on welfare would be significantly larger considering the reliance on road transportation for distribution of goods across the country, and effects are nearly uniformly distributed across households. Ongoing fuel subsidy reforms have led to the tripling of the pump prices over the last two years, to levels above cost parity at the current official exchange rate. Exchange rate unification would open a price gap with an annual cost of 1 to 1¼ percent of GDP. Partially addressing the impact, at a cost of 0.5 percent of GDP over a 12-month period, will be addressed with time-bound predetermined fuel price adjustment. To cap public subsidy cost at 0.1 percent of GDP and mitigate leakages, the authorities will rely on the existing targeted rebate mechanism, expand digital payment platforms, and limit targeted subsidy eligibility to city and regional public bus transportation.

4. Fulfilling all suppressed fertilizer demand at the current subsidized price level would be prohibitively costly. Import volumes have halved over the last two years, curtailed by FX shortages (FX supply for fertilizer was capped at around US$1 billion) and the surge in international prices. Under-fertilization is among the most important factors behind relatively low production yields in wheat and other cereals. Considering the current budgetary subsidy of 0.3 percent of GDP and the price gap of close to 50 percent, a full offset of the exchange rate depreciation would increase the subsidy cost by 0.6 percent of GDP. Doubling the import volume to its 2019/20 level would add an additional 0.9 percent of GDP to the cost and US$1 billion to the gross external financing requirement per year. In this light, partial price pass-through maintaining current import values is essential to contain direct fiscal costs, with the total subsidy capped at 0.5 percent of GDP.

Annex V. Quasi-Fiscal Activity and Financial Repression

The main quasi-fiscal operations result in about 3 percent of GDP in quasi-fiscal deficit, formerly funded mainly through exchange rate distortions and financial repression. Considering the impact of reform measures in the Fund-supported program, the consolidated public sector deficit including key quasi-fiscal operations will contract by about 3 percent of GDP over two years, exceeding the fiscal effort measured by the overall general government balance. The additional effort contributes to restoring internal and external stability. Key measures are: (i) domestic revenue mobilization with continued spending restraint; (ii) SOE reforms and subsidy rationalization; (iii) CBE rehabilitation; and (iv) gradual phasing out of financially repressive measures such as mandatory bond purchases.

A. Quasi-Fiscal Activity, Fiscal Transparency, and Macroeconomic Effects

1. Quasi-fiscal activities (QFAs) are any operation carried out by public corporations to further public policy objective that worsens their financial position relative to a strictly commercial profit-maximizing level.[1] QFAs can take a variety of forms, including selling goods and services (e.g., energy, water) at less than their commercial cost or paying more than commercial prices to selected suppliers. In principle, such activities could be replaced by specific on-budget taxes, subsidies, or other direct expenditures. In contrast to explicit budgetary operations, QFAs typically entail limited disclosure and public scrutiny. Piecing together accurate, conceptually appropriate, and comprehensive data on QFAs, and assessing the consolidated fiscal impact requires analyzing public sector policies inside and outside the budget.

2. The most macroeconomically important QFAs used in Ethiopia can be grouped into the following three categories:

i. **Operations related to commercial activity and public sector obligations:**
   - **Implicit fiscal subsidies to consumers:** SOEs charging less than commercial (cost recovery) prices for the goods and services, such as fertilizers, electricity, and fuel, to some or all consumers.
   - **Other activities:** noncompetitive (above competitive market clearing) pricing by SOEs (telecom), including for budget revenue purposes.

ii. **Operations related to the financial sector[2]:**
   - **Subsidized lending:** state-owned banks (CBE, DBE) providing loans to SOEs or private borrowers at below market interest rates. This also includes lending that is poorly secured or made to borrowers who are not creditworthy.
   - **Interest rate management:** maintaining negative or below market equilibrium real interest rates on captive domestic savers to ensure low-cost credit to SOEs, selected economic sectors or industries, or to lower government debt costs.

[1] See IMF Fiscal Transparency Handbook (2018) for methodological background.

[2] See Reinhart and Sbrancia (2011) for further discussion of financial repression mechanisms.

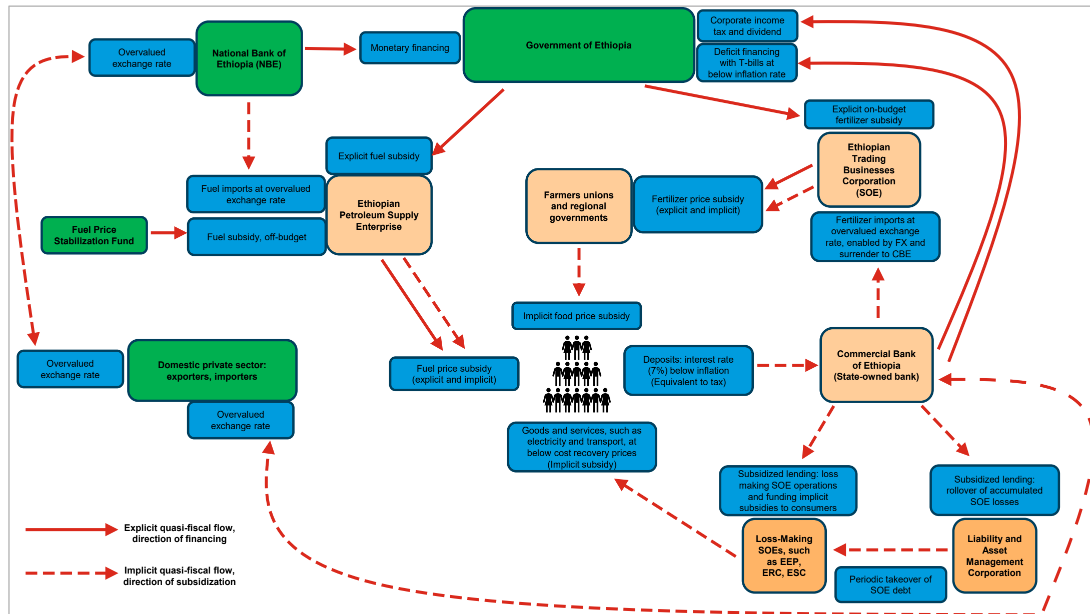
- **Other activities:** direct central bank lending to the government; under-remunerated central bank reserve requirements. Ceilings on commercial bank credit entail a quasi-fiscal impact via crowding out.

iii. Operations related to the exchange rate and trade systems:

- **Multiple exchange rates:** Key examples are: (i) SOEs (or the end users of their products) benefitting from preferential access to FX at the official exchange, e.g., the implicit fiscal subsidy on fuel imports via the exchange rate; (ii) surrender or repatriation of export proceeds at an overvalued exchange rates (an implicit tax on exporters).
- **Other activities:** such as (i) explicit exchange rate guarantees or assumption of FX risk provided by the central bank or state-owned financial institutions, (ii) nontariff barriers, e.g., bans or restrictions on certain exports (grains such as maize and barley) and imports, (iii) advance import deposit requirements.

B. Mapping Quasi-Fiscal Activity in Ethiopia

3. At the institutional level, SOEs, state-owned banks, and extrabudgetary units facilitate quasi-fiscal activity. The main macroeconomically relevant quasi-fiscal activities, financial flows, and their relation to explicit budgetary operations can be charted as below.[3]



4. At the instrument level, financial repression and exchange rate distortions have been the main quasi-fiscal funding tools. Both instruments create distortions in key relative prices with negative effects, for example by undermining incentives for investing in export production, impeding the development of credit and the financial sector, and dissuading private saving.

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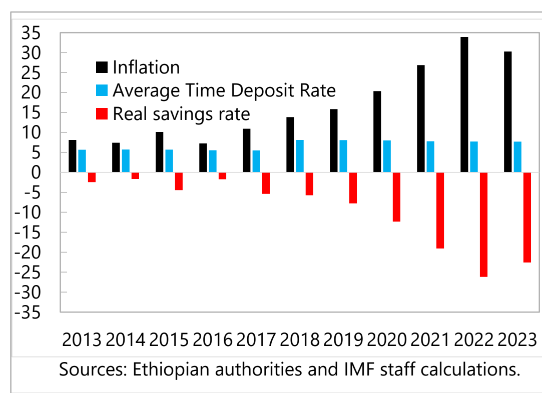
[3] For an expanded instrument-level mapping of financial repression in Ethiopia, see Chauffour and Gobezie, (2019).

- **Financial repression has functioned through negative real deposit rates and credit allocation to the public sector at low interest rates.** Direct control over the state-dominated financial system allowed the public sector to capture savings cheaply and with limited legislative or regulatory interference. CBE's systemic dominance has been a key factor in setting interest rates across the financial sector, with private banks constrained by operational restrictions. Low interest rate savings mobilized by CBE were channeled to public investment and allowed evergreening of loss-making operations of SOEs. Government budget financing also benefitted through low interest rates on Treasury bills in the context of high inflation. T-bills have been placed mainly with state-owned investors, such as CBE and pension funds. In addition, there has been substantial recourse to monetary financing, that fueled inflationary pressures.

The Federal Democratic Republic of Ethiopia: Source of Financial Repression
(In percent)



Sources: Ethiopian authorities and IMF staff calculations.

- **Maintenance of an overvalued official exchange rate allowed resources to be channeled to quasi-fiscal activities.** The overvalued official exchange rate resulted in severe FX shortages and led to rationing of FX in favor of public policy priorities. Every FX transaction at the official rate simultaneously imposes an implicit tax on the exporter, who is forced to surrender FX at an overvalued exchange rate, and an implicit subsidy to the importer receiving FX at that rate, and the importer's ultimate beneficiaries (which could be some part of the public, for example in the form of cheaper fuel). From the fiscal standpoint, an overvalued exchange rate is a proxy for tax and expenditure policy, substituting for efficient income tax collection and agricultural taxation on the tax side, and creating a large implicit subsidy for above all fertilizers and fuel on the spending side (in addition to explicit subsidy schemes for those commodities). Overvalued exchange rates also lower the valuation base in Birr terms for import-related taxes, reducing the import tax take and dampening imported inflation.

C. Quantifying Impacts of QFAs

5. **Quantifying the macroeconomic impact of quasi-fiscal activity requires assessment of shadow or market equilibrium prices, notably foreign exchange rate and interest rates, which can be inherently imprecise and subject to policy framework and macroeconomic uncertainty.** Staff's estimate factors in the following key assumptions:

- Real exchange rate overvaluation to quantify implicit fuel and fertilizer subsidies. These are reported as adjusted SOE deficits (EPSE and EABC) in the pre-program period, and then on-budget in line with program's subsidy reform path.

- Real exchange rate overvaluation to quantify the implicit tax on exporters via surrender at the official exchange rate and foregone tax on importers through impact on the import tax base.
- Adjustment to the effective interest rate paid by the public sector on domestic borrowing, equivalent to an implicit positive real interest rate averaging about 3 percent over the last decade, and an interest rate path consistent with gradual unwinding of financial repression in the program period. A similar adjustment to effective interest rate assumptions is applied to CBE's interest-bearing liabilities.

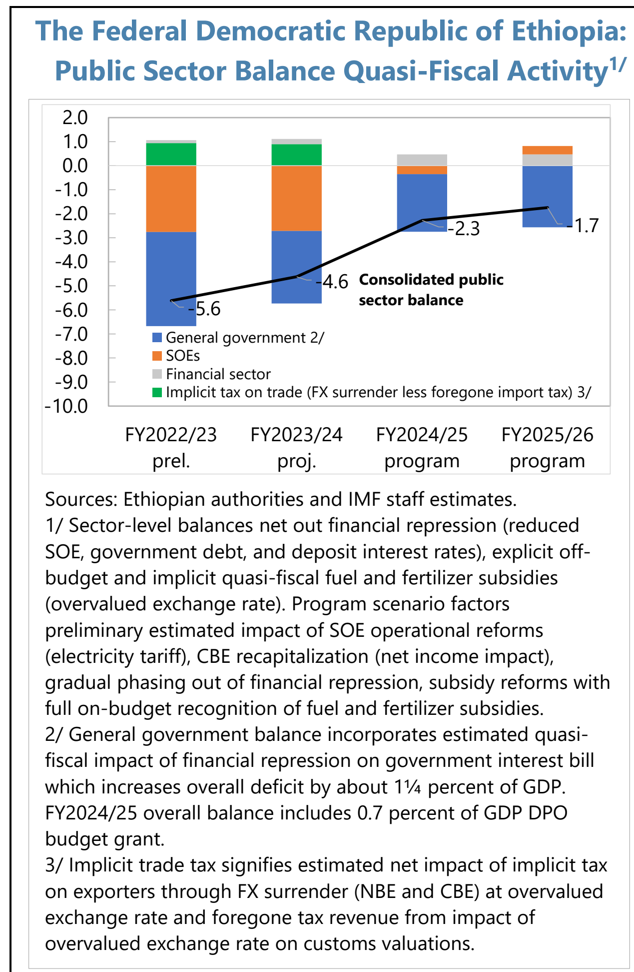
6. Staff assesses the main quasi-fiscal operations correspond to a quasi-fiscal deficit of about 3 percent of GDP, of which:

(i) 2¾ percentage points due to actual and quasi-fiscal deficits from SOE operations;

(ii) 1¼ percentage points in additional spending financed by lower general government debt interest payments due to low effective rates on domestic debt from financial repression; and,

(iii) A net 1 percent of GDP of deficit reduction from implicit tax revenues on trade, specifically the implicit tax on exporters via FX surrender at the official exchange rate net of foregone tax revenue on importers through impact on the official exchange rate on custom valuation.

The Federal Democratic Republic of Ethiopia: Public Sector Balance Quasi-Fiscal Activity[1/]



Sources: Ethiopian authorities and IMF staff estimates.
1/ Sector-level balances net out financial repression (reduced SOE, government debt, and deposit interest rates), explicit off-budget and implicit quasi-fiscal fuel and fertilizer subsidies (overvalued exchange rate). Program scenario factors preliminary estimated impact of SOE operational reforms (electricity tariff), CBE recapitalization (net income impact), gradual phasing out of financial repression, subsidy reforms with full on-budget recognition of fuel and fertilizer subsidies.
2/ General government balance incorporates estimated quasi-fiscal impact of financial repression on government interest bill which increases overall deficit by about 1¼ percent of GDP. FY2024/25 overall balance includes 0.7 percent of GDP DPO budget grant.
3/ Implicit trade tax signifies estimated net impact of implicit tax on exporters through FX surrender (NBE and CBE) at overvalued exchange rate and foregone tax revenue from impact of overvalued exchange rate on customs valuations.

7. Program-supported reforms reducing financial repression and exchange rate distortions underpin consolidation of quasi-fiscal activity. Reforms underpin an overall (fiscal plus quasi-fiscal) adjustment of about 3 percent of GDP over the next two years. Reforms include (i) budget consolidation through domestic revenue mobilization and spending restraint; (ii) SOE reforms and subsidy rationalization; (iii) rehabilitation of CBE, including writing off claims on LAMC and full provisioning of non-performing loans to EEP; and (iv) the gradual phasing out of financially repressive measures such as mandatory bond purchases. The CF debt treatment and write-off of EEP's domestic debt to CBE will relieve SOE liquidity and solvency pressures for key SOEs (EEP, ERC, ESC). In addition, elimination of quasi-fiscal activity and on-budget recognition of previously quasi-fiscal public sector operations through explicit subsidies will increase fiscal transparency.

Appendix I. Letter of Intent

Addis Ababa, July 10, 2024

Madame Kristalina Georgieva
Managing Director
International Monetary Fund
Washington, DC 20431
USA

Dear Madame Managing Director:

Following two decades of rapid development, Ethiopia's economy has since 2020 been hard hit by a series of shocks. These included the global COVID-19 pandemic, international commodity price increases, severe drought, and domestic conflict. While economic activity has remained resilient, this unprecedented combination of major shocks led to moderation in economic growth. We are now facing significant economic pressures, including high inflationary pressure, foreign exchange shortages, and unsustainable debts.

In response to these challenges, we are implementing a comprehensive program to address macroeconomic imbalances and promote private sector-led growth. The objectives of our economic program are to (i) address foreign exchange shortages and long-term balance of payments vulnerabilities; (ii) reduce inflation through prudent monetary policies and sound public finances; (iii) address debt vulnerabilities and strengthen domestic revenue to enable government investment and other priority spending; (iv) strengthen the financial sector, address vulnerabilities in SOEs, and lift financial repression progressively; and (v) promote a robust, inclusive, and sustainable economy.

This economic program supports our recently released HGER2.0, which updates the original HGER and aims to deliver a vibrant private sector that can accelerate growth and create decent jobs. HGER 2.0 rests on four key pillars: (i) ensuring macro-economic stability; (ii) creating a conducive investment and trade climate; (iii) increasing productivity across key sectors; and (iv) building a capable and efficient civil service.

We have already taken important steps to safeguard macroeconomic stability and lay a strong foundation for continued economic development. More specifically, we have contained and more recently substantially reduced the fiscal deficit, curtailed non-concessional external borrowing, scaled back borrowing by state-owned enterprises (SOEs) while strengthening their management, tightened monetary policy, and successfully engaged creditors leading to a temporary standstill on servicing of official external debt. Key sectors, including telecom, logistics, and retail and wholesale trade were opened to foreign investment, while other sectors are currently being opened up in areas such as banking and residential housing. We have also made progress in strengthening the institutional and regulatory framework, with new central bank, banking, investment, trade, procurement, and public enterprise laws already enacted or close to finalization. A securities exchange is about to be launched.

We request the Fund's financial support for our economic program through a four-year arrangement under the Extended Credit Facility (ECF) in the amount of SDR 2,555.95 million and temporary approval of an exchange transaction commission that gives rise to an exchange restriction and a multiple currency practice. Along with support from development partners and financing provided through the comprehensive debt restructuring that has been launched within the G-20 Common Framework, the proposed financing arrangement will cover our fiscal and external financing gaps as we embark on a multiyear adjustment effort. We intend to use part of the ECF funds for direct budget support. In view of this, a memorandum of understanding between the government and the NBE on their respective responsibilities for servicing financial obligations to the IMF has been signed.

The policies and actions underpinning the proposed ECF arrangement are set out in the attached Memorandum of Economic and Financial Policies (MEFP). The implementation of our program will be monitored through quantitative performance criteria, indicative targets, and structural benchmarks described in the MEFP and also in the attached Technical Memorandum of Understanding (TMU). We will provide the IMF with all the data and information required to monitor implementation of the agreed measures and the execution of the program, as detailed in the TMU. We commit to undertaking an Article VIII assessment by the Fund prior to the first review, and will provide all necessary information for the Fund to complete an update of the safeguards assessment of the National Bank of Ethiopia before the first review.

We are confident that the policies and measures outlined in the MEFP will enable us to achieve our program objectives. We will promptly take any additional measures that may become appropriate for that purpose, in consultation with the IMF, and in accordance with applicable IMF policies. We will refrain from any policy that would not be consistent with the program's objectives and commitments herein. We are committed to working closely with IMF staff to ensure that the program is successful, and we will provide the IMF with the information necessary for monitoring our progress.

In line with our commitment to transparency, we consent to the publication of this letter and its attachments, and the related staff report.

Very truly yours,

/s/

H. E. Mr. Ahmed Shide
Minister of Finance
The Federal Democratic Republic of Ethiopia

/s/

H. E. Mr. Mamo E. Mihretu
Governor, National Bank of Ethiopia
The Federal Democratic Republic of Ethiopia

Attachments:

I. Memorandum of Economic and Financial Policies

II. Technical Memorandum of Understanding

Attachment I. Memorandum of Economic and Financial Policies

Addis Ababa, July 10, 2024

A. Context

1. After two decades of rapid economic and social development, Ethiopia's economy, while facing challenges, is resilient. Per capita income rose 650 percent from 2000–20, supporting gains in human development, health, and education indicators. The proportion of people living below the poverty line declined from 44 to 24 percent during 2000-2016. Although a key driver of growth was public investment in large infrastructure projects, this contributed to macroeconomic imbalances that threatened to undermine progress. In 2019, the government embarked on the Homegrown Economic Reform Agenda (HGER) to address imbalances and encourage private sector-led development. A series of economic shocks, including the COVID 19 pandemic, drought, domestic conflict, and international commodity price rises, delayed reforms and led to a moderation in growth, worsening economic imbalances, significant internal displacement, and food insecurity. Financing reconstruction and recovery from conflict and managing the long-term effects of climate change add to the challenges that must be addressed.

2. To sustain progress, we are reinvigorating our reform agenda, addressing macroeconomic pressures, and shifting to private sector-led growth. The recently released HGER2.0 (2023/24-25/26) renews the government's commitment to maximizing the potential and building the resilience of our economy. Immediate challenges include tackling high inflation, persistent external imbalances, including foreign exchange (FX) shortages and low international reserves, and external debt risks. Over the medium term, reforms will foster sustainable, private sector-led growth. HGER2.0 is built on four pillars: (i) macroeconomic reforms, to establish a modern and sound macroeconomic policy framework that supports stability, resilience, and sustainability; (ii) investment and trade sector reforms, to boost competitiveness through a favorable environment that promotes and enhances innovation and entrepreneurship; (iii) productive sector reforms, to expand capacity and raise productivity growth by increasing investment; and (iv) public sector reforms, to enhance the government's capacity to ensure the efficient delivery of high quality services.

3. At the same time, certain core elements of the economic reform plans have successfully been implemented despite very challenging circumstances. The deterioration in fiscal balances has been limited, difficult subsidy reforms have been implemented helping minimize fiscal risks, and a tight management of new state-owned enterprise (SOE) borrowing (including avoidance of non-concessional debt) has worked to reduce and control future liabilities. Treasury Bill auctions were successfully launched to provide a market-based system for domestic borrowing, replacing the previous mandatory NBE Bills, and despite the much higher financing cost for Government. Work on launching capital markets proceeded with the approval of a new Proclamation, establishment of the Capital Markets Authority, and well-advanced preparations for the inauguration of the Ethiopian Stock Exchange in 2024. A new holding company, Ethiopian Investment Holdings, was established to achieve improved performance in public enterprises

through use of modern management practices, corporate governance standards, and partnerships with foreign investors. Major regulatory changes in telecom and logistics sectors (both previously dominated by a government monopoly) were opened to competition for the first time to help relieve critical bottlenecks in this area. The decision to open the banking sector to foreign participation was another decisive reform measure taken to help address long-standing weaknesses in the scope, depth, and accessibility of modern financial services.

4. In summary, the overall direction and reform effort in macroeconomic policies and performance during the HGER1 period has been strong despite a series of shocks and delays in some reform components. Reflecting a number of focused policy initiatives, a positive growth rate has been maintained, debt ratios have been reduced, SOE reform and privatization measures have been maintained, and the financial sector oversight prudently managed. Fundamental reforms in key enabling sectors—telecom, logistics, banking, capital markets—have also been launched to lay the groundwork for private sector led growth over the coming years.

B. Economic Challenges and Opportunities

5. Real GDP growth has remained resilient but has moderated in recent years. Growth rose from 6.4 in 2021/22 to 7.2 percent in 2022/23, above sub-Saharan African averages, but down from average growth of 9 percent prior to 2019. The Cessation of Hostilities Agreement in November 2022, strong performance in transport services and hotels following the pandemic, and strong agricultural production due to favorable rains and initiatives to increase irrigated crop production have supported the recovery. Growth in industry has suffered from supply bottlenecks (particularly in construction) and foreign exchange shortages.

6. Inflation has fallen but remains high. Inflation peaked at 37 percent in May 2022, but has since declined to 23 percent as of May 2024. Although the National Bank of Ethiopia (NBE) took decisive measures to reduce inflation in FY2023/24, including limiting monetary financing of fiscal deficits and growth in credit to the private sector, persistently high food inflation has offset declines in non-food prices. With the slow pace of crawl of the official exchange rate, the real exchange rate has appreciated rapidly.

7. Balance of payments (BOP) pressures are acute. The domestic conflict, application for debt treatment under the G20 Common Framework (CF), and external shocks such as the war in Ukraine, led to a significant decline in external financing. Import price rises for food, fertilizer, and fuel, have weakened the trade balance while gold and coffee exports and remittance flows declined. International reserves fell below one month of import coverage at end-2021/22 and further declined in 2022/23. Import restrictions were imposed on 38 non-essential goods and the surrender requirement to NBE on FX earnings from exports was raised to 70 percent—though we subsequently eased restrictions on imports of construction-related items and lowered the surrender requirement to 50 percent.

8. Temporary financial support from the Official Creditor Committee (OCC) has relieved short-term FX liquidity pressures. The Official Creditor Committee (OCC) for Ethiopia under the CF

agreed in November 2023 to suspend debt service due in 2023 and 2024, retroactive to January 1, 2023. A US$33 million Eurobond coupon payment was not made on December 11, 2023, reflecting our concern to treat our private and official creditors comparably. We have opened debt restructuring negotiations with representatives of Eurobond holders.

9. Government spending has been cut to reduce deficit financing needs, with declining revenues and little external support. The general government deficit fell to 2.6 percent of GDP in 2022/23, down from 4.2 percent of GDP in 2021/22, as peace brought a decline in defense spending and capital spending was constrained. Grants fell to 0.3 percent of GDP in 2022/23, down from an average of 1 percent of GDP during the pre-conflict years. General government tax revenues continued their long-term decline, falling to 6.8 percent of GDP in 2022/23, a critically low level that jeopardizes public service delivery, poverty reduction, and capacity to finance large public investment and post-conflict reconstruction needs. Despite revenue mobilization efforts (a new Social Welfare Duty tax imposed on imports and rationalization of tax expenditure on vehicle import duties), federal tax revenues fell to 4.3 percent of GDP in 2022/23 from 4.8 percent the year before.

10. Reforms of SOEs are underway. Infrastructure investment and quasi-fiscal activities of some large SOEs have been curtailed, and longer-term reform programs to restore operational viability are underway. A key macro-financial vulnerability stems from past lending to these SOEs by the systemic state-owned Commercial Bank of Ethiopia (CBE). Operating losses and failure to service debt resulted in CBE evergreening these loans, as sovereign guarantees were not made effective. The equivalent of about 6.2 percent of GDP in such legacy loans, including overdue interest, had been taken over by the federally owned Liability and Asset Management Corporation (LAMC) by 2022/23. After LAMC made repayments on these debts with resources from the sale of telecom and mobile money licenses, SOE reform and privatization plans were affected by the domestic conflict, and no additional repayments were made, incurring substantial new arrears to CBE.

11. Monetary policy has been tightened. Against the backdrop of external financing constraints and limited scope for increasing domestic market financing, NBE advances became the main source of deficit financing in 2022/23 (2.4 percent of GDP), leading to an expansion in reserve money (32 percent) and inflationary pressures. In 2023/24, to reduce inflation, monetary financing was reduced to 0.8 percent of GDP and growth in commercial bank credit to the private sector capped at 14 percent. The rate on monthly borrowing from the central bank was raised to 18 percent from 16 percent. Market-determined term deposit rates have also increased, from around 7.5 percent in September 2023 to around 14 percent in March 2024. Nonetheless, interest rates remain well below inflation.

12. Debt levels have fallen sharply. The government has not contracted new external non-concessional loans since 2018, while SOEs have not started new externally financed investments, continuing only a few ongoing projects. The stock of external debt declined from 29.0 percent of GDP in 2020/21 to 17.4 percent of GDP in 2022/23. With domestic debt falling too, total public and publicly guaranteed debt declined from 56.1 percent of GDP in 2020/21 to 39.4 percent in 2022/23.

C. Objectives of the Program

13. Our economic reform agenda will provide a foundation for strong, inclusive, and private sector-led growth. We envision a return to high and stable growth and single digit inflation within the program period. Correcting exchange rate distortions, unlocking external financing, controlling inflation, boosting tax revenues, optimizing public investment, ensuring debt sustainability, strengthening banking sector resilience, and improving the business environment will anchor macroeconomic stability and stimulate economic growth.

14. Our economic program supported by the IMF and outlined in this memorandum is built on the HGER. Key objectives under the program are to (i) address foreign exchange (FX) shortages and long-term balance of payments (BOP) vulnerabilities stemming from exchange rate distortions among other factors; (ii) reduce inflation through modernizing the monetary policy framework and sound public finances; (iii) address debt vulnerabilities and strengthen domestic revenue to enable government investment and other priority spending; (iv) strengthen the financial sector, address vulnerabilities in SOEs, and lift financial repression progressively; and (v) promote a robust, inclusive, and sustainable economy, through improving governance, financial inclusion, public service delivery and bolstering climate resilience and food security. Strengthening institutions and macroeconomic policy frameworks is critical to achieve these goals, which together will create the right conditions for private investors to unlock the economic potential of our country.

D. Foreign Exchange Policy

15. Eliminating distortive current account controls and adopting a market-determined exchange rate are critical to relieving FX shortages, reducing BOP vulnerabilities, and removing constraints to private sector investment and growth. Sustaining an official exchange rate below the market-clearing level undermines investment and growth, incentivizes hoarding of foreign exchange and rent seeking, and speculation in assets that could offer an exchange rate hedge. It has acted as a significant implicit cost on exports that earn the official rate, discouraging their production, and FX and import shortages. Initiatives aimed at boosting external competitiveness have had limited impact with an overvalued exchange rate.

16. Necessary preparations for a move to a market-based exchange rate regime were completed. The NBE undertook a thorough review of current FX regulations in consultation with Fund staff and finalized, in July 2024, a new consolidated FX directive consistent with a market determined exchange rate regime. The NBE is also implementing a system to receive real-time data on foreign exchange transactions from market participants (commercial banks and foreign exchange bureaus) to compute the market-determined exchange rate on a daily basis. Operational guidelines for foreign exchange operations of the NBE and the foreign exchange market, along with an updated Code of Conduct for market participants were implemented in July 2024. An assessment of all banks' net open positions (NOP) was finalized in June 2024. Finally, the tightening of macroeconomic policies will underpin FX market stability and support the transition to the new exchange rate regime by reducing inflation and maintaining a sustainable budget deficit.

17. We have taken decisive measures to ensure a market clearing exchange rate, including upfront steps to liberalize current account transactions (prior action). These measures will close the gap between the parallel and official market exchange rates:

- **We have published a directive announcing that authorized dealers can buy and sell FX from their clients and among themselves at freely negotiated exchange rates**. We will compute the benchmark exchange rate as the weighted average rate of transactions between authorized dealers and their clients as well as transactions between authorized dealers themselves, as reported daily to the NBE. This benchmark will be published at the close of market every day and will be the official exchange rate for accounting purposes.
- **We have removed distortive current account controls**, specifically: (i) the rationing of FX allocations for imports and the three-tier priority list of imports; (ii) the NBE import reference price system linked to minimum import prices by customs office; (iii) the security deposit requirement of 50 percent when queuing for FX for import payments. We will review the exchange commission fees charged by NBE on purchase of foreign currency for import payments by the second program review to ensure the practice does not give rise to an exchange restriction or multiple currency practice. The requirement for importers to open letters of credit (LCs) with banks has been completely removed, allowing the removal of restrictions placed on franco valuta imports. In consultation with IMF staff, current account restrictions on the outstanding stock of dividends (which have been applied for but are waiting approval at the time of the transition to a market clearing exchange rate) and suppliers' credits have been retained temporarily given the potential to exert sudden pressure on FX demand. No current account restriction will be applied to the new dividend payments and the repayment of supplier's credits that are agreed upon following the transition to a market clearing exchange rate. The capital account has not been liberalized; we will consider reform in this area once the foreign exchange market is well established and with due consideration to financial stability in our growing domestic banking and capital market. Finally, we commit to an Article VIII assessment by the Fund prior to the first review.

18. We have fully switched surrender requirements for foreign exchange earners from the NBE to the commercial banks. This is to support efficient foreign exchange pricing by ensuring an adequate supply of foreign exchange to the market. The surrender rate to the commercial banks is at 50 percent, while foreign exchange earners retain the rest. As a transitional measure, exporters have one month to use non-surrendered FX before it too must be surrendered. This measure will be reconsidered at the first program review with a view to its removal. The exchange rate applicable to the surrender requirement is the market exchange rate. We will completely phase out surrender requirements by the end of the program, at a pace determined by the development of FX market liquidity.

19. To ensure that banks manage FX risks well in the new regime, we will increase monitoring and enforce daily NOP limits, adjusting for banks' legacy positions before the move to a market-clearing exchange rate. We will order all banks not in compliance with the regulatory threshold prior to the change of FX regime to provide plans to ensure full compliance by

end-June 2025 (end-September 2024, structural benchmark). If needed, an additional extension of up to one year will be provided to CBE to unwind its excess NOP attributable to public policy decisions. This approach provides time for banks to close legacy NOP, while daily monitoring and enforcement will ensure that positions do not widen further. We will further strengthen the measurement of NOPs to better capture bank's FX risk profiles, revise the NOP prudential regulation, and redesign the call report to collect more granular data on the subcomponents of on- and off-balance sheet FX positions and facilitate reconciliation with the balance sheet data.

20. Intervention in the foreign exchange market will be limited to stemming disorderly market conditions. The NBE has approved an FX intervention strategy (including governance process) that allows, but does not oblige, the NBE to buy or sell foreign currency in volatile market conditions. Any FX intervention will be conducted via public auction open to all banks. As a transitional measure to facilitate clearance of pre-existing obligations for fuel imports until the Ethiopia Petroleum Supply Enterprise has had time to build up adequate FX by regular purchases at the market rate, NBE may use a maximum of US$670 million to settle LCs for fuel imports that fall due in July and August 2024. Such payments, to be made at the prevailing market exchange rate, would not be subject to the FX intervention framework. In addition, NBE may conduct a limited number of low value FX sale auctions during the two-month period immediately after the change of FX regime to support price-discovery, consistent with the framework. These policies support the objective of restoring foreign exchange reserves to adequate levels to reduce external vulnerabilities, by the end of the program. We have developed a FX communication strategy, drawing on advice from the Fund and other central banks.

E. Monetary Policy

21. We are modernizing the monetary policy framework. The NBE's strategic plan for 2023-26 prioritizes maintaining low and stable inflation and transitioning to an interest rate-based monetary policy regime using open market operations. NBE has prepared a governance framework for monetary policy that will be implemented alongside enactment of the NBE establishment proclamation. A monetary policy committee (MPC) was established in early July 2024 to recommend the policy stance to the Board of the NBE and approve all instruments and guidelines relating to the implementation of monetary policy; the MPC will play an advisory role until it assumes its formal role as set out in the amended NBE establishment proclamation. In the initial period, and until a regular schedule has been established, the MPC will meet as frequently as needed at the behest of the NBE Governor. To prepare the transition to the interest rate-based monetary policy framework, NBE has also: (i) published operational guidelines, including for implementing open-market operations and the collateral framework; (ii) enhanced coordination with the Ministry of Finance (MoF), supplementing weekly with daily liquidity forecasts; and (iii) developed a comprehensive and transparent communication strategy for all stakeholders.

22. NBE established an interest rate-based monetary policy, beginning open market operations in July 2024. On July 9, 2024, we announced a target policy rate of 15 percent, the mid-point between the standing lending and deposit facility rates, set at ± 3 percent around the policy

rate, with the interbank lending rate as an operational target (prior action). To achieve this policy stance, the NBE introduced regular full allotment Open Market Operations (OMOs) at the policy rate (prior action) to align banking sector liquidity with the monetary policy stance and to promote strong transmission of the monetary policy rate to financial conditions. Our monetary policy measures will be supported by the deployment of a central securities depository by end-December 2024. We will review the reserve requirement framework to ensure more efficient liquidity management from the banking sector, through consolidation of reserve and payment and settlement accounts, and reviewing the calculation and operation of maintenance periods. Finally, we also plan to strengthen the emergency liquidity assistance framework (SB, end-September 2024).

23. We will continue to tighten monetary policy as needed to anchor exchange rate and inflation expectations with the objective of ensuring price stability. Further increases to interest rates will be implemented with the objective of achieving a positive real policy rate (based on six-month ahead projected inflation) in the first quarter of 2025. In accordance with the new monetary policy framework, we will rely first and foremost on interest rates to signal the policy stance. We will maintain a close dialogue with the IMF on monetary policy setting, consulting as needed if inflation deviates from the baseline. We stand ready to take additional monetary policy measures to manage inflation expectations as needed, including raising reserve requirements depending on liquidity conditions and implementing credit caps.

24. We have begun to address distortions in the T-bill market to reduce financial repression and contain inflationary pressures. NBE will continue conducting all auctions in accordance with the T-bill market directive (NBE/TRB/001/2011) and establish new internal auction procedures from July 2024 to promote better market functioning and price discovery in the T-bill market. We will allow T-bill rates to move freely to the market-clearing rate set in the auctions. Reflecting that the monetary policy rate is now the principal reference for all interest rates in the economy, rates are expected to rise. In order to apply reserve requirements consistently across the banking system we will remove the eligibility of T-bills toward meeting the reserve requirement for CBE. We will do so by at least 50 percent in December 2024 (more if the bank's liquidity position allows), and fully eliminate the eligibility of T-bills to meeting reserve requirements by end-2025.

25. We have eliminated monetary financing of fiscal deficits, ending a key driver of inflation. All direct advances are now terminated (quantitative performance criterion, QPC). To ensure the federal government can manage its cash position as liquidity forecasting improves and the Treasury bill and bond market develops, a government short-term credit facility will be created in the amended NBE proclamation currently in preparation that caps the amount, specifies the reference interest rate, and limits the maturity of any credit provision to the government from NBE in line with good international practice. Tighter fiscal policy and limits on SOE borrowing (IT) will also support tighter monetary conditions, with a significant impact on overall credit demand given the large share of government and public enterprises in total credit.

26. We are strengthening NBE governance and transparency. With technical assistance from the IMF, we are preparing comprehensive amendments to the NBE Proclamation, with respect to NBE's mandate, decision-making structure (internal checks and balances and collegial decision-

making), accountability, external audit, transparency, and autonomy, and will submit draft legal amendments to Parliament no later than end-December 2024 (structural benchmark) with a view to parliamentary approval by end-March 2025. To strengthen external audit of NBE (prior action): (i) the Federal Auditor General has authorized NBE to engage a new auditor; (ii) NBE will adopt a selection and rotation policy for an external auditor; and (iii) NBE will float a competitive bid for the audit starting with 2022/23 financial statements by a suitably qualified firm that includes international experts experienced in auditing central banks. NBE will publish financial statements for 2021/22 and 2022/23 (structural benchmark, end-December 2024). Amendments to the NBE proclamation will ensure there is a legal basis for NBE to be audited by a qualified audit firm with the requisite expertise to conduct IFRS-based audits and experience in auditing central banks.

27. An assessment of NBE's capital will be undertaken. To ensure that NBE has adequate capital to attain its policy objectives and operate independently, we will seek an external assessment on the level of capital needed for NBE to effectively fulfill its mandate. This assessment could inform the amount and instrument used for recapitalization if needed with the NBE proclamation providing a legal basis.

F. Fiscal Policy

28. Our fiscal policy will create space for critical public investment in human capital—health, education, and social protection—and basic infrastructure to support inclusive growth. A revenue-led strategy will restore long-term stability to the public finances, while ensuring a significant contribution to restoring debt sustainability.

29. The immediate objective of our fiscal policy has been to reduce financing pressures and strengthen macroeconomic stability. With little external financing, we have delivered a substantial reduction of 0.7 percent of GDP in the 2023/24 federal government primary deficit, a significant effort in the post-conflict context. We reduced reliance on monetary financing by 1.5 percent of GDP compared to the previous year. Given continued compression of tax revenues, partly due to FX distortions, significant rationalization of spending was needed to meet our macroeconomic stabilization objectives.

30. Fiscal consolidation will be maintained over the medium term to underpin sustainable public finances for long-term development. We will reduce the primary federal government deficit, on a cash basis, from 1.1 percent of GDP in 2023/24 to 0.7 percent of GDP in 2027/28 (quantitative performance criterion, QPC). The general government deficit will decline in line with that of the budgetary federal government, underpinned by continued restraint in borrowing by regional governments. To accommodate the fiscal package (about 1½ percent of 2024/25 GDP) supporting the FX reform, the overall deficit, excluding budget grants, will temporarily widen by 0.7 percent of GDP in 2024/25 (half of the fiscal package cost).

31. Durably raising domestic revenues is essential to increase space for social and capital spending (QPC). Over the medium-term, a 4-percentage point rise in the tax-to-GDP ratio to 10.2 percent of GDP by 2027/28, including 0.8 percent of GDP from the foreign exchange impact,

will provide a sustainable resource base for raising pro-poor and capital expenditure by 2 and 1.2 percent of GDP, respectively, and help meet recovery and reconstruction needs. Our revised Medium-Term Fiscal Framework for 2024/25-27/28, which will be published in mid-July 2024, defines the strategy for reaching this goal. We are committed to undertaking additional revenue and expenditure measures that may become necessary to ensure the attainment of our revenue and primary deficit targets.

32. We have embarked on comprehensive tax reforms. We have formed a steering committee headed by the Minister of Finance and an export working group with representatives from the Ministry of Finance, the Ministry of Revenue, and the Customs Commission to provide leadership and secure comprehensive and synchronized implementation and monitoring of tax policy and tax administration reforms. In consultation with the IMF, we are developing a National Medium-Term Revenue Strategy (NMTRS), which will be adopted by the Council of Ministers and published (SB, end-September 2024). The NMTRS will guide tax reforms, considering economic growth and the distributional impact of the tax system over the course of the program. Revenue yields will come primarily from tax policy reforms at first, with gains from tax administration reforms setting in over time.

33. We are taking strong upfront tax policy measures that will generate revenues of 0.7 percent of GDP in 2024/25, including:

- Introduction of an excise stamp regime (following finalization of the tender, selection of the provider, and issuance of an excise stamp track and tracing directive) and circular that increases specific rates by accumulated inflation since 2020 on beer and tobacco under Schedule One of the 2020 Excise Tax Proclamation (for expected revenue yield of 0.3 percent of GDP, prior action). The adjustment for beer is to be implemented immediately starting July 2024 while that on tobacco will be occur following the introduction of the excise stamp on tobacco.
- Adoption and publication of a new VAT Proclamation, which maintains a uniform 15 percent tax rate, and MoF Directive which removes exemptions less targeted to the poor (for expected revenue 0.5 percent of GDP, prior action). This involves removing exemptions granted to specific organizations by Directive, on transportation services (taxi and car sharing), telecommunications, e-commerce, financial, and utilities (water and electricity with consideration for low-income and vulnerable groups). Further, we have clearly defined list of exempt medical equipment and services, removed exemption on non-prescription medicines, sugar, and kerosene.
- Implementation of the new Real Estate Property Tax Proclamation is on track to yield 0.1percent of GDP in FY2024/25, with plans for advance rollout by the largest cities in FY2024/25 and nationwide implementation (at least 0.3 percent of GDP) by FY2026/27, as legally mandated.

34. We are committed to strengthening tax and customs administration and improving compliance. Our efforts will focus on strengthening taxpayer registration, e-filing and digitalized

self-assessment, compliance risk management (particularly in construction, manufacturing, and retail), and tax audit efficiency, guided by specific actions and timelines as will be specified in the NMTRS. The Customs Commission will digitalize the valuation and the tariff classification process to strengthen tax base control and transparency. To advance swiftly with digitalization of tax revenue administration, the 2024/25 Federal Budget allocates the full funding requirement to procure the Integrated Tax Administration System. The next TADAT Assessment, planned for 2025, will assist in identifying the gaps and facilitate the designing and prioritization of tax administration reforms. We will continue to work closely with capacity development partners to specify new policies by June-2025, to: (i) raise revenue through agricultural sector taxation while ensuring efficiency and fairness by keeping farmers with low incomes below the taxable threshold, (ii) revise the income tax proclamation covering personal income tax, corporate income tax, and double taxation agreements, in line with objectives of NMTRS, and (iii) streamline and reduce tax revenue losses from the proliferation of tax incentives and tax holidays across a range of economic sectors. We will consult with the Fund before implementing any voluntary asset repatriation program. Any such program will aim to ensure full transparency and consistency with international Anti-Money Laundering/ Combating the Financing of Terrorism (AML/CFT) standards and avoid erosion in the legitimacy and fairness of the tax system.

35. The FY2024/25 Budget contains a spending package of 1½ percent of GDP that will help mitigate the adverse social impact of FX reform. Our fiscal response stands on four pillars:

- **We will prioritize expanding the existing targeted social safety net (PSNP) as the most cost-effective, direct, and efficient way of providing support to vulnerable people**. We have taken steps to ensure timely expansion of the PSNP to the *woredas* (districts) that are not yet covered. Adjustments to rural and urban PSNP will include raising benefits to mitigate erosion from accumulated inflation. This requires raising the budgetary allocation for PSNP from about 0.1 to 0.5 percent of GDP per year (indicative target, IT). The envisaged additional social safety project financing by the World Bank (0.2 percent of GDP) will co-finance PSNP and help cover the funding gap of the existing PSNP5 over the next 18 months.
- **We will provide temporary direct subsidies on select food items and medicines to accommodate adequate and timely expansion of PSNP.** This will allow cushioning the immediate consumer price impact of FX reform, despite the inefficiencies of untargeted schemes. In the event of socially unsustainable rises in prices for essential imported commodities (such as wheat, edible oil, and medicines) we will purchase imported commodities through the Ethiopian Trading Business Corporation for domestic distribution at subsidized prices, up to a cap in value of 0.2 percent of GDP, which would be recognized in full on the federal budget. These subsidies will be phased out entirely by June-2025. We will refrain from direct price controls.
- **We will provide temporary, time bound, and gradually declining fuel subsidies to partially address the large impact of FX reform on households.** The move to a market-clearing exchange rate will open a large price gap vis-à-vis fuel costs (estimated at around 35 percent of the breakeven), with an annual cost of 1 to 1¼ percent of GDP. To contain the

fiscal costs to 0.5 percent of GDP and smooth the impact of price increases on the public, we will raise fuel prices by 5 percent per month to close the price gap resulting from FX reform by early 2025. We will continue to provide targeted fuel subsidies for public transportation that will cushion the impact for vulnerable households across the country. To cap public transport subsidy costs at 0.1 percent of GDP and mitigate leakages, we will continue to rely on the current targeting mechanisms and digital solutions (rebates through mobile payment and digital wallets) and limit eligibility to city and regional public bus transportation.

- **We will increase fertilizer subsidies to 0.5 percent of GDP.** Even though under-fertilization remains among the most important factors behind relatively low production yields in wheat and other cereals, addressing suppressed fertilizer demand at the current price subsidy level would be prohibitively expensive (in terms of fiscal and additional external financing needs). Increasing the budgeted fertilizer subsidy from the current level of 0.3 percent of GDP to 0.5 percent of GDP will suffice to retain the existing subsidy level for farmers. In future, we will reduce fertilizer subsidy costs to 0.3 percent of GDP by FY2025/26.

36. We will settle legacy fuel subsidy debt and prevent the reemergence of similar liabilities. Fuel subsidy reform since December-2021 has already eliminated about 1 percent of GDP in extrabudgetary fiscal costs and helped reduce the large stock of subsidy related public debt. Our plan is to continue increasing fuel pump prices to above cost parity to clear the subsidy debt (projected at 80 billion Birr as of end-June 2024) and rebuild a surplus at the Fuel Price Stabilization Fund and to eliminate the fuel price subsidy net of taxes by end-2025. The Council of Ministers will increase the authorized capital of EPSE to offset losses stemming from FX reform (given trade credit liabilities), estimated at 120 billion Birr as of end-June 2024, and to allow transition to lower cost sight letters of credit for future fuel purchases. Starting with the FY2024/25 Budget, fuel subsidies will be explicitly recognized as federal government spending. To ensure its sufficient Birr liquidity, EPSE will bill MoF on a month ahead basis and MoF will fully settle in cash within a month the amount of the projected fuel subsidy and EPSE's additional cash shortfall related to maturing FX liabilities. We plan to seek technical assistance from the Fund to devise a strategy for rebuilding and managing fuel price stabilization buffers and implementing transparent and automatic fuel price adjustment.

37. In the medium-term, we plan to increase pro-poor spending and capital expenditure, as a share of GDP, to above pre-2019 levels. Higher revenues will underpin sustainable expansion of public spending, which will also help meet reconstruction needs. Specifically:

- **Safety nets:** we will continue to enhance the adequacy, coverage, and sustainability of our expenditure on the Productive Safety Nets Program. The increased budgetary envelope for the PSNP will help to expand coverage of the food insecure and poorest households, building robust infrastructure for shock response and humanitarian disaster support. We will work with development partners to strengthen targeting mechanisms, update and improve poverty assessment metrics, and pursue regular program evaluations with a view to strengthening effectiveness and credibility of our poverty reduction programs. As the cost-

of-living shock abates, we will concentrate PSNP on durable livelihood improvement to reduce poverty.

- **Public investment:** Promoting sustainably financed growth-enhancing investment in public infrastructure is one of our main priorities. We adopted the Public Investment Proclamation (2020), and notwithstanding the freeze on the start of new investment projects, took steps to strengthen the public investment framework, focusing on project-level pre-screening tools. To tackle the large unfinished public investment portfolio and facilitate medium-term capital expenditure planning, we plan to formulate an explicit framework for centralized prioritization, selection, and budgeting of the investment project pipeline, which will be backed by an IT system, currently under development, to systematize public investment data. We have undertaken a comprehensive review of the public investment management institutional landscape (March 2024 IMF Public Investment Management Assessment (PIMA) mission) and will publish the report. We will use the findings of this assessment, which also included a climate module, to improve planning, allocation, and implementation stages, as well as transparency of the public investment management cycle.
- **Reconstruction:** Our Resilient Recovery and Reconstruction (3RF) planning framework lays out how we aim to address reconstruction needs following the war in Tigray. Given the large cost, estimated at close to US$20 billion, and limited budgetary resources, we will leverage contributions from development partner and the private sector, including via public-private partnerships, to mobilize resources. So far, donor projects and a multi-donor trust fund have received contributions of some US$335 million. Given the large remaining financing needs, interventions will have to be carefully prioritized and to a large extent rely on private funding.

38. We will enhance transparency and accountability in the management of public finances. Starting with FY2024/25, MoF will publish monthly federal budget revenue, expense, and financing execution. The ongoing rollout of the integrated financial management information system (IFMIS) will also facilitate preparation of a mid-year review report (a 2019 Public Expenditure and Financial Accountability report recommendation) analyzing economic development, consolidated budget performance against commitments, cash flow, near-term fiscal risks, and proposed policy responses. The publication of all these documents should include making them available on the ministry's website.

39. We will improve transparency and monitoring of fiscal risks from extrabudgetary units. We will expand of the coverage of extrabudgetary units in government finance statistics, to comply with GFSM2001/2014, specifically moving the large extrabudgetary government units (the Oil Price Stabilization Fund and LAMC) into the general government perimeter. Guided by Fund TA we will strengthen Government Finance Statistics compilation, reconciliation, and reporting practices. In addition, fuel taxes (VAT and excise) will be recognized as government tax revenues starting in FY2025/26. The introduction of public sector obligations (PSO) framework, supported by the World Bank, will be an important step toward a comprehensive disclosure of quasi-fiscal activities and managing fiscal risks.

G. Public Debt

40. Supported by the financing provided by the IMF-supported program, we will agree Memoranda of Understanding (MoUs) for the treatment of official bilateral debt with the Common Framework official bilateral creditors and make progress in talks with other creditors by the time of the second review. The MoUs will specify: (i) the reduction in debt service during the period determined by the parties to the MoU; (ii) the extension of the duration of payments and, if necessary; (iii) the reduction in the present value of payments. These parameters would guide the implementation of relief by other official bilateral and private creditors through bilateral agreements following comparable treatment.

41. We continue our efforts to resolve arrears. The government is making best efforts to resolve external arrears. The arrears are "deemed away" under the IMF's policy on arrears to official bilateral creditors, as the underlying CF agreement is adequately representative the creditors have consented to proceed with the program in accordance with the IMF's policy on arrears to official bilateral creditors. No new external arrears will be accumulated in line with our commitment to a zero limit on accumulation of external arrears (continuous performance criterion).

42. We will refrain from new non-concessional borrowing. The Government will continue to ensure that all public and publicly guaranteed (PPG) external financing agreements are on concessional terms (at least 35 percent of grant element) and are taken up at a pace consistent with the external borrowing plan (see Technical Memorandum of Understanding—TMU). This will be underpinned by a zero limit on contracting and guaranteeing PPG non-concessional borrowing (continuous performance criterion) and an indicative target on the PV of contracting and guaranteeing new PPG external borrowing (see TMU). Details of all new contracted loans will be communicated to the IMF.

43. We request an exemption from the zero-limit on non-concessional borrowing for the macro-critical Koysha Hydroelectric Dam project. Despite sustained efforts, we have not been able to secure concessional financing to finalize this project, which is critical for our medium-term growth and poverty-reduction strategy and is already some 66 percent completed. Securing external financing and resuming construction are crucial to avoid incurring contractual penalties due to delays, potential termination, and overall construction cost increases. The project is expected to generate 1,800 MW of power upon completion, equivalent to 40 percent of the current generation capacity. Per capita electricity consumption is only 5 percent of the global average, and nearly 57 million people, primarily in rural areas, are without this essential service. Koysha is expected to underpin improved access to electricity, rural electrification, generate export revenues, and strengthen climate resilience.

44. We are taking measures to manage the legacy of domestic public debt, balancing fiscal sustainability with the gradual elimination of financial repression. This will support bond market development, credit allocation to the private sector and ensure that the cost of funding for

the government is market determined, reflecting the opportunity cost of using investable funds. We are taking the following actions to phase out non-market-based financing of the public sector:

- Eliminating monetary financing of public deficits, and addressing the capital position of NBE comprehensively, including the stock of government debt (¶26).
- We intend to phase out the mandatory purchase of 5-year treasury bonds by commercial banks, by end-June 2025. In 2024/25, we will require banks to purchase 50 billion Birr of 5-year T-bonds at 9 percent interest (minimum savings rate plus 2 percent). Thereafter, we intend to develop the market for longer-dated government securities exclusively through market-based mechanisms.
- We will propose a sustainable funding strategy for the Development Bank of Ethiopia (DBE) by the third review and the requirement that financial institutions purchase DBE bonds will be removed before the fifth review of the program. In the interim, the yield on newly issued DBE bonds will be aligned to the yield of the most recent Treasury bond at time of issuance.
- We are implementing a voluntary exchange of the current stock of T-bills held by Public Servants Social Security Agency and the Private Organizations Employees' Social Security Administration for 10-year securities paying 9 percent interest, that (i) better matches duration of the pensions funds' assets and liabilities; (ii) protects pensioners through returns expected to keep pace with medium-term inflation; and (iii) provides substantial debt service relief to the Treasury.
- For all other purposes, we will rely on market-based domestic financing, notably through developing the T-bill market. We will inform Fund staff before taking any action to roll over or restructure public sector liabilities at rates below contemporaneous T-bill rates, including the T-bill exchange noted above.

45. We are strengthening debt management and transparency. We will develop a medium-term debt management strategy by the end of FY2024/25, with capacity development support as needed. We are enhancing the comprehensiveness and transparency of our debt disclosures by publishing in the public debt bulletin government guaranteed DBE bonds.

H. State-Owned Enterprise Policy

46. We have strengthened oversight and governance of the SOE sector. The creation of two entities holding the state's interests in SOEs (the Public Enterprise Holding and Administration Agency, PEHAA 2018, and Ethiopian Investment Holdings, EIH, 2022 have substantially modernized and centralized SOE oversight and fiscal risk management:

- **PEHAA and EIH have made progress in addressing long delays in submitting audited accounts by SOEs and improved IFRS compliance**. To that end, 23 out of 35 PEHAA and EIH supervised SOEs have produced audited financial statements for 2021/22, while 20 out of 26 EIH SOEs and three out of nine PEHAA SOEs had finalized their 2022/23 audited financial reports by October 2023. The 2022/23 IFRS-based and audited financial statements

for three critical SOEs, and the 2021/22 accounts for another four[1], will be published by end-September 2024 (SB, end-September 2024).

- **We are developing a comprehensive digital reporting system**. This system will enable MoF supervision of SOEs' key performance indicators and monitoring of financial relations between SOEs and the state, including financial flows (subsidies, lending, and tax obligations), implicit transfers (public service obligations—PSO, preferential tax regimes), and loan guarantees and contingent liabilities. The IT budget allocation has been approved and the project will be operational by June 2025.
- **The MoF fiscal oversight function will be strengthened to ensure centralized periodic, timely, and standardized SOE financial and performance indicator reporting.** An inaugural SOE sector risk report was published in May 2023, covering financial and operational performance of 21 SOEs in PEHAA's portfolio for the period 2018/19-2020/21. To build on this progress, we will establish a dedicated SOE Directorate tasked with central SOE oversight function and a clear mandate vis-à-vis EIH and PEHAA. The unit will provide high level data analytics and strategic insight into SOE sector regarding actual, potential, and contingent fiscal exposure, aggregated performance particularly related to policy delivery and safeguarding of public assets and financial return (dividend).

47. We are developing a comprehensive legal framework governing SOEs. The new Public Enterprise law was approved in January 2024. To assess and recognize uncompensated SOE activities undertaken in the public interest rather than on a commercial basis, we will implement PSO costing and disclosure regulations, beginning with pilots in the electricity sector by December 2025, and assess SOE performance in meeting their public service mandates. These measures will lead to transparent budgetary disclosure of and compensation for non-commercial services. EIH and PEHAA, in their role as commercially oriented shareholders on behalf of the state, will continue to perform a key function in pressing for cost efficiency, good governance, and transparency for the sector. EIH has finalized a dividend policy with respect to its subsidiaries, prescribing transparent and sustainable profit retention and distribution that also considers the SOEs' investment plans and treasury financing and debt servicing needs. To ringfence public finances from SOE operations in line with Public Debt and Guarantee Issuance Directive (No 46/2017), we will refrain from further expansion of state guarantees.

48. We are taking measures to restore the viability of the three largest loss-making SOEs (EEP, ERC, ESC). The transfer to LAMC of the debts of the most indebted nonfinancial SOEs contributes to restoring their financial health. Further actions are required to improve their operational viability.

- **In the electricity sector:** The Petroleum and Energy Authority (PEA) developed and adopted new tariff setting methodologies for the supply, transmission, and distribution of electricity.

[1] The 2022/23 audited accounts will be published for Ethiopian Electric Power (EEP), Ethiopian Electric Utility (EEU), and Ethiopia Petroleum Supply Enterprise (EPSE), while Ethiopian Sugar Corporation (ESC), Ethiopian Railway Corporation (ERC), Ethiopian Engineering Group (EEG), and Ethiopian Construction Works (ECW) will publish 2021/22 audited accounts.

The new framework underpins the 2025-2028 four-year tariff adjustment plan that aims to reach cost recovery. Under this plan, which was approved by the Council of Ministers in June 2024, end-user electricity tariffs will be increased by on average about 10 percent each quarter to move toward cost recovery for the electricity sector, with larger price increases in the beginning. In line with the June-2024 Council of Ministers decision on the multi-year electricity tariff increase, the first quarterly tariff increase will be implemented by end-September 2024 (SB). The adequacy of the tariff plan will subsequently be reviewed on an annual basis given prospective changes to the sector's cost structure arising from exchange rate, inflation, and other economic developments. A revised schedule of electricity tariff changes will be put into adopted by end-June 2025 to ensure full recovery of the sector's operational and debt service costs by 2028.

- **In the railway sector:** Building on efforts to strengthen standards and timeliness of SOE financial reporting, we will develop a strategy to address financial vulnerabilities and fiscal risk emanating from the Ethiopian Railway Corporation. Proposed reform areas include streamlining the fragmented infrastructure management and operations, including allowing the private sector to participate both in management and operations of the railway sector. We aim to secure financial sustainability and continuity in the provision of public funding through targeting diversified funding sources, ensuring long-term commitments from the government, and developing sustainable cost recovery strategies. Further, by creating a robust institutional framework, we aim to attract private investors, leverage their expertise, and accelerate the development of a modern, efficient, and integrated railway network. Complementary measures include finalization of the legal framework for the liberalization of key logistics sub-sectors (dry port, freight, and logistics services) by end-December 2026
- **In the sugar sector:** We have relaunched the privatization process for nine sugar estates to attract private sector investment to exploit Ethiopia's sugar industry potential and help recoup the large public investments in the sector. We aim to finalize the bid process and transfer assets to successful private investors by end-December 2025. Finalizing the bid process and transferring ownership to successful investors by end-December 2025 will be a major milestone in propelling the Ethiopian sugar industry to become a leading regional exporter and a significant contributor to our national economic growth strategy, Home Grown Economic Reform 2.0.

I. Financial Sector Policy

49. To complete CBE's transition to a sound, viable, and commercially oriented bank, we are addressing legacy issues arising from CBE's role in lending to SOEs. We have decisively strengthened CBE's capital position by (i) writing off all of CBE's claims on LAMC; (ii) fully provisioning CBE's claims on EEP; (iii) covering losses incurred from CBE's NOP that are not made good through CBE's own operations; and (iv) restoring CBE's capital adequacy ratio to 8 percent. To achieve this objective:

- We have made a capital injection with government securities in an amount equal to CBE's claim on LAMC, the fully provisioned amount of CBE's claims on EEP, plus the residual

amount required to bring CBE's capital adequacy ratio up to the regulatory minimum (Prior Action). CBE will contribute to covering the provisioning requirement through retaining earnings and paying no dividends until CBE's capital adequacy ratio reaches 12.5 percent.

- The government securities used in the recapitalization will ensure the liquidity and viability of CBE while respecting fiscal constraints. They comprise a ten-year amortizing bond with a three-year grace period, paying (i) 9 percent for the first year, at least 10 percent for the second year, and at least 10.5 percent in the third year; and (ii) the prevailing monetary policy rate thereafter, to be reset annually. The recapitalization bonds are tradable securities that can be used as collateral for transactions in the interbank market and with NBE.
- The reform, restructuring, and recapitalization of CBE will be supported by a World Bank Financial Sector Strengthening Project that is about to be finalized. This project, with World Bank financial and technical support, aims to ensure that CBE can function as a fully capitalized, commercially oriented, and viable financial institution in a competitive financial sector.
- With the support of the World Bank, we commit to reforming the governance of CBE by (i) ensuring arm's length dealings with the public sector on commercial terms; (ii) appointing directors independent of the government for at least one third of positions on the board of directors; (iii) ensuring a robust risk governance framework; and (iv) enforcing through the NBE as independent supervisor, strict adherence to prudential regulations and directives. We will review CBE's public policy obligations in the context of SOE policy. Maintaining tight financial controls and a cautious lending model will be important as the risk management framework is being strengthened.
- MoF and CBE will revise the memorandum of understanding on guaranteed lending to ensure that restructuring of guaranteed debts follows the regulations on debt restructuring by the second review.

50. The NBE will revise the asset classification and provisioning directive in accordance with international practices, with capacity development support as needed to ensure the prompt identification and provisioning of NPLs, including with public entities, and including appropriate recognition of non-performing guarantees (SB, second review). We are also upgrading our capital framework (Basel II/III) with the support of Fund TA.

51. The entry of new banks and the development of capital markets will help to improve access to finance and the allocation of credit. Thirteen new banks have entered the market since September 2021, increasing competition. We will enhance banking regulation and supervision to strengthen: (i) measurement of FX exposures, interest rate, and funding risks and (ii) stress testing. We will review and update the regulatory framework for licensing, and for mobile money institutions.

52. We are developing the capital markets. Formalizing existing over-the-counter markets in equities and debt securities will provide alternative sources of funding for firms, enhance risk sharing and support innovation—but this is likely a longer-term endeavor. The market will facilitate, and in

turn be supported by the development of our pension and insurance industries. The Capital Market Proclamation (No 1248/2021), issued in 2021, provides the legal framework for regulating capital markets, including by establishing the Ethiopian Capital Market Authority (ECMA), and creating the Ethiopian Securities Exchange (ESX). ECMA is the regulatory body responsible for granting exchange licenses, setting the minimum admission criteria, and providing conditions for listing on the exchange. ESX is expected to become operational by November 2024, providing the first formal exchange for secondary market debt securities and equities.

- We are committed to developing the asset management industry, including by ongoing regulatory work on an industry directive supported by the Capital Market Proclamation that, among others, will establish a solid framework for the development of collective investment schemes (CIS). The CIS products will further expand financial inclusion and resource mobilization with funds invested in government and corporate fixed income instruments.
- Capital market development will be supported by clear and predictable taxation of tax The ECMA has effectively engaged the MoF in promoting favorable taxation policies as well as clarity and predictability of taxation treatment for capital market products. This includes the adoption, in principle, of the concept of taxation "neutrality" in relation to capital market products relative to alternative funding mechanisms, including bank lending and to direct investment.

J. Promoting Sustainable, Inclusive Growth

53. Tangible progress in reforming the business environment has been made under HGER, but gaps remain. The Commercial Code, enacted in 1960, was revised in 2021, including with respect to insolvency procedures and protection of the rights of minority shareholders. Sixty previously closed sectors and sub-sectors (e.g., logistics and telecom) have been opened to both domestic and foreign investment. Legal frameworks for contract farming have been put in place to provide alternative sources of finance and market access for farmers. Liberalization of the telecom sector has enhanced competition and paved the way for digital transformation. On mining, the "National Artisanal and Small-Scale Mining Strategy" was implemented to encourage formalization of the sector. Finally, a national ID is being rolled out which will provide the basis for increasing financial inclusion and public service delivery.

54. Structural reforms under HGER2.0 focus on creating a conducive trade and investment climate and increasing productivity across key sectors, which will contribute to poverty reduction and improving living standards. Retail and wholesale market structure will be modernized, including through sequenced liberalization. We are pursuing accession to global and regional trade agreements—including the World Trade Organization—to improve access to markets and support exports. Efforts will be stepped up to simplify and fully digitalize trade registration, licensing, certification, and customs polices. Rural land administration and use rights will be reformed to unlock economic value through investment. Financing strategies for agriculture will be implemented to allow for lease financing, movable collateral, and contract farming. Privatization of SOEs will continue, including partial privatization of Ethio-telecom, issuance of a second telecom

license and the sale of eight sugar factories. The roll-out of the National Digital ID system will be completed. Strategic e-government initiatives will be launched to bring efficiency and effectiveness to public service delivery.

55. We are adopting policies to bolster climate resilience and food security. Ethiopia faces significant challenges from climate change. The Climate Resilient Green Economy Strategy defines adaptation and mitigation policies, building a green economy and meeting commitments made in our nationally determined contributions for greenhouse gas emissions under the Paris Agreement. Our essential infrastructure projects also consider adaptation to climate change, including on sustainable green energy generation and distribution, irrigation systems, and water reservoirs to ensure water security—a key consideration for food security. To further improve climate-aware planning and coordination between entities, we conducted a Climate Public Investment Management Assessment (C-PIMA) in March 2024, and completed a Country Climate and Development Report with the World Bank in February 2024. The recommendations of these reports will inform our policy agenda, including for potential borrowing operations with international financial institutions.

K. Economic Statistics

56. Improving the quality of economic statistics is a key priority under HGER2.0. In December 2023, the government adopted Ethiopian Statistical Development Program (ESDP) to strengthening capacity to collect and process data and improve the economic data available to the public. We will conduct a diagnostic of national account statistics using the IMF Data Quality Assessment Framework by December 2024, with the support of Fund technical assistance, to identify a timeline toward producing and publishing annual and quarterly GDP by production and expenditure side. We will use the findings of this diagnostic to complete a rebasing of the national accounts to base year 2025/26 by December 2026. Other priority areas include aligning data presentation with BPM6 in the external sector statistics and price indices.

L. Risks and Contingencies

57. The authorities stand ready to adjust policies if risks materialize. Downside risks to the program in the near-term include disruption from domestic conflict if this was to intensify; rising import costs due to new international commodity price increases; and potentially social unrest associated with higher inflation. An abrupt slowdown of global growth also presents a risk via its adverse effects on exports and potentially remittances. Over the medium-term, risks from climate change are salient. Climate shocks could exert pressure on food security and food prices. If these risks materialize, we stand ready to adjust our policies, in close consultation with IMF staff, to ensure the achievement of the program's objectives.

M. Program Design, Financing and Monitoring

58. The ultimate responsibility for program monitoring and coordination will rest with the Ministry of Finance and National Bank of Ethiopia. To ensure coordinated implementation of the program, the MoF and NBE will consult with the other public institutions involved in meeting program objectives to track progress on various targets and reforms under the program. Similarly, the MoF will provide oversight responsibility for ensuring that public spending is compliant with budget limits.

59. The program will be monitored by the IMF's Executive Board. Progress in implementation of the policies under this program will be evaluated through quarterly reviews in 2024 (August 16th and end-September), then moving to semi-annual reviews of the quantitative performance criteria (end-June and end-December), indicative targets, and structural benchmarks, as presented in Table 1 and Table 3, respectively. Detailed definitions and reporting requirements for all performance criteria and indicative targets are presented in the Technical Memorandum of Understanding (TMU) attached to this letter, which also defines the scope and frequency of data to be reported for program monitoring purposes and presents the projected assumptions that form the basis for some of the performance assessments. The first two quarterly reviews will take place on or after September 10, 2024, and December 10, 2024. To this end, the government plans to:

- Not introduce or intensify restrictions on payments and transfers for current international transactions, introduce multiple currency practices, enter into bilateral payment agreements that are inconsistent with Article VIII of the IMF Articles of Agreement, or introduce or intensify import restrictions for balance of payments purposes; and will complete an Article VIII assessment before the second review of the program.
- Adopt any new financial or structural measures that may be necessary for the success of its policies, in consultation with the IMF.

60. We will strengthen internal coordination and monitoring mechanisms to ensure strong program implementation. The MoF and the NBE will establish a Technical Committee to monitor and report program performance to the Minister of Finance.

61. The government estimates that the residual financing gap of US$10.7 billion for the 2024/25–2027/28 program will be covered. In addition to US$3.4 billion from the IMF, we currently expect US$3.75 billion in budget support from the World Bank. The remaining gap of US$3.5 billion will be filled by financing associated with debt treatment under the Common Framework.

62. The government believes the policies specified in this MEFP provide a foundation for sustaining growth, reducing inflation, and alleviating poverty, and we stand ready to take additional measures if required. The government will provide IMF staff with the information needed to assess progress in implementing our program as specified in the TMU and will consult with Fund staff on any measures that may be appropriate at the initiative of the government or whenever the Fund requests a consultation. The government intends to make this letter and the

TMU available to the public. In this context, it authorizes the IMF to arrange for them to be posted on the IMF website, subsequent to Executive Board approval.

63. Accordingly, the government is requesting Board approval of the policies set forth in the MEFP, and disbursement of the first loan installment, totaling SDR 767 million, out of a total four-year arrangement of SDR 2,556 million.

Table 1. The Federal Democratic Republic of Ethiopia: Quantitative Performance Criteria and Indicative Targets, June 2024 – June 2025

(In millions of Ethiopian birr, unless otherwise indicated)

	end-Jun 2024	Aug. 16, 2024	end-Sep 2024	end-Dec 2024	end-Mar 2025	end-Jun 2025
	Staff est. Initial level	Program target	Program target	Program target	Indicative target	Program target
Quantitative performance criteria						
Net financing of the general government primary balance (ceiling, cumulative change since previous June, includes grants and excludes interest payments) [1/, 2/]	146,000	N/A	42,000	69,000	95,000	106,000
Net international reserves (floor, cumulative change since previous June, US$ millions) (end-Jun 2024 is for initial level)	512	630	500	400	300	100
Tax revenue collected by the federal government (floor, cumulative sum of tax revenues collected since the beginning of the current fiscal year)	384,000	N/A	86,000	192,000	347,000	578,000
Net NBE claims on the general government (ceiling, cumulative change since previous June) (end-June 2024 for initial level)	616,300	0	0	0	0	0
Continuous performance criteria						
Contracting or guaranteeing of external non-concessional debt by the general government, the NBE and public enterprises (ceiling, US$ millions) [3/]		0	0	0	0	0
Accumulation of external payment arrears by the general government, the NBE and public enterprises (ceiling, US$ millions)		0	0	0	0	0
Indicative targets						
Gross claims on public enterprises by commercial banks (ceiling, cumulative change since previous June) (end-Jun 2024 is for initial level) [2/]	760,775	N/A	37,000	74,000	110,000	147,000
Government Contributions to Productive Safety Net Programme cash transfers (floor, cumulative sum of contributions since the beginning of the current fiscal year) [4/]	9,000	N/A	6,500	22,100	33,200	51,400
Present value of external new debt (excluding IMF credit) contracted or guaranteed by the general government, the NBE and public enterprises (ceiling for the fiscal year ending June, US$ millions)		N/A	2,000	2,500	2,750	3,000
Memorandum items:						
Official external grants disbursed to the government (US$ millions, cumulative since previous June)	791		210	420	630	840
Official external loans disbursed to the government (US$ millions, cumulative since previous June)	627		1638	1775	1913	2050
Gross privatization proceeds (US$ millions, cumulative since previous June)	0	0	0	0	0	0

Sources: Ethiopian authorities and IMF staff estimates and projections.

1/ Excluding on-lending from the general government.

2/ Excludes commercial banks' claims related to Addis Ababa Housing credit.

3/ The limit is a continuous target (ceiling) on the contracting of non-concessional debt for the fiscal year by the government including general government, NBE and public enterprises (see TMU). An exception is applied for new non-concessional external debt contracted or guaranteed by the general government for the Koysha dam project, which is capped at USD 950 over the duration of the program.

4/ Excludes in-kind benefits and donor contributions. Includes Government of Ethiopia contributions to cash transfers to beneficiaries under the rural Productive Safety Net Programme (PSNP) and Urban Productive Safety Net Programme (UPSNP).

Table 2. The Federal Democratic Republic of Ethiopia: Prior Actions

Measure	Rationale	Status
1. NBE to publish a directive announcing that Authorized Dealers can buy and sell FX from their clients and among themselves at freely negotiated rates, allowing market participants to determine a market-clearing exchange rate for current account transactions; and in consultation with Fund staff, eliminate the current account controls (the rationing of FX allocations for imports and the three-tier priority list of imports, the NBE import reference price system linked to minimum import prices by customs office, and the security deposit requirement of 50 percent when queuing for FX for import payments), removal of which is necessary for reaching market unification, with immediate effect, and publicly communicate the same.	Liberalization of foreign exchange market	To be completed
2. Introduction of an excise stamp regime, including finalizing the excise stamp tender, issuing excise stamp track and tracing directive, and issuing a circular on adjusting for inflation on specific excise rate on beer.	Tax revenue mobilization	Completed
3. Adoption by MoF of VAT directive to remove exemptions less targeted to the poor, to be specified in consultation with the Fund.	Tax revenue mobilization	Completed
4. The Federal Auditor General has authorized NBE to engage a new auditor; NBE will adopt a selection and rotation policy for an external auditor; and NBE will float a competitive bid for the audit starting with 2022/23 financial statements by a suitably qualified firm that includes international experts experienced in auditing central banks.	Update and modernize governance of the NBE and reduce vulnerability to corruption	Completed
5. The Federal Government has made a capital injection in the Commercial Bank of Ethiopia (CBE) with government securities in an amount equal to (i) CBE's claim on LAMC; (ii) the fully provisioned amount of CBE's claims on EEP; and (iii) the residual amount required to bring CBE's capital adequacy ratio up to the regulatory minimum.	Financial sector stability	Completed
6. Announcement of a target monetary policy rate of 15 percent, at the mid-point between the standing lending and deposit facility rates, set at ± 3 percent around the policy rate, with the interbank lending rate as an operational target	Reduce financial repression	Completed
7. NBE to begin conducting regular fixed rate (the policy rate) and full allotment open market operations before the move to a market-clearing exchange rate to manage banking sector liquidity, aligned to the monetary policy stance.	Strengthen monetary policy implementation	Completed

Table 3. The Federal Democratic Republic of Ethiopia: Proposed Structural Benchmarks

Measure	Rationale	Target Date
1. Council of Ministers to adopt and publish a medium-term revenue strategy (drawing on FAD TA) specifying tax policy and revenue administration compliance measures with a clear timeframe.	Tax revenue mobilization	End-September 2024
2. NBE to issue an order to all banks not in compliance with the regulatory threshold on net open position to develop plans to ensure full compliance with the regulation by end-June 2025.	Financial sector stability	End-September 2024
3. Publish IFRS-based and audited financial statements for 2022/23 for Ethiopian Electric Power (EEP), Ethiopian Electric Utility (EEU), and Ethiopia Petroleum Supply Enterprise (EPSE); and for 2021/22 for Ethiopian Sugar Corporation (ESC), Ethiopian Railway Corporation (ERC), Ethiopian Engineering Group (EEG), and Ethiopian Construction Works (ECW).	Strengthen SOE finances and reduce vulnerability to corruption	End-September 2024
4. NBE to implement an emergency liquidity assistance framework for financial stability purposes provided at the discretion of NBE to viable (solvent) banks with adequate collateral and a funding plan to recover the liquidity situation of the bank	Strengthen monetary policy implementation	End-September 2024
5. Implement the first quarterly electricity tariff increase under the multi-year plan as approved by the Council of Ministers in June 2024.	Strengthen SOE finances	End-September 2024
6. The NBE to finalize and publish audited financial statements for 2021/22-2022/23.	Update and modernize governance of the NBE	End-December 2024
7. NBE to submit to Parliament comprehensive draft legal amendments to the NBE Proclamation, to be prepared in consultation with IMF staff, with respect to the NBE's mandate, decision-making structure (internal check and balances and collegial implementation of decisions), accountability, transparency, and autonomy.	Update and modernize governance of the NBE	End-December 2024

Attachment II. Technical Memorandum of Understanding

Addis Ababa, July 10, 2024

1. This Technical Memorandum of Understanding (TMU) describes the performance criteria (PCs), indicative targets (ITs), and structural assessment criteria established by the Ethiopian authorities and the staff of the International Monetary Fund (IMF) to monitor the program supported by the Fund's Extended Credit Facility (ECF) arrangement, as described in the Memorandum of Economic and Financial Policies (MEFP) and its attached tables. It also specifies the content, the periodicity, and deadlines for the transmission of data to Fund staff for program monitoring purposes.

A. Institutional Definitions

2. Unless otherwise specified, the government is defined in this TMU as the general government of Ethiopia, the National Bank of Ethiopia (NBE), the Liability and Asset Management Corporation (LAMC), and the state-owned or public enterprises.

3. The general government is defined for program monitoring purposes as the budgetary central government plus state governments and woredas, excluding state-owned enterprises and existing extra-budgetary funds (listed in the next paragraph). The definition of the general government includes any new funds, or other special budgetary or extra-budgetary entities, at federal, state, or local level, that may be created during the program period to carry out operations of a fiscal nature as defined in the IMF's Manual on Government Finance Statistics 2014. The authorities will inform IMF staff on the creation of any such entities without delay.

4. Unless otherwise specified, state-owned or public enterprises refer to those entities that are principally engaged in the production of market goods or nonfinancial services and are owned or controlled, partially or fully, by the general government or units of the general government. For program monitoring purposes this definition will exclude the following entities: Addis Ababa and Regional Housing or other credit facilitators, and Ethiopian Airlines. The Liability and Asset Management Corporation (LAMC) will be treated as an extra-budgetary entity and not a state-owned enterprise. Existing extra budgetary funds excluded from the general government include the Fuel Price Stabilization Fund, Public Servants Social Security and Pension Fund, and the Road Maintenance Fund.

B. Program Exchange Rates

5. **Program exchange rates.** Reserve assets and liabilities will be converted into U.S. dollar terms at exchange rates and the gold price in effect on May 31, 2024, as follows:

Original Currency (1 unit, unless otherwise specified)	**Value in US$** (unless otherwise specified)
Special Drawing Right (SDR)/ African Development Bank Unit of Account	0.7543
Euro	1.0823
Japanese yen (per USD)	151.38
Pound sterling	1.2638
Chinese yuan (per USD)	7.2065
Canadian dollar (per USD)	1.3581
Norwegian krone (per USD)	10.7336
Swedish krona (per USD)	10.53543
UAE diram (per USD)	3.6725
South African rand (per USD)	18.9907
Gold (1 troy ounce)	2,164.400

Assets and liabilities denominated in other currencies will be evaluated based on their respective exchange rates with the U.S. dollar on May 31, 2024 as published in the IMF's *International Financial Statistics (IFS)*. For the purpose of evaluating inflows of foreign grants and budget support loans and other direct financing of the general government, the program exchange rate used will be **1 U.S dollar = Birr 57.0504**, which is the rate prevailing on May 31, 2024.

C. Quantitative Performance Criteria (QPC) and Indicative Targets (IT)

6. **Test Dates** for evaluating performance against performance criteria (PC) for the first, second and third reviews under the arrangements are August 16, 2024, September 30, 2024, and December 31, 2024, except for the continuous PCs, which remain effective continuously throughout the term of the Fund-supported program. Program reviews usually take place in between two test dates. The continuous PCs remain effective even during delays in reviews.

7. **The quantitative performance criteria listed below are those specified in Table 1 of the MEFP.** Definitions and adjusters (to account for factors or changes beyond the control of the government) for each criterion are specified in the subsequent sections. The quantitative performance criteria targets monitored and evaluated under the program are defined as ceilings or floors set on cumulative changes between June 30 immediately prior to the test date in question and the specified test date itself, unless otherwise indicated. The quantitative performance criteria are set as follows in paragraphs 8–12.

8. **Periodic PCs** that are evaluated as of each test date:

- Net financing of the general government primary balance (ceiling, cumulative change), (Section D).
- Net international reserves of the NBE (floor, cumulative change), (Section E).
- Net claims on the general government by the NBE (ceiling, cumulative change), (Section F).

- Tax revenue collected by the federal government (floor, cumulative change), (Section G).

To facilitate program monitoring, indicative targets for the periodic PCs described above will be set for March 31, 2025.

9. Continuous PCs that are evaluated on a continuous basis starting from program approval:

- Contracting of external non-concessional borrowing by the government (as defined in paragraph 2) and provision of government guarantees on external non-concessional borrowing (zero ceiling), (Section H).
- Accumulation of external payment arrears by the government (zero ceiling), (Section I).

10. The following continuous conditionality will also apply:

- Non-imposition or intensification of restrictions on the making of payments and transfers for current international transactions;
- Non-introduction or modification of multiple currency practice;
- Prohibition of entering into bilateral payments agreements that are inconsistent with Article VIII of the Fund's Articles of Agreement; and
- Non-imposition or intensification of import restrictions for balance of payments reasons.

11. Periodic indicative targets evaluated as of July 31, 2024, September 30, 2024, December 31, 2024, March 31, 2025, and June 30, 2025 (with certain exceptions described below) are:

- Claims on public enterprises by commercial banks (ceiling, cumulative change), (Section J).
- Government Contributions to Productive Safety Net Programs (floor, cumulative change, evaluated at the end of Ethiopian calendar month immediately after the test/evaluation dates listed above), (Section K).
- The present value of new external concessional borrowing contracted or guaranteed by the government, as defined in paragraph 2 (ceiling for the fiscal year ending June), (Section L).

12. Continuous indicative targets evaluated on a continuous basis during a fiscal year, starting from program approval are:

- The amount of net foreign exchange sales by the NBE (Section M).

D. QPC on Net financing of the General Government primary balance

Definitions

13. The net financing of the general government cash deficit, including grants and the operations of sub-national (state and woreda) governments financed from local funds, will be monitored quarterly. Net financing will be measured below the line and will include:

- **Net external financing of the general government,** excluding valuation gains and losses and changes to on-lending to public enterprises. This will be based on data prepared for the debt bulletin by the debt management directorate at the Ministry of Finance (MOF), including relief received from debt operations.
- **Change in net domestic credit of the banking system to the general government** is defined as the change in outstanding claims of the banking system on the general government. The calculation of net domestic credit of the banking system will be based on monetary survey data compiled by the NBE and will include: (i) net claims on the general government by the NBE (see below for definition), (ii) loans and advances from commercial banks to the general government, and (iii) holdings of government securities (including bonds, notes, and Treasury bills), less (i) local currency deposits of the central and state and local governments at the NBE and commercial banks, (ii) foreign currency deposits of the central government at the NBE. The definition will exclude valuation gains and losses from government deposits denominated in foreign currency. As with net external financing, on-lending from domestic banks through the general government to public enterprises (if any) should also be excluded. For program monitoring purposes, any bonds issued by states or regional housing agencies for housing projects where the debt obligations will be transferred to the private owners of the housing units shall be excluded.
- **Change in the net domestic nonbank financing to the general government**. These include (i) privatization receipts transferred from the privatization accounts to the budget, (ii) the change in the stock of outstanding government securities held by nonbank financial institutions (including pension funds, insurance companies), net of valuation changes, (iii) change in net credit from the domestic nonfinancial sector (including extra-budgetary funds classified outside the general government) to the general government minus (i) change in government financial assets with nonbank financial institutions, (ii) change in financial assets (either in the form of additional equity or loans) owned by the government with public enterprises as the counterparty (as a result of capital injections), and (iii) net flow from the general government to LAMC.

14. Net financing of the general government primary balance (including grants) is defined as the net financing of the general government cash deficit minus the consolidated interest bill of the federal and regional government budgets (general government is defined in paragraph 3 and the general government cash deficit in paragraph 13 of this memorandum).

15. Total external grants to the federal and regional governments are defined as the sum of project grants, cash external grants for budgetary support, capital grants reflecting the principal amounts of external debt cancellation or swaps, and other grants.

Adjustment Factor

16. The ceiling on the net financing of the general government primary balance (including grants) will be adjusted relative to the baseline projections:

- Upward by the amount of cumulative shortfall in external grants relative to the baseline projection up to US$200 million at actual exchange rates.
- Upward by the cumulative excess in external project financing relative to the program projections evaluated in Birr terms at actual exchange rates. External project financing is defined as disbursements from bilateral and multilateral creditors to the general government for specific project expenditure.
- Upward by cumulative excess in the programmed privatization receipts transferred from the privatization accounts to the budget from privatization to non-resident investors.
- Downward by the full amount of any increase in the stock of budgetary arrears on social payments such as wages, pensions, social benefits accumulated since the beginning of the fiscal year.

E. QPC on Net international reserves of the NBE

Definitions

17. Net international reserves (NIR) of the NBE, are defined as reserve assets of the NBE (i.e., the external assets that are readily available to, and controlled by, the NBE, as per the 6th edition of the IMF *Balance of Payments Manual*), minus the NBE's short term foreign exchange liabilities to residents and nonresidents, and Fund credit outstanding, including any use of it as budget support. Short-term liabilities refer to those that can be called immediately (e.g., FX demand deposits of banks, the general government, LAMC, public enterprises or the private sector) or have residual maturity of less than 1 year, including deposits, commitments to sell foreign exchange arising from derivatives (such as futures, forwards, swaps, and options) and other arrangements. The performance criterion will be evaluated as the cumulative change in NIR between June 30 immediately prior to the test date in question and the specified test date itself (see Section O).

Adjustment Factor

18. The floor on cumulative change in NIR will be adjusted:

i. Upward or downward for any deviation in the expected cumulative inflows of official grants and loans disbursed to the government from official development partners in foreign currency from the beginning of the fiscal year. The projected inflows of official grants and loans to the government are set out in the macroeconomic framework underpinning the program.

ii. Upward or downward for any deviation in the programmed inflows from privatization to non-resident investors (see definition in Section N).

19. The total downward adjustment to the floor on cumulative change in NIR target for FY2024/25 is capped at US$300 million. The total upward adjustment to the floor on cumulative change in NIR target for FY2024/25 is capped at US$150 million.

F. QPC on Net Claims on the General Government by the NBE

20. Net claims on the general government by the NBE is defined as the stock of claims of the NBE on the general government, net of general government deposits with the NBE.

G. QPC on Tax Revenues Collected by the Federal Government

Definition

21. Tax Revenues Collected by the Federal Government. Total tax revenues collected are defined as the sum of revenues collected by the Ministry of Revenues from any of the following:

(i) duties, taxes, and other charges on international trade;
(ii) personal income tax of federal government employees (including on employment income, royalty income, dividends, interest, capital gains);
(iii) profit (including repatriated profits) tax and sales (including value-added tax, and excises) taxes from enterprises assigned to the federal government (including sole proprietors subject to the turnover tax);
(iv) taxes on gains from lotteries and gambling;
(v) taxes from air, rail, and marine transport;
(vi) taxes from rent of property assigned to the federal government;
(vii) taxes and fees on licenses and federal services;
(viii) stamp duties;
(ix) personal income tax of staff of enterprises jointly assigned to the federal and regional governments;
(x) profit tax, royalties, and rent from large scale mining, petroleum, and gas incorporated enterprises;
(xi) any other excises not covered by the list thus far;
(xii) all revenue assignments under the concurrent taxation powers of the federal and regional governments – namely, corporate income tax and dividend withholding tax on companies, profit and sales tax on enterprises jointly assigned to the federal and regional governments;
(xiii) unclassified tax revenues minus corresponding refunds.

22. To the extent that revenue assignments change after the date of this Memorandum, and the federal government is entitled to levy and collect any other instruments not covered by the list above, revenue from such instruments should also be included from that moment. That may include taxes on private movable and immovable property and land use, as well as agricultural income tax and personal income tax of private employees. Total tax revenue collection will be defined, for each test date, as the cumulative sum of tax revenues collected since the beginning of the fiscal year. Note that any end of the month targets for this series refer to end of the respective Ethiopian calendar month, which typically ends on the 7th or 8th of the following Gregorian calendar month.

H. PC on Contracting of External Non-concessional Debt by the Government and Provision of Government Guarantees on External Non-Concessional Debt

Definition

23. For program purposes, the definition of debt is set out in paragraph 8(a) of the Guidelines on Public Debt Conditionality in Fund Arrangements, attached to IMF Executive Board Decision No. 16919(20/103) adopted on October 28, 2020.[1]

"For the purposes of these guidelines, the term "debt" is understood to mean a current (i.e., noncontingent) liability created by a contractual arrangement whereby a value is provided in the form of assets (including currency) or services, and under which the obligor undertakes to make one or more payments in the form of assets (including currency) or services at a future time, in accordance with a given schedule; these payments will discharge the obligor from its contracted principal and interest liabilities. Debt may take several forms, the primary ones being as follows:

i. *Loans, that is, advances of money to the borrower by the lender on the basis of an undertaking that the borrower will repay the funds in the future (including deposits, bonds, debentures, commercial loans, and buyers' credits), as well as temporary swaps of assets that are equivalent to fully collateralized loans, under which the borrower is required to repay the funds, and often pays interest, by repurchasing the collateral from the buyer in the future (repurchase agreements and official swap arrangements);*
ii. *Suppliers' credits, that is, contracts under which the supplier allows the borrower to defer payments until sometime after the date when the pertinent goods are delivered, or the services are provided; and*
iii. *Leases, that is, agreements governing the provision of property that the lessee has the right to use for one or more specified period(s), generally shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purposes of the guidelines, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement, apart from payments related to the operation, repair, or maintenance of the property."*

According to the above-mentioned definition, debt includes arrears, penalties, and damages awarded by the courts in the event of a default on a contractual payment obligation that represents a debt. Failure to make payment on an obligation that is not considered a debt according to this definition (e.g., payment on delivery) does not give rise to a debt.

24. External debt, in the assessment of the relevant criteria, is defined as any borrowing from nonresidents. The relevant performance criteria are applicable to external debt contracted or guaranteed by the government, or to any private debt for which the government has provided a

[1] IMF Policy Paper, Reform of the Policy on Public Debt Limits in IMF-Supported Programs—Proposed Decision and Proposed New Guidelines, November 2020.

guarantee. Guaranteed debt refers to any explicit legal obligation for the government to repay a debt in the event of default by the debtor (whether payments are to be made in cash or in kind). Public sector external debt includes foreign-currency denominated obligations of NBE contracted on behalf of the national government (excluding newly contracted financing from the IMF and the General SDR allocation). Deposits made at NBE by foreign partners that have been used to support the BOP and are categorized as debt, in line with the treatment of similar deposits in the past. For program purposes, this definition of external debt does not include routine commercial debt related to import operations and maturing in less than a year.

25. Medium- and long-term external debt refers to external debt originally maturing in one year or more. **Short-term external debt** refers to external debt originally maturing in less than one year.

26. For program purposes, a debt is deemed concessional if it contains a grant element representing at least 35 percent. The grant element is the difference between the present value (PV) of the loan and its face value, expressed as a percentage of the loan's face value. The PV of a loan at the time of its signing date is calculated by discounting future principal and interest payments, based on the unified discount rate of 5 percent set forth in Executive Board Decision No. 15248-(13/97). Concessionality will be assessed based on all aspects of the loan agreement, including maturity, grace period, repayment schedule, front-end fees, and management fees. The calculation is performed by the authorities, using the IMF model,[2] and verified by IMF staff based on data provided by the authorities. For loans with a grant component of zero or less, the PV is set at an amount equal to the face value. In cases where a combination of financing instruments is involved, staff will need to assess, with support of necessary documentation provided by the authorities, if such a combination can be treated as a financing package for the purpose of determining if it is concessional under the Fund-supported program. To the extent a financing package is found to be concessional, the combined nominal amounts of the underlying instruments will be counted toward any debt limits on concessional debt.

27. In the case of debt with a variable interest rate represented by a reference interest rate plus a fixed margin, the grant element of the debt will be calculated on the basis of a program reference rate plus a fixed margin (in basis points) specified in the loan agreement. The program reference rate for variable interest rates will be based on the 10-year average projections made in the Fall or Spring edition, whichever is the latest, of the Fund's *World Economic Outlook* (WEO) until modified. Based on the April 2024 WEO projections, the program reference rate for these currencies, until modified, are shown below on a calendar year basis, using their averages over 2023–32. To convert to Ethiopian fiscal year, a simple average of two successive calendar years will be used (e.g., for 2022/23, simple average of 2022 and 2023 will be used). Where the variable rate is linked to a benchmark interest rate other than the six-month USD Secured Overnight Financing Rate (SOFR), a spread reflecting the difference between the benchmark rate and the six-month USD SOFR (rounded to the nearest 50 bps) will be added.

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[2] http://www.imf.org/external/np/spr/2015/conc/index.htm.

The Federal Democratic Republic of Ethiopia: Assumptions for Variable Interest Rate Set Limits		
	10-year average six-month Secured Overnight Financing Rate (SOFR), in percent	Spread (rate in currency noted minus US$, in percent
U.S. dollars	3.688	0.0
Euro	2.803	-1.0
Pound sterling	4.056	0.5
Other	3.316	-0.5

28. External debt is deemed to have been contracted or guaranteed on the date of signing a loan contract by authorized signatories of the government (as defined in paragraph 2). Contracting of credit lines with no predetermined disbursement schedules or with multiple disbursements will be also considered as contracting of debt. For program purposes, external debt denominated in currencies other than the U.S. dollar will be converted to U.S. dollars on the basis of the exchange rate as of the assessment date. Such conversions to U.S. dollars will be undertaken by the government and communicated to IMF staff.

29. The performance criterion (ceiling) applies to the nominal value of new non-concessional external debt and the nominal value of new concessional external debt, contracted or guaranteed by the government. The ceiling applies to debt and commitments contracted or guaranteed for which value has not yet been received, including private debt for which official guarantees have been extended. An exception is applied for new non-concessional external debt contracted or guaranteed by the general government for the Koysha dam project, which is capped at US$950 million over the duration of the program. Operations that resolve pre-HIPC arrears and result in reduction in outstanding stock of debt are excluded from the ceiling. Court or arbitral decisions and related debt operations with respect to government guarantees on existing external debt in dispute as of end-June 2024, that result in more favorable terms to the guarantor than those of the initial debt, will be excluded from the ceiling. Debt operations that restructure existing loans and that result in a reduction of the present value (present value savings) compared with the initial debt and/or an improvement of the overall public external debt service profile will be excluded from the ceiling. In the calculation of the present value savings for these debt operations, the discounted future stream of payments of debt service due on the newly issued debt instrument (including all costs associated with the operation) will be compared with the discounted future stream of debt service due on the instrument it replaces using a discount rate of 5 percent and these amounts will not be capped by the nominal value of the debt.

I. Continuous PC on Accumulation of External Payment Arrears by the Government

30. External payment arrears are defined as payments (principal and interest) on external debt contracted or guaranteed by the government that are overdue (considering any contractually

agreed grace periods). For the purposes of the program, the government undertake not to accumulate any new external payments arrears on their debt. The definition excludes arrears relating to debt subject to renegotiation (dispute or ongoing renegotiation). The performance criterion on the public and publicly-guaranteed external debt arrears is defined as a cumulative flow in gross terms from the date of program approval and applies on a continuous basis.

J. IT on Claims on Public Enterprises by Commercial Banks

31. Claims on public enterprises by commercial banks are defined as the stock of claims on public enterprises (as defined in paragraph 4 of this memorandum) by commercial banks. Claims on public enterprises by commercial banks shall consist of all domestic commercial bank claims on public enterprises, including loans, bonds, and other liabilities issued by public enterprises.

K. IT on Government Contributions to Productive Safety Net Programs

32. Government Contributions to Productive Safety Net Programs (PSNP) are defined as general government cash contributions to the rural and urban Productive Safety Net Programs. The IT will be measured using total government contributions to disbursements for both programs from Channel 1 and Channel 2 directorates in the MOF. End-of-month targets for this IT refer to end of the respective Ethiopian calendar month, which typically ends on the 7th or 8th of the following Gregorian calendar month.

L. IT on Present Value of New External Debt Contracted or Guaranteed by the Government

33. An indicative target (ceiling) applies to the PV of new external debt contracted or guaranteed by the government, as defined in section H. The ceiling applies also to debt contracted or guaranteed for which value has not yet been received. The ceiling is set in alignment with the external borrowing plan (prepared as per the template below). Operations that resolve arrears to pre-HIPC countries and result in reduction in outstanding stock of debt are excluded from the ceiling. Court or arbitral decisions and related debt operations with respect to government guarantees on existing external debt in dispute as of end-June 2024, that result in more favorable terms to the guarantor than those of the initial debt, will be excluded from the ceiling. Debt operations that restructure existing loans and that result in a reduction of the present value (present value savings) compared with the initial debt and/or an improvement of the overall public external debt service profile will be excluded from the ceiling. In the calculation of the present value savings for these debt operations, the discounted future stream of payments of debt service due on the newly issued debt instrument (including all costs associated with the operation) will be compared with the discounted future stream of debt service due on the instrument it replaces using a discount rate of 5 percent and these amounts will not be capped by the nominal value of the debt.

The Federal Democratic Republic of Ethiopia: External Borrowing Plan for 2024/25

(Programmed Contracted Debt)

PPG external debt	Volume of new debt in 2024/25		PV of new debt in 2024/25 (program purposes)	
	USD million 1/	Percent	USD million 1/	Percent
By sources of debt financing	**4,900**	**100**	**2,856**	**100**
Concessional debt, of which 2/	**3,950**	**81**	**1,906**	**67**
Multilateral debt	3,600	73	1,683	59
Bilateral debt	350	7	224	8
Non-concessional debt, of which 2/	**950**	**19**	**950**	**33**
Semi-concessional 3/	-	-	-	-
Commercial terms 4/	950	19	950	33

1/ Contracting and guaranteeing of new debt. The present value of debt is calculated using the terms of individual loans and applying the 5 percent program discount rate

2/ Debt with a grant element that exceeds a minimum threshold. This minimum is typically 35 percent, but could be established at a higher level.

3/ Debt with a positive grant element which does not meet the minimum grant element.

4/ Debt without a positive grant element. For commercial debt, the present value would be defined as the nominal/face value.

M. Foreign Exchange Intervention (FXI) Framework (ITs)

34. The FXI rule allows but does not oblige, the NBE to intervene. FXI will be conducted via auction that satisfies the following criteria: (i) access to bid at the auction is granted to all authorized dealers in good standing, in the wholesale FX market, to sell or make purchases of FX for themselves and on behalf of their clients; (ii) there should be no constraints imposed on the range or level of the exchange rates that bidders can submit; (iii) allotment at the auction should be determined solely on the basis of the bid prices submitted by participants to buy or sell FX.

N. Other Definitions

35. Privatization shall be understood to mean both the disposal to private owners by a government unit of equity, controlling or otherwise, in a public corporation or quasi-corporation (transaction in equity), and the disposal of intangible non-produced assets in the form of contracts, leases, and licenses, where a government unit grants a license for the economic ownership of an asset by allowing the licensee to use a natural resource (such as telecommunications spectrum) for an extended period, with little or no intervention.

36. For the purposes of monitoring structural benchmarks, the following definitions will be used:

- **Tax expenditure** is understood as any benefit under the tax code that deviates from the benchmark treatment of the code and whose benefit to the relevant taxpayers could be alternatively affected through government spending (such as through the provision of subsidies or other transfers to the relevant taxpayers).

- **Revocation of tax incentives** currently granted on a contractual, rather than legislative basis, entails grandfathering of existing incentives until the term of the original benefit (the case of corporate income tax holidays, for example). The revocation will therefore inhibit at a first stage, the granting of new tax exemptions based on the definition of tax incentives provided above.
- **Subsidies are understood to include both explicit and implicit subsidies.** The former are defined as current unrequited transfers that government units make to enterprises on the basis of the level of their production activities or the quantities or values of the goods or services they produce, sell, export, or import. In turn, implicit subsidies can include, but need not be limited to an official system of multiple exchange rates, payable tax credits, and losses of government trading organizations whose function is to buy products and then sell them at lower prices to residents or nonresidents as a matter of deliberate government economic or social policy, the central bank accepting interest rates lower than the prevailing market rates. The complete definition is included in the Government Finance Statistics Manual 2014 (6.89 and 6.90).

O. Reporting Procedures to the IMF

37. Data on all the variables subject to quantitative performance criteria and indicative targets and information on the progress towards meeting structural benchmarks will be transmitted regularly to the IMF in accordance with the table shown below. Revisions to data will be forwarded to the IMF within 5 days after being made. In addition, the authorities will transmit to IMF staff any information or data not defined in this TMU but pertinent for assessing or monitoring performance relative to the program objectives.

38. To effectively monitor the program performance and development of economic situation, the Ethiopian authorities will provide the IMF with the information listed below:

Information	Provider	Periodicity and Due Date
Gross international reserves and foreign liabilities of the National Bank of Ethiopia (NBE), reported by the amounts in the original currency of the assets and liabilities; and the weight (in oz.) of holdings of monetary gold. Breakdown between liquid and unencumbered reserves and reserves that are pledged, swapped, or otherwise encumbered	NBE	Weekly, within five business days of end of each week
Net domestic assets of the NBE	NBE	Monthly within six weeks of the end of each month
Reserve Money	NBE	Monthly within six weeks of the end of each month
Net claims on the general government	MOF/NBE	Monthly within six weeks of the end of each month

Information	Provider	Periodicity and Due Date
Regional government's fiscal data	MOF	Quarterly within twelve weeks of the end of each month
Domestic Arrears incurred by the government	MOF	Monthly within six weeks of the end of each month
External Arrears incurred by the government	MOF/NBE	Continuously with no lag
Claims on public enterprises by commercial banks.	NBE/MOF	Monthly within six weeks of the end of each month
Claims on entities excluded as SOEs in paragraph 4 by commercial banks, including, but not limited to, Addis Ababa and Regional Housing and Liability and Asset Management Company.	NBE/MOF	Monthly within six weeks of the end of each month
Federal Government Tax Revenue	MOF	Monthly within 45 days of the end of each month
Rural and Urban Productive Safety Net Program government's cash contributions	MOF	Monthly within six weeks of the end of each month
Stock of claims of the Ethiopian Petroleum Supply Enterprise on the Fuel Price Stabilization Fund	MOF	Monthly within six weeks of the end of each month
Consumer Price Index	NBE	Monthly within six weeks of end of each month
National Accounts, annual	NDPC	Within three weeks of any revision or data release
Composite Indicator of Economic Activity (quarterly) and underlying indicators	NBE	Within six weeks of the end of each quarter
Consolidated Budget Report of Federal and Regional Government	MOF	Quarterly within twelve weeks of end of each quarter
Monetary Survey	NBE	Monthly within six weeks of end of each month
NBE's outstanding credit to private commercial banks, CBE and DBE	NBE	Monthly within two weeks of end of each month
Financial Soundness Indicators (aggregate and bank-by-bank), including capital to risk-weighted assets, capital to assets, NPLs to total loans, NPLs net of provisions to capital, return on assets, return on equity, gross interest income to total income, interest margin to gross income, non-interest expenses to gross income, liquid assets to total assets, and liquid assets to short term liabilities.	NBE	Quarterly, within eight weeks of the end of each quarter.
Lending and savings interest rates, interbank interest rates, term deposit rates.	NBE	Monthly, within 30 calendar days

Information	Provider	Periodicity and Due Date
Credit data on distribution by sector (private/public); credit to enterprises (by economic sector); and credit to individuals (by purpose).	NBE	Monthly, within 30 calendar days
Bank-by-bank financial data of commercial banks and the DBE, including balance sheets, income statements, net open foreign currency positions, NPLs and liquidity positions broken down by currency by template provided by the IMF	NBE	Quarterly, within eight weeks of the end of each quarter.
T-Bill and T-bond auction details	NBE	Bi-weekly, within five business days of each auction/placement
T-bill and T-bond purchases and outstanding stocks by institution.	NBE	Quarterly, within eight weeks of the end of each quarter.
Monetary policy operations and liquidity factors: weekly and monthly balances. Detailed table including: (1) intervention on the money market of the central bank (Birr); (2) deposit facilities; (3) ordinary tenders; (4) loan facility; (5) overnight lending; (6) all structural operations; (7) FX swap exchange; (8) open market operations; (9) minimum reserves; and (10) excess reserves (including by institution) (11) central bank policy rate; and (12) participation in open market operations by institution.	NBE	Monthly within 15 calendar days
Daily official exchange rate	NBE	Weekly, within five business days of end of each week
Daily foreign exchange intervention by the NBE: (i) US$ amount in purchases and sales of foreign exchange in spot and derivative transactions by counterparty, respectively; (ii) US$ amount in net sales of foreign exchange by the NBE in any 30-day rolling period; (iii) Daily cumulative net sales of foreign exchange by the NBE in a given quarter; (iv) Share of foreign exchange intervention by the NBE over total interbank market transactions: (v) Exchange rate at which the NBE buys or sells foreign exchange	NBE	Weekly, within five business days of end of each week
Weekly US$ amount of trade volume, in interbank market and foreign exchange bureaus, respectively	NBE	Weekly, within five business days of end of each week
Daily data underlying the FX benchmark calculation	NBE	Weekly, within five business days of end of each week
Interbank market transactions in the spot market for US dollars: total value transacted in US$, total number of transactions, number of banks involved in transactions, average value transacted in US$	NBE	Weekly, within five business days of end of each week
Gross international reserves	NBE	Weekly, within five business days of end of each week

Information	Provider	Periodicity and Due Date
Foreign exchange cash flows	NBE	Monthly, within ten business days of end of each month
BoP data: exports, imports, services, transfers, and capital and financial account transactions	NBE	Monthly, within six weeks of end of each month
Detailed international trade data on goods exports and imports by commodities	NBE	Monthly, within four weeks of end of each month
Imports by type of institutions (e.g., state-owned enterprises or government, and private sector)	NBE	Monthly, within four weeks of end of each month
New external debt obligations contracted and/or guaranteed (concessional and non-concessional) by the government of Ethiopia, including details on the amounts, terms, and conditions of each new obligation	MOF/NBE	Monthly, within four weeks of end of each month with details of the loans contracted (creditor, terms, projects, estimated grants element, and users—Federal government's direct use or other purposes etc.)
Outstanding stock of external debt, disbursements/issuance to the government (for Federal government, breakdown to include the amounts for on-lending to public enterprises), and debt service, by debtors, creditors, and type of debt	MOF/NBE	Monthly, within six weeks of end of each month
Disbursements of loans and grants to Federal government by each creditor/donor with breakdown into cash and non-cash components	MOF	Monthly, within six weeks of end of each month
Outstanding stock of domestic debt, disbursements/issuance, and debt service, by debtors, creditors, and type of debt	MOF/NBE	Monthly, within six weeks of end of each month
Public Enterprise Financial Statements (those under PEHAA and EIH)	MOF	Annually, end September.

INTERNATIONAL MONETARY FUND

THE FEDERAL DEMOCRATIC REPUBLIC OF ETHIOPIA

REQUEST FOR AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—DEBT SUSTAINABILITY ANALYSIS

July 12, 2024

Approved By
Hassan Zaman and Manuela Francisco (IDA) and Annalisa Fedelino (IMF)

The Debt Sustainability Analysis (DSA) was prepared by the staffs of the International Monetary Fund (IMF) and the International Development Association (IDA), in consultation with the authorities.

The Federal Democratic Republic of Ethiopia: Joint Bank—Fund Debt Sustainability Analysis[1]	
Risk of external debt distress	*In debt distress*
Risk of overall debt distress	*In debt distress*
Granularity in the risk rating	*Unsustainable*
Application of judgement	*No*

Ethiopia faces political, economic, and humanitarian challenges. Support from the international community weakened notably during the two-year conflict in Tigray but is now resuming. Bunching of debt service in the near to medium term and adverse developments have led to the realization of debt repayment risks.

Ethiopia's debt is assessed to be unsustainable, mainly due to protracted breaches of exports-related external debt indicators. Following a missed Eurobond interest payment in December 2023, the country is in debt distress. Debt carrying capacity (DCC) was downgraded to "weak" in October 2022.[2] Timely implementation of the authorities' reform agenda and debt relief from external creditors are required to alleviate liquidity pressures and restore debt sustainability. The authorities have committed to achieving a moderate risk of debt distress rating by the end of the proposed ECF arrangement. An Official Creditor Committee under the G20 Common Framework was formed in September 2021, and agreed to suspend debt service due in 2023 and 2024 on November 9, 2023. Creditors reiterated their commitment to providing a debt treatment as part of an IMF-supported program.

[1] This preliminary analysis is based on the Joint Bank-Fund Debt Sustainability Framework for Low-Income Countries (LIC-DSF) that was approved in 2017.

[2] The downgrade to "weak" followed two successive weak signals in April and October 2022. The composite indicator, based on the April 2024 World Economic Outlook (WEO) and 2022 World Bank Country Policy and Institutional Assessment (CPIA) data that was published in July 2023, is currently estimated at 2.31, which indicates a weak DCC.

A. Public Debt Coverage

1. Debt coverage under this Debt Sustainability Analysis (DSA) is consistent with the LIC–DSF guidance and previous DSAs.[3] In particular, the DSA includes Federal government debt, the central bank's debt to the IMF and two bilateral creditors, guaranteed nonfinancial public enterprises' debt, and non-guaranteed debt of Ethio-Telecom, a major telecommunication company.[4] External debt is defined according to the residency principle. Notwithstanding the comprehensive coverage, staff assumes a larger contingent liability shock of 4.5 percent of GDP than the default level of 2 percent of GDP, to account for additional risks associated with large state-owned enterprises (SOEs). Financial market shock is assumed at 5 percent of GDP, the default level.

Text Table 1. The Federal Democratic Republic of Ethiopia: Coverage of Public and Publicly Guaranteed Debt and Parameters of Contingent Liability Shocks for the Tailored Stress Test

	Public debt coverage	Sub-sectors covered
1	Central government	X
2	State and local government	X
3	Other elements in the general government	
4	o/w: Social security fund	
5	o/w: Extra budgetary funds (EBFs)	
6	Guarantees (to other entities in the public and private sector, including to SOEs)	X
7	Central bank (borrowed on behalf of the government)	X
8	Non-guaranteed SOE debt	X

1	The country's coverage of public debt	The central, state, and local governments, central bank, government-guaranteed debt, non-guaranteed SOE debt		
		Default	Used for the analysis	Reasons for deviations from the default settings
2	Other elements of the general government not captured in 1.	0 percent of GDP	0.0	None
3	SoE's debt (guaranteed and not guaranteed by the government) 1/	2 percent of GDP	4.5	Potential liabilities, including from a policy bank and claims by Koysha contractor
4	PPP	0 percent of PPP stock	0.0	None
5	Financial market (the default value of 5 percent of GDP is the minimum value)	5 percent of GDP	5.0	None
	Total (2+3+4+5) (in percent of GDP)		9.5	

1/ The default shock of 2% of GDP will be triggered for countries whose government-guaranteed debt is not fully captured under the country's public debt definition (1.). If it is already included in the government debt (1.) and risks associated with SoE's debt not guaranteed by the government is assessed to be negligible, a country team may reduce this to 0%.

2. The coverage of debt statistics is comprehensive. The authorities publish domestic and external debt statistics of the Federal government and SOEs on a quarterly basis.[5] Debt reporting continues to improve under the World Bank's Growth and Competitiveness Programmatic Development Policy

[3] The coverage differs from the official public debt data in two aspects: the DSA does not include Ethiopian Airlines but includes the deposits of two bilateral creditors at the central bank, as these deposits have the economic characteristics of debt (interest rate and a regular debt-service schedule until maturity, and that a public entity is responsible for servicing these debts) and meeting balance of payment needs.

[4] Ethiopian Airlines and Ethio Telecom are the only state-owned enterprises with non-guaranteed debt. Ethio Telecom's debt service payments are added to revenue as a proxy for the company's net income in the calculation of external debt service to revenue ratio as total operating profit is larger than the debt payments. The inclusion of Ethio Telecom debt service is a conservative estimate of its larger operating profit.

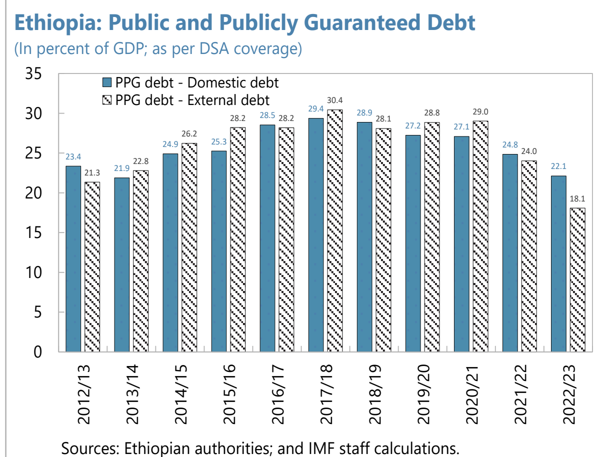
[5] Debt bulletins are available on the Ministry of Finance website (https://www.mofed.gov.et/resources/bulletin/).

Operation series, with expanded coverage of SOE domestic debt in the quarterly debt reports and the publication of an annual debt report.[6]

B. Background

3. Ethiopia's total public and publicly guaranteed debt as a share of GDP declined by about 9 percentage points in 2022/23. Total public and publicly guaranteed (PPG) debt stood at 40 percent of GDP at end-June 2023, down from 49 percent of GDP a year before. This decline mainly reflected low external disbursements combined with high nominal GDP growth, with the external debt-to-GDP ratio declining by about 6 percentage points. The domestic debt-to-GDP ratio also declined, rising less than nominal GDP. Debt owed by the Federal government and the central bank accounted for 79 and 4 percent of the total PPG debt stock, respectively, with the remainder owed by SOEs (17percent).

Ethiopia: Public and Publicly Guaranteed Debt
(In percent of GDP; as per DSA coverage)

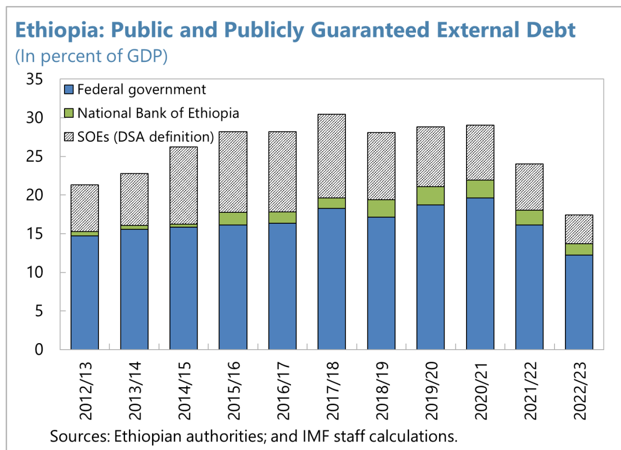


Sources: Ethiopian authorities; and IMF staff calculations.

External Debt

4. External debt accounted for 45 percent of total PPG debt as of end-June 2023. In 2022/23, PPG external debt amounted to 18 percent of GDP, down from 24 percent of GDP a year before. The decline reflected lower disbursements to the Federal government, as official bilateral and market external creditors have mostly halted disbursements in response to Ethiopia's application for a debt treatment under the G20 Common Framework (CF). The Federal government accounts for about 70 percent of total external debt, predominantly to the World Bank and other official creditors. For the SOEs included in the DSA, the PPG external debt ratio fell for the fifth successive year. This decline is due largely to active measures taken by the authorities to contain SOEs' external borrowing, including no new contracting of non-concessional external debt, consistent both with the International Development Association's Sustainable Development Financing Policy and a continuous performance criterion under the 2019 ECF-EFF program.

Ethiopia: Public and Publicly Guaranteed External Debt
(In percent of GDP)



Sources: Ethiopian authorities; and IMF staff calculations.

[6] Further information about the transparency of Ethiopia's debt reporting practices, including changes over time, can be found on the World Bank's Debt Reporting Heatmap (https://www.worldbank.org/en/topic/debt/brief/debt-transparency-report).

Text Table 2. The Federal Democratic Republic of Ethiopia: Public and Publicly Guaranteed Debt Profile

	Debt stock 1/ (as of end-June 2023)			Debt Service 2/					
				2023/24	2024/25	2025/26	2023/24	2024/25	2025/26
	In US$ million	In percent of total	In percent of GDP	In US$ million			In percent of GDP		
Total	**64,274**	**100.0**	**40.2**	**8,211**	**7,502**	**5,103**	**3.9**	**5.5**	**3.5**
o/w Federal government	50,404	78.4	31.5	7,990	6,480	3,562	3.8	4.8	2.5
External	**28,930**	**45.0**	**18.1**	**920**	**2,557**	**1,916**	**0.4**	**1.2**	**0.9**
International financial institutions	15,269	23.8	9.6	650	694	553	0.3	0.3	0.3
IMF	709	1.1	0.4	230	232	60	0.1	0.1	0.0
World Bank	11,589	18.0	7.3	331	363	387	0.2	0.2	0.2
AfDB/AfDF	2,198	3.4	1.4	52	55	58	0.0	0.0	0.0
Others	773	1.2	0.5	37	44	48	0.0	0.0	0.0
o/w IFAD	410	0.6	0.3	13	14	16	0.0	0.0	0.0
Bilateral official creditors 3/ 4/	12,406	19.3	7.8	115	761	1,315	0.1	0.4	0.6
Paris Club	1,853	2.9	1.2	21	109	168	0.0	0.1	0.1
o/w Italy	510	0.8	0.3	20	53	75	0.0	0.0	0.0
o/w Korea	335	0.5	0.2	0	0	0	0.0	0.0	0.0
Non-Paris Club	10,553	16.4	6.6	94	653	1,147	0.0	0.3	0.5
o/w China	7,421	11.5	4.6	93	588	1,023	0.0	0.3	0.5
o/w Saudi Arabia	1,099	1.7	0.7	0	48	95	0.0	0.0	0.0
Bonds	1,033	1.6	0.6	33	1,066	0	0.0	0.5	0.0
Commercial creditors 4/ 5/	222	0.3	0.1	122	68	37	0.1	0.0	0.0
Domestic	**35,343**	**55.0**	**22.1**	**7,291**	**4,945**	**3,188**	**3.5**	**3.6**	**2.2**
Held by residents, total	35,343	55.0	22.1	7,291	4,945	3,188	3.5	3.6	2.2
T-bills 6/	6,262	9.7	3.9	...			...	...	
Commercial banks	2,698	4.2	1.7	...			...	...	
Non-bank financial institutions	3,564	5.5	2.2	...			...	...	
Bonds 7/	12,453	19.4	7.8	...			...	...	
Central bank	7,949	12.4	5.0	...			...	...	
Loans	6,734	10.5	4.2	...			...	...	
Central bank direct advance	2,381	3.7	1.5	...			...	...	
Commercial banks	4,353	6.8	2.7	...			...	...	
Transferred to LAMC	9,894	15.4	6.2						
Held by nonresidents, total	0	0.0	0.0	...			...	...	
Memo Items:									
Collateralized debt 8/	0	...	...	...			...	...	
Contingent liabilities 9/	0	...	...	...			...	...	
Nominal GDP (US dollar, end of period)	159,766	...	...	...			...	...	

Sources: Ethiopian authorities; and IMF staff estimates and projections.
1/ Consistent with the DSA coverage and may differ from official debt statistics on external debt.
2/ Includes roll-over of T-bills and staff's estimate of standstill agreement with official bilateral creditors.
3/ Includes loans backed by export credit agencies.
4/ Includes pre-HIPC arrears waiting to receive HIPC comparable treatment.
5/ Loans from commercial banks and credit suppliers non-backed by ECAs
6/ Marketable T-bills issued under auctions since December 2019.
7/ Includes previously issued short-term debt (direct advance and T-bills) that were converted into bonds.
8/ No collateralized debt is reported.
9/ No significant contingent liabilities have been identified, with the debt perimeter comprehensive encompassing non-guaranteed SOEs debt.

- The bulk of external debt is debt to official creditors.[7] IDA and official non-Paris club creditors accounted for about 41.7 and 35.1 percent of PPG external debt, respectively. Non-official creditors accounted for 4.1 percent of PPG external debt, including a US$1 billion Eurobond maturing in December 2024 and SOE debt not backed by export credit agencies.

[7] Ethiopia has pre-HIPC arrears to Libya, Russia, and the former Yugoslavia, totaling about US$525 million as of end-June 2023, which are deemed away. . Furthermore, there are about US$15 million worth of external arrears to commercial creditors from the former Czechoslovakia, India, Italy, and the former Yugoslavia, all pre-dating the 1990s, which the authorities are also making good faith efforts to resolve.

- IDA financing provided positive net transfers of US$1.7 billion in 2022/23, from US$1.1 billion and US$1.2 billion in 2021/22 and 2020/21, respectively. Approved arrangements amounted to US$3.2 billion in 2023/24. Recent IDA support is project financing (see WB website).
- The IMF Executive Board approved a blended ECF–EFF arrangement of SDR 2.1049 billion (700 percent of quota)[8] in December 2019, of which Ethiopia drew down SDR 223.85 million. In addition, following the COVID-19 shock, emergency financing was provided through a Rapid Financing Instrument for SDR 300.7 million (100 percent of quota or 0.4 percent of GDP) in April 2020. Debt service relief of obligations under the Catastrophe Containment and Relief Trust was provided until April 13, 2022 (about SDR 14 million).
- Ethiopia also received debt service relief via the G20 Debt Service Suspension Initiative (DSSI), for about US$220 million over May 2020–June 2021. Ethiopia did not seek debt relief under the July–December 2021 phase of the DSSI.
- Principal repayments of bilateral deposits at the National Bank of Ethiopia (NBE) were reprofiled in 2020/21, for total relief during 2022/23–2025/26 estimated at US$1.3 billion. The authorities have confirmed that there is no collateralized debt outstanding.

5. The authorities requested debt treatment under the CF in February 2021 and the Official Creditor Committee (OCC) was formed in September 2021. The request was to strengthen debt sustainability and improve the risk of debt distress rating to moderate by the end of the 2019 ECF-EFF arrangements, consistent with the Fund's exceptional access criteria. This requirement will remain under the newly requested Fund-supported program. Eight OCC meetings have already taken place, with the last one held on April 3, 2024.

6. A standstill agreement was reached with official creditors in November 2023, suspending debt service due in 2023 and 2024. The debt service suspension is retroactive to January 1, 2023, and therefore resolves US$1.2 billion of official arrears that had accumulated (US$1.1 billion to China) earlier in 2023. The debt service suspension agreement includes a claw-back provision, allowing the OCC to restore the original debt service obligation schedule if staff level agreement on a new IMF-supported program is not reached by end-June 2024 (extended by the OCC from end-March 2024). Ethiopia defaulted on its Eurobond obligations by missing a coupon payment of US$33 million in December 2023. The authorities have begun restructuring negotiations with bondholders.

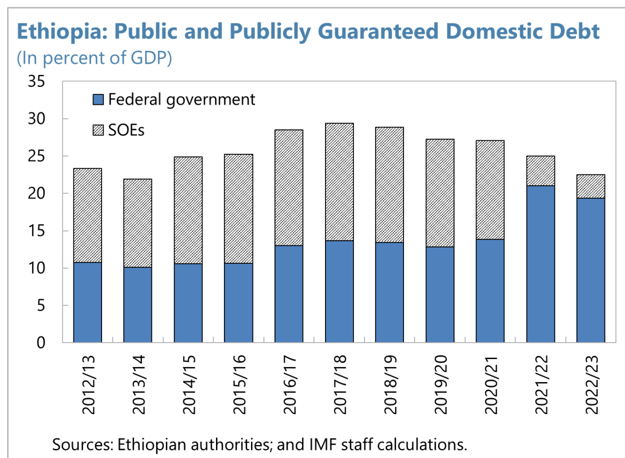
Domestic Debt

7. The domestic debt to GDP ratio has declined and stood at 22 percent of GDP at end-June 2023. With SOE debt transferred to the Liability and Asset Management Corporation (LAMC) now classified as government debt (6.3 percent of GDP at end-June 2023), the Federal government accounted for about

[8] Total access under the 2019 ECF-EFF arrangements were modified to 650 percent of quota via a reduction in the EFF access at the time of the Rapid Financing Instrument approval in April 2020 to comply with applicable policies on annual access limits. At the time of program approval in December 2019, PRGT access was subject to a hard cap of 300 percent of quota (which was removed in July 2021), hence the need for blending with GRA resources.

87 percent of the total domestic debt. Meanwhile SOE domestic debt fell from 13 to 3 percent of GDP in the two years to end-June 2023.

- ***Around 38 percent of the Federal government's domestic debt is legacy debt issued at well below market rates,*** including a long-term bond resulting from the conversion of past direct advances from the NBE, and debt issued for purposes of bank recapitalization. With scarce external financing, the government continued to rely mainly on domestic borrowing in 2022/23 through direct advances from the NBE and issuance of Treasury bills (T-bills).



- ***Treasury bill auctions began in December 2019 at the time of the approval of the ECF-EFF arrangements.*** As of end-June 2023, the stock of T-bills stood at 4.0 percent of GDP down from 5.2 percent of GDP at end-June 2022. The weighted average yield, though still negative in real terms, has gone up (8–11 percent in 2022/23 from 1–2 percent offered on non-market instruments in the past). The stock of advances from the NBE decreased to 1.5 percent of GDP at end-June 2023 from 2.6 percent of GDP at end-June 2022, following partial conversion into long-term bonds in October 2022, including the flow of new advances over the year. The authorities reintroduced some financial repression measures, including mandatory commercial bank purchases of bonds issued by the Development Bank of Ethiopia (August 2021) and of non-marketable 5-year government bonds (November 2022).

- ***Domestic SOE debt is highly concentrated.*** The Commercial Bank of Ethiopia (CBE), a large public sector bank, holds virtually all SOE domestic debt including debt that was transferred to LAMC. More than 90 percent of this debt is owed by three troubled SOEs that have not regularly serviced their loans, which are publicly guaranteed. These loans have been systematically renewed and guarantees have not been made effective.

- ***The authorities have established LAMC to manage the SOEs' debt burden.*** In August 2021, SOE domestic debt of nearly ETB 400 billion (9.4 percent of GDP) was transferred to LAMC, classified by staff as an extra-budgetary government agency, which in turn made repayments to the CBE using the local currency proceeds from the first telecom license auction held in late fiscal year 2020/21 (US$850 million). Debt transferred to LAMC is treated as government debt. Even with the repayments made by LAMC, outstanding debt carried by the agency increased to ETB 540.2 billion as of end-June 2023, from ETB 420.7 billion as of end-June 2022, as additional SOE domestic debt of ETB 94 billion was transferred to LAMC in May 2023 and arrears on interest payments were capitalized.

C. Outlook and Key Assumptions

The DSA builds on the program scenario. The projections assume program approval in July 2024, a full transition to market-determined exchange rate with positive effects on the current account and FDI, as well as a revenue-driven fiscal consolidation with safeguards on pro-poor spending.

8. The near-term outlook is challenging (Text Table 3).

- ***Growth has moderated but has held up overall.*** Average growth has fallen to over 6 percent during 2019/20-2022/23 from over 9 percent per year in the decade to 2018/19 and was 7.2 percent for 2022/23. Favorable rainfall and expansion of irrigated crop-production have supported agricultural output, while double-digit growth in transport, communications and hospitality sectors bolstered service sector growth supported by post-conflict recovery.
    - Growth of 6.1 percent is forecast in 2023/24. Tight macroeconomic policies, FX shortages, lower agricultural output (including due to droughts in some regions), and policy uncertainty constrain economic activity. Over the medium term, the competitiveness and allocative efficiency gains from exchange rate unification (reduction in policy uncertainty, correction of overvaluation, and better FX availability) and stronger policy framework (higher spending financed with domestic revenues and concessional external financing and a stable monetary policy framework with positive real interest rates) will support trend growth of 7.5–8 percent (see Box 1 on baseline growth projections).
    - Growth in 2024/25 is projected at 6.5 percent, with potential uncertainties linked to the transition to market-determined exchange rate offset by improving agricultural conditions and the easement of import shortages. Between 2025/26–2033/34, average real GDP growth is projected at 7.3 percent, slower than historical rates of around 10 percent per annum over the two decades prior to 2019. The long-term projection reflects demographic factors (the median age is below 20 years) and expected productivity gains, including from reforms and economic transformation.
- ***Inflation has been relatively stable at high levels, with disinflation expected to gather pace in the medium term.*** The authorities are adopting an interest-rate based monetary policy framework, with low and stable inflation as the policy objective. Inflation declined moderately in 2023/24. Food price inflation moderated as international food commodity prices eased and a temporary rise in domestic crop inflation passed. Non-food inflation is declining in response to fiscal and monetary tightening including sharp reductions in monetary financing, albeit with a lag. Easing food price inflation lowers the average inflation forecast to 27 percent in 2023/24. The pass-through impact of a move to market-clearing exchange rate on inflation is expected to be limited. This is due to the low share of imports occurring at the official exchange rate in private consumption expenditure and evidence that price formation using the parallel market exchange rate is consistent with international prices. Tightening monetary policy by eliminating monetary financing and moving to positive real interest rates will help contain the second-round impact on inflation. Measures to mitigate the impact of price adjustments of essential imports (fuel, fertilizer, and

medicines) will smooth the impact of exchange rate changes.[9]

- ***The current account deficit is expected to increase in the near term, before narrowing in the medium term.*** The move to market-clearing exchange rate in 2024/25 and international financial support are expected to alleviate FX shortages and help rebuild international reserves from low levels. The current account deficit is expected to rise at first before settling at around 2.0 percent of GDP in 2027/28.
  - Imports of goods are forecast to decline from 10.5 percent of GDP in 2022/23 to 8.2 percent of GDP in 2023/24 due to FX shortages, before increasing to 13.8 percent of GDP in 2024/25 following program approval as increased FX availability results in a decompression of currently suppressed imports. As price and substitution effects weigh more, imports are expected to decline as a proportion of GDP. Imports would react relatively slowly to the exchange rate unification since a significant part of transactions are already completed at the parallel rate, while transactions that are completed at the official rate are for essential goods with relatively inelastic demand. Materialization of the pent-up demand and higher project financing from external creditors would both contribute to the rise in the goods imports-to-GDP ratio.
  - Exports of goods are forecast to decline from 2.2 to 1.7 percent of GDP between 2022/23 and 2023/24, given lower-than-expected coffee and flower exports. Following the move to market-determined exchange rate regime, goods exports are expected to improve over the medium-term and revert to pre-COVID trends. Goods and services exports are assumed to remain around 10 percent of GDP over the medium term (consistent with observed long-term trends), given Ethiopian Airlines strong prospects and expected positive effects from the exchange rate unification.
  - Private transfers (remittances and NGO transfers) are expected to recover to historical levels of about 5 percent of GDP, reacting positively to the ER unification, paired with the removal of current account restrictions, which would reduce uncertainty and costs, incentives for informal transfers, and fears associated with the imposition of restrictions.
- ***Foreign direct investment (FDI) is projected to recover as FX reforms take hold.*** The proceeds from the partial privatization of Ethio Telecom, the auction of the second telecom license as well as potential privatization of 8 sugar factories are assumed to lead to inflows of US$650 million in 2025/26. Moreover, the DSA does not include future telecom investments from private foreign companies, which the authorities estimate could add around US$8 billion in additional foreign investment over the next 10 years. Over the medium term, FDI is expected to settle at around 3.0 percent of GDP, consistent with pre-COVID trends.

[9] The program envisages a move to a market-clearing exchange rate in July 2024, which will contribute to correcting an estimated REER overvaluation of about 52 percent in 2022/23. The REER, based on weighted average CPI of trading partners (including US, EU, China, MENA, and India), is projected unchanged thereafter assuming that the market-determined exchange rate offsets inflation differentials. The change in the real exchange rate in the DSA template is measured as the bilateral real exchange rate against the US using GDP deflator on an annual basis, giving a different result. The US dollar carries only a 6 percent weight in REER.

Box 1. The Federal Democratic Republic of Ethiopia: Baseline Growth Projection

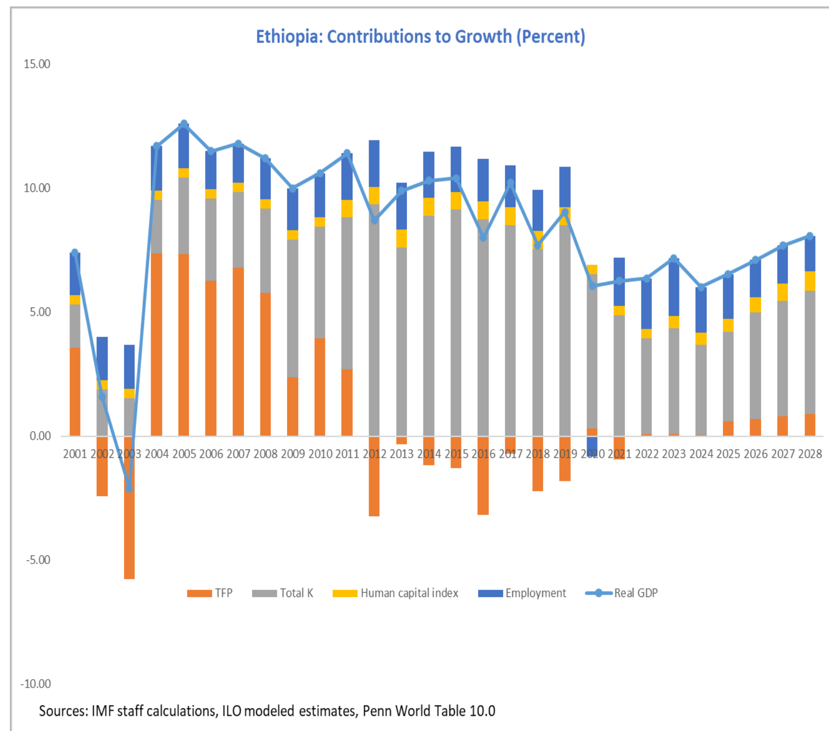
The baseline growth projection reflects ambitious reforms to stimulate private sector-led growth, including a move to market-clearing exchange rate and elimination of financial repression.

The Ethiopian economy was among the fastest growing in the world over the past 15 years before slowing in response to recent shocks. In 2003/04–2010/11, Ethiopia achieved average annual growth rate of 11.4 percent mainly driven by rising productivity. Strong growth continued in 2011/12–2018/19 led by debt-financed public sector capital investment, while productivity growth declined. Growth slowed down in 2019/20–2022/23 with lower contributions from most factors due to a series of shocks including COVID-19, the domestic conflict, drought, and spillover from the war in Ukraine.

Contributions to Growth (annual average, %)					
	Real GDP growth	TFP	Physical Capital	Human Capital	Employment
2003/04-2010/11	11.4	5.3	3.9	0.4	1.7
2011/12-2018/19	9.3	-1.7	8.5	0.7	1.8
2019/20-2022/23	6.5	-0.1	4.8	0.4	1.4

GDP growth is projected to reach around 8 percent over the medium term:

- ***Recovery from the shocks.*** Near-term growth is driven by post-conflict recovery and resilient crop production. However, the rebound is constrained by FX shortages, tighter macro-economic policies, and policy uncertainty.
- ***Growth dividends from reforms.*** Structural, fiscal, and institutional reforms under the program will raise growth potential by improving resource allocation and attracting external financing leading to higher productivity and private investment.
    - A move to a market clearing exchange rate would spur structural transformation through stimulating business investment and eliminating uncertainty on the availability of foreign exchange. FDI and remittances to finance private investment and consumption are expected to increase, along with exports, with upside risks to current conservative projections.
    - Moderate fiscal consolidation, refocus of policy away from SOE-led, debt-financed investment, and elimination of financial repression should enable competitive, private sector-led growth. Reorientation of government expenditure toward investments in education, health, and social protection will help build human capital.
    - Strengthening financial stability mainly through tackling CBE's non-performing lending to SOEs can support resilient economic growth.



Sources: IMF staff calculations, ILO modeled estimates, Penn World Table 10.0

- ***Revenue mobilization will anchor debt sustainability while safeguarding humanitarian and pro-poor spending.*** The general government primary deficit is expected to narrow from 1.1 percent of GDP in 2023/24 to 0.7 percent of GDP in 2027/2028, having already declined from a peak of 3.5 in 2021/22. Consolidation will be driven by tax revenue measures, while pro-poor spending will increase, and capital expenditure will partially recover to meet reconstruction needs.

Text Table 3. The Federal Democratic Republic of Ethiopia: Key Macroeconomic Assumptions

Fiscal year ending June	2023/24	2024/25	2025/26	2026/27	2027/28	Average (2029-2044) 1/
Real GDP Growth (annual percent change)						
Current DSA	6.1	6.5	7.1	7.7	8.0	6.2
2019 Article IV DSA	8.0	7.0	6.6	6.2	6.2	5.6
Current Account Balance (percent of GDP)						
Current DSA	-2.6	-4.3	-3.2	-2.5	-2.0	-2.3
2019 Article IV DSA	-3.4	-3.6	-3.7	-3.8	-3.8	-4.1
Exports of goods and services (percent of GDP)						
Current DSA	5.4	8.9	9.6	10.0	10.4	9.3
2019 Article IV DSA	10.7	11.2	11.2	11.2	11.2	11.7
Exports of goods and services (annual percent change)						
Current DSA	3.9	7.9	15.0	17.3	17.0	9.4
2019 Article IV DSA	9.7	9.2	9.4	9.6	9.6	9.8
Fiscal balance, including grants (percent of GDP)						
Current DSA	-1.7	-2.4	-2.0	-2.0	-2.0	-2.0
2019 Article IV DSA	-1.9	-1.8	-1.8	-2.3	-1.9	-2.0
International reserves (billions of U.S. dollars)						
Current DSA	1.0	2.8	5.1	7.0	10.2	20.6
2019 Article IV DSA	11.2	11.6	13.0	14.5	15.8	27.5
General government revenue (percent of GDP)						
Current DSA	7.4	8.4	9.9	11.0	11.4	12.2
2019 Article IV DSA	14.7	14.8	14.7	14.6	14.6	14.5
Grant element of new external borrowing						
Current DSA	23.3	34.4	39.3	37.2	28.8	51.2
2019 Article IV DSA	49.6	53.1	52.9	52.8	52.7	51.4
Nonconcessional debt disbursements (billions of U.S. dollars)						
Current DSA	2.00	0.05	0.20	0.27	0.30	0.00
2019 Article IV DSA	0.02	0.00	0.00	0.00	0.00	0.00

Source: IMF staff projections.
1/For 2019 Article IV:2028/29-2038/39

9. The main risks to the outlook stem from domestic policy slippages, potential social discontent, security challenges, and a slowdown in global growth. Reform fatigue due to political and social pressures, could lead to delay in or reversal of policy measures. Macroeconomic conditions could threaten social stability through continued shortages or further increases in prices for essential goods, or by an expectations-led inflation-depreciation spiral arising from exchange rate reforms. Recurrent volatility in global commodity prices also poses a risk to the outlook, as do potential delays in the debt restructuring process. Deterioration in the domestic security situation could renew economic disruption and derail international support. Intensifying spillovers from regional conflicts also pose downside risks to the outlook.

There is also upside potential if security conditions continue to improve, strengthening the economic recovery and unlocking investment.

10. The fiscal adjustment is driven by tax policy measures, the recovery of the tax base from recent shocks and by continued restraint of SOE borrowing. The DSA realism tools do not indicate that the projected fiscal adjustment is unrealistic, with the primary balance adjustment below the top quartile of the historical distribution. Furthermore, the risk that the adjustment proves infeasible is mitigated by the specific measures under the program to raise revenues, including (i) the broadening of the excise tax base and switching to a specific excise tax system with higher rates on alcohol, tobacco, and fuels; (ii) removal of VAT exemptions; (iii) introduction of a motor vehicle circulation tax; and (iv) recovery of the tax base from the historical lows reached during the pandemic and conflict. The program envisages a limit on domestic bank borrowing by SOEs to supplement the zero limit on non-concessional external borrowing and reforms to the electricity tariff framework with a view to further reducing the total SOE debt to GDP ratio. Lower investment and a diminished growth contribution from public investment than expected in the previous DSA are mitigated by a pick-up in productivity through more efficient resource allocation as FX rationing and market distortions stemming from the exchange rate ease, and by the increase in spending on education, health, and social safety net (Figures 3 and 4).

11. Program-supported reforms reducing financial repression and exchange rate distortions underpin a consolidation of quasi fiscal activity and increase fiscal transparency. Moving to positive real interest rates and phasing out of mandatory purchase by banks of Treasury and Development Bank of Ethiopia bonds at sub-market interest rates will eliminate subsidized lending to SOEs and government from captive domestic savers. Recapitalizing CBE with government securities enables writing off CBE's claims on LAMC and provisioning of non-performing exposures to SOEs recognizes historic costs of subsidized lending to SOEs on-budget. Eliminating real exchange rate overvaluation lifts the implicit tax on exporters previously obliged to surrender FX at a below market exchange rate as well as the implicit subsidy to fuel and fertilizers which were imported at the favorable official rate. Subsidies are brought on-budget, and the impacts of the reforms managed through targeted cash transfers to vulnerable groups.

12. This DSA makes the following assumptions on external and domestic financing and debt servicing:

- New debt projections add to debt outstanding as of end-June 2023. All bilateral sovereign deposits at NBE including the recent deposits from a non-OCC country are categorized as debt, as these deposits have been used to meet BOP needs, and in line with the treatment in the past. No contracting or guaranteeing of new non-concessional external loans is assumed during the duration of the arrangement, with one exception: the authorities have requested an exemption from the zero-limit on non-concessional borrowing for the macro-critical Koysha Hydroelectric Dam project (US$950 million).[10] The ECF includes a present value-

[10] The authorities could not mobilize concessional financing to finalize the Koysha dam project despite sustained efforts. The project is critical for generating export revenues, rural electrification, and meeting climate change policy goals and is already two-thirds complete.

based indicative target on overall external borrowing that is consistent with the authorities' borrowing plan and debt sustainability (text table 4).

- The overall IDA project financing envelope is expected to reach about US$1.8 billion by 2027/28. Most of IDA envelope is assumed to be in loans, consistent with the LIC-DSF guidance that regular credit terms on IDA lending should be assumed in all years for which grant finance has not already been committed.
- Forecasts incorporate reprofiling of debt payment of US$2.5 billion due to all the official bilateral creditors in CY2023 and CY2024, broadly following the term sheet of the standstill.
- A residual financing gap of US$10.7 billion during the program period is assumed. Reserve adequacy would be brought to about 3.5 months of import coverage by the end of the program. The Fund would contribute about a third of resources to fill the gap. Besides IMF financing, the remaining gap is assumed to be financed equally by budget support from multilateral and bilateral donors and debt relief from the OCC, proxied by the issuance of a NPV neutral bond. No assumption on the parameters and modality of the needed debt treatment is made.

Text Table 4. The Federal Democratic Republic of Ethiopia: External Borrowing Plan for FY2024/25 1/

(Programmed Contracted Debt)

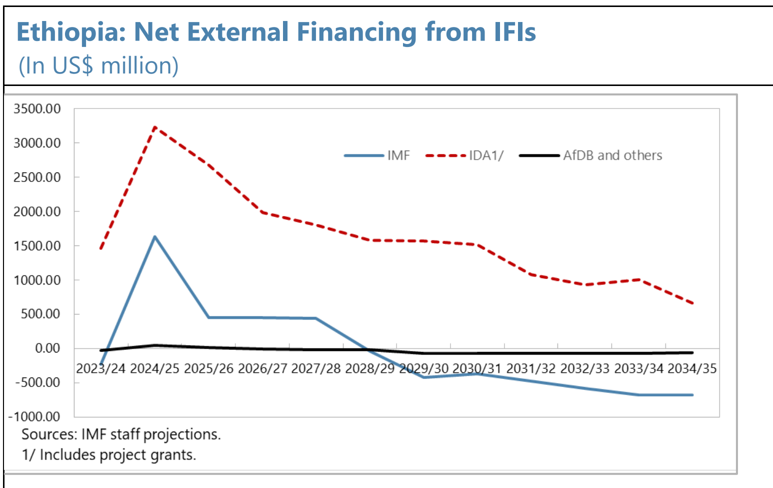
PPG external debt	Volume of new debt in 2024/25		PV of new debt in 2024/25 (program purposes)	
	USD million 1/	Percent	USD million 1/	Percent
By sources of debt financing	**4,900**	**100**	**2,856**	**100**
Concessional debt, of which 2/	**3,950**	**81**	**1,906**	**67**
Multilateral debt	3,600	73	1,683	59
Bilateral debt	350	7	224	8
Non-concessional debt, of which 2/	**950**	**19**	**950**	**33**
Semi-concessional 3/	-	-	-	-
Commercial terms 4/	950	19	950	33

1/ Contracting and guaranteeing of new debt. The present value of debt is calculated using the terms of individual loans and applying the 5 percent program discount rate
2/ Debt with a grant element that exceeds a minimum threshold. This minimum is typically 35 percent, but could be established at a higher level.
3/ Debt with a positive grant element which does not meet the minimum grant element.
4/ Debt without a positive grant element. For commercial debt, the present value would be defined as the nominal/face value.

- For domestic debt, the program balances phasing out of non-market-based financing of the public sector and maintaining fiscal sustainability:
  - The authorities issued 870 billion Birr of 10-year government securities to write off all CBE claims on LAMC (580 billion birr) and fully provision nonperforming SOE exposures (240 billion birr) and bring CBE's capital adequacy ratio to the regulatory minimum**.** This has no material impact on domestic debt level since CBE's claims on LAMC and SOEs were already part of domestic PPG debt in the DSA.

- Monetary financing of fiscal deficits will be eliminated from FY2024/25.
- The mandatory purchase of 5-year treasury bonds at sub-market interest rates by commercial banks will be phased out by end-June 2025, with an intention to develop the market for longer-dated government securities.
- The requirement that financial institutions purchase DBE bonds will be removed before the fifth review of the Fund program.
- A voluntary exchange of the current stock of T-bills held by Public Servants Social Security Agency and the Private Organizations Employees' Social Security Administration for 10-year securities was conducted. The exchange provides debt service relief to the Treasury and an instrument that better matches the pension funds' asset and liability durations.

Ethiopia: Net External Financing from IFIs
(In US$ million)



Sources: IMF staff projections.
1/ Includes project grants.

- In future, domestic financing needs will be covered by market-oriented instruments. The government's net domestic financing is projected to shift predominantly to T-bills with market-determined interest rates, while SOEs are assumed to issue medium to long-term bonds. Interest rates will rise to positive levels in real terms over the medium term, consistent with the phasing out of financial repression under an interest rate-based monetary policy framework.

D. Country Classification

13. Ethiopia's debt carrying capacity is weak, due fundamentally to the decline in FX reserves. The Composite Indicator (CI)—based on the IMF World Economic Outlook projections in April 2024 and the 2022 World Bank's Country Policy and Institutional Assessment (CPIA) score that was published in July 2023—stands at 2.31, which corresponds to a weak signal. Ethiopia's debt carrying capacity was downgraded to "weak" in October 2022 after two consecutive weak signals driven by low FX reserves and a slight decline in CPIA.

E. External Debt Sustainability Analysis

Baseline

14. Public and publicly guaranteed (PPG) external debt is expected to decline over the projection period, but three indicators consistently breach their indicative thresholds. The debt service-to-revenue ratio and the two exports-linked external debt ratios present protracted breaches,

reflecting two main factors: (i) high and bunched debt service from SOE investment projects and repayment of the US$1 billion Eurobond in December 2024; and (ii) the low level of exports. Finally, the PV of debt-to GDP ratio remains well below its indicative threshold for the entire projection period (Figure 1).

Standardized Stress Tests

15. The standard stress tests highlight vulnerabilities to export shocks. Adverse shocks to exports would exacerbate external debt servicing pressures and difficulties in financing external and domestic needs (Figure 1). In the case of the two exports related indicators that consistently breach the thresholds, the breaches become larger. Implementation of FX reforms, building FX reserves and materialization of upside risks to exports from a better-than-expected response to reforms or the impact of faster global growth, would help strengthen external debt sustainability. The debt service-to-revenue ratio experiences larger and persistent breaches under a one-time exchange rate depreciation shock, which points to risks of devoting significant amount of revenue to external debt service at the expense of cutting priority spending under a sharp depreciation scenario.

Text Table 5. The Federal Democratic Republic of Ethiopia: Calculation of the CI Index

Components	Coefficients (A)	10-year average values (B)	CI Score components (A*B) = (C)	Contribution of components
CPIA	0.385	3.369	1.30	56%
Real growth rate (in percent)	2.719	6.808	0.19	8%
Import coverage of reserves (in percent)	4.052	10.340	0.42	18%
Import coverage of reserves^2 (in percent)	-3.990	1.069	-0.04	-2%
Remittances (in percent)	2.022	3.105	0.06	3%
World economic growth (in percent)	13.520	2.909	0.39	17%
CI Score			2.31	100%
CI rating			Weak	

New framework	Cut-off values	
Weak	CI < 2.69	
Medium	2.69 ≤ CI ≤	3.05
Strong	CI > 3.05	

APPLICABLE	
EXTERNAL debt burden thresholds	
PV of debt in % of	
Exports	140
GDP	30
Debt service in % of	
Exports	10
Revenue	14

APPLICABLE	
TOTAL public debt benchmark	
PV of total public debt in percent of GDP	35

16. Indicators of market financing risks remain elevated. The EMBI spread is at distressed levels, well beyond the LIC-DSF benchmark of 570 basis points. The relatively contained external financing needs lead to a moderate rating for market financing risks under the LIC DSF. A return to market access is

unrealistic at current spreads and is neither foreseen by the authorities nor necessary to meet external financing needs. Market financing risks are currently assessed as moderate per the mechanical risk rating under the LIC DSF (below the LIC DSF benchmark of 14 percent of GDP for signaling market-financing pressures) (Figure 5). Gradual consolidation of public sector including SOEs, along with deepening of financial markets through the opening of banking sector to foreign investors and the growth of pension funds, can mitigate domestic financing pressures.

F. Public Debt Sustainability Analysis

Baseline

17. The present value of overall public debt/GDP ratio is projected to steadily decline, with breaches only in 2024/25. As public sector consolidation takes hold and the external debt situation improves with continued restraint on borrowing, the PV of public debt/GDP ratio will stay below the applicable threshold throughout the projection period (with a one-off breach discounted). Gross financing needs are projected to average around 6 percent of GDP during the program period through 2027/28 (below the LIC-DSF benchmark of 14 percent of GDP) and stabilize at around 9 percent of GDP by 2033/34. This mainly reflects a lower gross financing need in the near term due to the voluntary exchange of T-bills for longer-term securities with the pension funds. This need is expected to revert to normal levels, alongside an anticipated increase in the real cost of new domestic borrowing over the medium to long term. Should downside risks of public sector balances lead to larger fiscal needs in the near term, the authorities' commitment to consolidation during the Fund-supported program would help contain the risks to public debt. The PV of public debt-to-revenue also remains on a downward trend.

Standardized Stress Tests

18. Overall public debt is susceptible to the materialization of contingent liabilities. The PV debt/GDP ratio rises to 46 percent in 2024/25 under combined contingent liabilities shock but remains below the threshold from 2027/28 onwards.

19. Risks from Ethiopian Airlines appear negligible in the near term The airline, which is excluded from the DSA, adjusted well to the COVID shock with support from a strong balance sheet at the beginning of the crisis and active measures, including changes in business focus to cargo. This operational shift allowed the company to achieve record profitability. The authorities have conveyed that Ethiopian Airlines does not intend to seek government support.

G. Risk rating and Vulnerabilities

20. Ethiopia's debt is assessed to be unsustainable, mainly due to protracted breaches of exports-related external debt indicators. Following a missed Eurobond interest payment in December 2023, the country is in debt distress.

21. Successful completion of debt treatment and implementation of the reform agenda would restore debt sustainability and allow exit from debt distress. Ethiopia's DCC is classified as weak,

because of low reserves and recent modest declines in the CPIA. In relation to the debt thresholds for weak DCC, there are protracted breaches of the two exports-related indicators and of the debt service to revenue ratio, indicating both liquidity and solvency pressures. The PV of external debt to GDP ratio remains below the threshold for the entire projection period. All the external debt risk indicators exceed their thresholds for a protracted period under the most extreme shock scenario, with stress tests indicating vulnerabilities to export and depreciation shocks. The combination of prudent macroeconomic policies, including a move to market clearing exchange rate and export diversification, fiscal and debt conditionality, improved SOE governance, and the debt treatment would all contribute towards reducing debt vulnerabilities. A drawn-out debt restructuring process would however slow the reduction in debt vulnerabilities.

22. An external debt treatment is needed for Ethiopia to close financing gaps over the program period and to help achieve a moderate risk of debt distress by the end of the requested Fund-supported program. To close the BOP financing gap, required debt relief during the program period (2024/25–2027/28) amounts to about US$3.5 billion. To bring Ethiopia's risk of debt distress to "moderate" over the medium term, debt relief would need to bring the three binding external debt burden indicators below the thresholds (140 for PV of debt-to-exports ratio, 10 for debt service-to-exports ratio and 14 for debt service to revenue) by the end of the program period and over the DSA projection horizon.

23. The OCC provided financing assurances for a debt treatment consistent with the IMF-supported program. The authorities have also taken important steps towards discussing debt restructuring on comparable terms with private creditors.

H. Authorities' Views

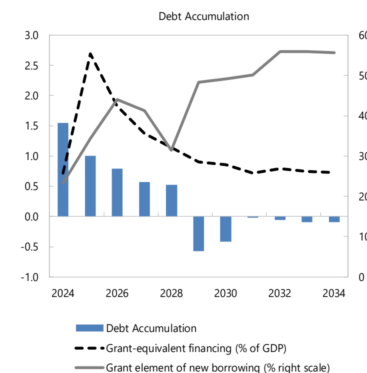
24. The authorities broadly agreed with the overall assessment of the country's debt sustainability. Debt sustainability is expected to be restored through a debt restructuring, development partner support, and the reforms contemplated under the Fund-supported program. The authorities are committed to further improve debt management.

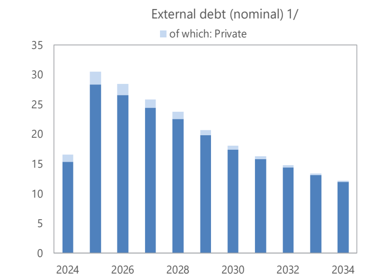
Table 1. The Federal Democratic Republic of Ethiopia: External Debt Sustainability Framework, 2021–2043

(In percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 8/	
	2021	2022	2023	2024	2025	2026	2027	2028	2029	2034	2043	Historical	Projections
External debt (nominal) 1/	31.4	25.8	19.5	16.6	30.5	28.4	25.8	23.7	20.7	12.2	6.1	28.9	20.0
of which: public and publicly guaranteed (PPG)	29.0	24.0	18.1	15.4	28.3	26.6	24.4	22.6	19.8	12.0	6.0	26.4	19.1
Change in external debt	0.0	-5.6	-6.3	-2.9	13.9	-2.1	-2.6	-2.1	-3.1	-1.2	-0.5		
Identified net debt-creating flows	-1.7	-2.4	-5.1	0.1	0.0	-2.1	-2.3	-2.8	-2.7	-1.1	-0.4	-0.6	-1.6
Non-interest current account deficit	2.3	3.6	2.5	2.4	3.7	2.6	1.9	1.5	1.4	2.1	2.2	5.5	2.2
Deficit in balance of goods and services	9.1	10.1	7.4	5.8	9.7	8.9	8.2	7.7	7.3	6.6	5.3	13.6	7.6
Exports	7.6	8.2	6.6	5.4	8.9	9.6	10.0	10.4	9.9	9.3	9.4		
Imports	16.7	18.3	14.0	11.2	18.6	18.5	18.2	18.1	17.2	15.9	14.7		
Net current transfers (negative = inflow)	-6.7	-6.5	-4.8	-3.4	-6.1	-6.3	-6.3	-6.2	-5.9	-4.5	-3.1	-8.1	-5.4
of which: official	-1.2	-0.9	-0.7	-0.5	-1.0	-1.1	-1.0	-0.9	-0.9	-0.8	-0.8		
Other current account flows (negative = net inflow)	0.0	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net FDI (negative = inflow)	-3.6	-2.6	-2.1	-1.6	-2.7	-3.2	-2.9	-3.0	-3.0	-2.6	-2.3	-3.4	-2.8
Endogenous debt dynamics 2/	-0.5	-3.4	-5.5	-0.7	-1.0	-1.4	-1.4	-1.3	-1.2	-0.6	-0.3		
Contribution from nominal interest rate	0.5	0.5	0.3	0.2	0.6	0.6	0.6	0.6	0.5	0.2	0.1		
Contribution from real GDP growth	-1.9	-1.8	-1.4	-0.9	-1.7	-2.0	-2.0	-1.8	-1.6	-0.8	-0.3		
Contribution from price and exchange rate changes	0.9	-2.1	-4.4	...	...	...	...	...	...	...	...		
Residual 3/	1.8	-3.2	-1.3	-3.0	14.0	0.0	-0.3	0.7	-0.3	-0.1	0.0	0.1	0.9
of which: exceptional financing	0.2	0.2	0.2	0.0	3.1	1.4	1.0	1.3	0.0	-0.2	0.0		
Sustainability indicators													
PV of PPG external debt-to-GDP ratio	...	...	13.4	11.8	19.6	19.1	17.4	16.0	13.8	7.8	3.7		
PV of PPG external debt-to-exports ratio	...	...	203.9	218.9	220.3	199.3	174.9	154.0	138.6	84.0	39.4		
PPG debt service-to-exports ratio	18.2	14.7	11.6	8.4	24.7	17.4	16.1	17.7	17.4	8.5	3.3		
PPG debt service-to-revenue ratio	13.6	15.0	9.8	6.1	26.3	16.9	14.7	16.3	15.1	6.7	2.5		
Gross external financing need (Million of U.S. dollars)	587.7	3170.6	2239.5	3068.6	4801.3	2012.3	1609.8	1150.3	764.3	1302.6	1358.7		
Key macroeconomic assumptions													
Real GDP growth (in percent)	6.3	6.4	7.2	6.1	6.5	7.1	7.7	8.0	7.8	6.8	5.5	8.2	7.2
GDP deflator in US dollar terms (change in percent)	-2.7	7.1	20.5	20.2	-38.7	-0.4	4.5	4.1	3.9	3.2	3.4	4.8	1.0
Effective interest rate (percent) 4/	1.7	1.7	1.6	1.2	2.5	2.2	2.3	2.5	2.3	1.6	1.0	2.0	2.0
Growth of exports of G&S (US dollar terms, in percent)	10.9	22.8	3.3	3.9	7.9	15.0	17.3	17.0	7.1	11.4	9.0	6.4	10.4
Growth of imports of G&S (US dollar terms, in percent)	2.3	24.9	-1.4	1.9	8.7	5.9	10.6	11.8	6.8	8.7	7.1	5.8	8.2
Grant element of new public sector borrowing (in percent)	...	...	...	23.3	34.4	44.0	41.2	31.5	48.3	55.6	50.4	...	44.5
Government revenues (excluding grants, in percent of GDP)	10.2	8.1	7.9	7.3	8.3	9.8	10.8	11.2	11.4	11.8	12.4	11.8	10.7
Aid flows (in Million of US dollars) 5/	879.3	549.6	602.9	1861.8	3695.1	3632.7	3035.2	2789.2	2802.4	3563.2	5234.6		
Grant-equivalent financing (in percent of GDP) 6/	...	...	...	0.7	2.7	1.8	1.4	1.1	0.9	0.7	0.5	...	1.1
Grant-equivalent financing (in percent of external financing) 6/	...	...	...	38.6	51.2	53.0	52.2	42.7	64.4	70.6	75.9	...	58.7
Memorandum items:													
PV of external debt 7/	...	...	14.8	13.0	21.7	20.9	18.8	17.1	14.7	8.0	3.8		
In percent of exports	...	...	225.1	241.1	244.9	218.5	189.0	165.1	147.6	86.2	40.1		
Total external debt service-to-exports ratio	23.1	18.7	14.4	12.0	28.7	21.2	19.4	20.6	19.7	9.0	3.6		
PV of PPG external debt (in Million of US dollars)			22007.4	24540.2	26636.2	27719.3	28544.1	29403.1	28342.0	26748.2	28525.6		
(PVt-PVt-1)/GDPt-1 (in percent)				1.5	1.0	0.8	0.6	0.5	-0.6	-0.1	0.0		
Non-interest current account deficit that stabilizes debt ratio	2.3	9.2	8.9	5.3	-10.3	4.7	4.5	3.6	4.4	3.3	2.7		

Definition of external/domestic debt	Residency-based
Is there a material difference between the two criteria?	No





Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt. Presented on fiscal year basis (e.g., 2020 referes to fiscal year ending in June 2020).

2/ Derived as [r - g - ρ(1+g) + Ɛα (1+r)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, ρ = growth rate of GDP deflator in U.S. dollar terms, Ɛ=nominal appreciation of the local currency, and α= share of local currency-denominated external debt in total external debt.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Current-year interest payments divided by previous period debt stock.

5/ Defined as grants, concessional loans, and debt relief.

6/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

7/ Assumes that PV of private sector debt is equivalent to its face value.

8/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

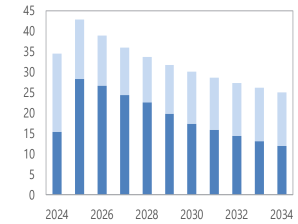
Table 2. The Federal Democratic Republic of Ethiopia: Public Sector Debt Sustainability Framework, 2021–2043

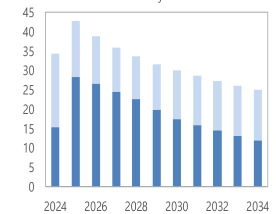
(In percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 6/	
	2021	2022	2023	2024	2025	2026	2027	2028	2029	2034	2043	Historical	Projections
Public sector debt 1/	56.1	48.9	40.2	34.4	42.8	38.9	35.9	33.7	31.7	25.1	20.6	52.4	32.2
of which: external debt	29.0	24.0	18.1	15.4	28.3	26.6	24.4	22.6	19.8	12.0	6.0	26.4	19.1
Change in public sector debt	0.0	-7.2	-8.7	-5.8	8.4	-4.0	-3.0	-2.2	-2.0	-1.1	-0.3		
Identified debt-creating flows	-4.6	-8.0	-10.5	-4.1	-4.4	-3.4	-2.3	-1.9	-1.5	-0.7	-0.2	-4.6	-2.0
Primary deficit	2.2	3.8	2.3	1.4	0.8	1.1	1.0	0.9	0.9	0.4	0.1	2.6	0.8
Revenue and grants	11.0	8.5	8.2	7.7	9.6	10.3	11.3	11.6	11.9	12.2	12.7	12.6	11.2
of which: grants	0.8	0.4	0.4	0.4	1.4	0.6	0.5	0.4	0.4	0.3	0.3		
Primary (noninterest) expenditure	13.2	12.4	10.5	9.1	10.4	11.4	12.3	12.6	12.8	12.5	12.8	15.2	12.0
Automatic debt dynamics	-6.0	-11.9	-12.7	-6.3	-5.2	-4.0	-3.3	-2.8	-2.4	-1.1	-0.3		
Contribution from interest rate/growth differential	-8.1	-10.7	-8.9	-6.3	-5.2	-4.0	-3.3	-2.8	-2.4	-1.1	-0.3		
of which: contribution from average real interest rate	-4.8	-7.3	-5.6	-4.0	-3.1	-1.2	-0.5	-0.2	0.0	0.6	0.8		
of which: contribution from real GDP growth	-3.3	-3.4	-3.3	-2.3	-2.1	-2.8	-2.8	-2.7	-2.4	-1.7	-1.1		
Contribution from real exchange rate depreciation	2.1	-1.2	-3.9	...	...	...	...	...	...	...	...		
Other identified debt-creating flows	-0.8	0.0	0.0	0.8	0.0	-0.4	0.0	0.0	0.0	0.0	0.0	-0.2	0.0
Privatization receipts (negative)	-0.8	0.0	0.0	0.0	0.0	-0.4	0.0	0.0	0.0	0.0	0.0		
Recognition of contingent liabilities (e.g., bank recapitalization)	0.0	0.0	0.0	0.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Debt relief (HIPC and other)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Other debt creating or reducing flow (liquid financial asset)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Residual	4.6	0.8	1.8	-1.6	12.8	-0.6	-0.6	-0.3	-0.5	-0.4	-0.1	4.1	0.6
Sustainability indicators													
PV of public debt-to-GDP ratio 2/	...	...	35.9	31.1	36.4	32.2	29.5	27.6	26.0	21.0	18.4		
PV of public debt-to-revenue and grants ratio	...	...	436.6	403.0	378.3	312.7	261.1	236.7	218.8	173.1	144.3		
Debt service-to-revenue and grants ratio 3/	21.9	47.9	60.4	51.1	56.4	35.1	32.5	44.2	49.9	70.0	52.6		
Gross financing need 4/	3.8	7.9	7.2	6.1	6.2	4.3	4.7	6.1	6.8	8.9	6.8		
Key macroeconomic and fiscal assumptions													
Real GDP growth (in percent)	6.3	6.4	7.2	6.1	6.5	7.1	7.7	8.0	7.8	6.8	5.5	8.2	7.2
Average nominal interest rate on external debt (in percent)	1.8	1.8	1.6	1.0	2.4	2.3	2.3	2.4	2.3	1.6	1.0	2.0	2.0
Average real interest rate on domestic debt (in percent)	-15.8	-23.6	-22.2	-18.2	-17.7	-9.3	-5.6	-2.7	-0.5	4.9	6.1	-10.8	-3.3
Real exchange rate depreciation (in percent, + indicates depreciation)	7.8	-4.5	-17.6	...	...	...	...	...	...	...	...	-1.6	...
Inflation rate (GDP deflator, in percent)	21.1	33.3	32.2	26.2	27.4	16.9	13.0	10.8	9.8	7.6	6.4	16.8	13.1
Growth of real primary spending (deflated by GDP deflator, in percent)	-7.6	-0.7	-9.1	-8.0	21.9	17.5	16.0	10.3	9.6	6.1	5.6	3.0	9.2
Primary deficit that stabilizes the debt-to-GDP ratio 5/	2.2	11.1	11.0	7.1	-7.6	5.1	4.0	3.2	2.9	1.5	0.4	8.1	2.2
PV of contingent liabilities (not included in public sector debt)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		

Definition of external/domestic debt	**Residency-based**
Is there a material difference between the two criteria?	**No**

Public sector debt 1/





Sources: Country authorities; and staff estimates and projections.

1/ Coverage of debt: The central, state, and local governments, central bank, government-guaranteed debt, non-guaranteed SOE debt . Definition of external debt is Residency-based. Presented on fiscal year basis (e.g., 2020 referes to fiscal year ending in June 2020).

2/ The underlying PV of external debt-to-GDP ratio under the public DSA differs from the external DSA with the size of differences depending on exchange rates projections.

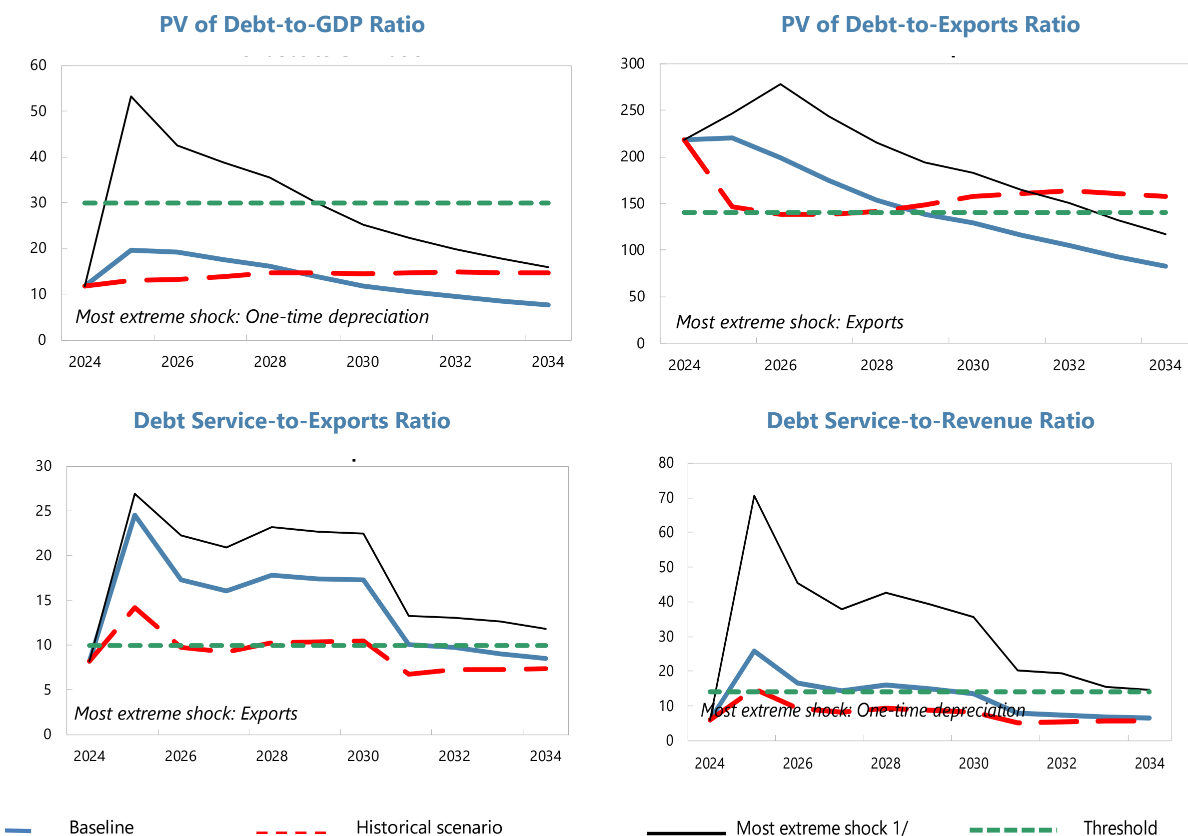
3/ Debt service is defined as the sum of interest and amortization of medium and long-term, and short-term debt.

4/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period and other debt creating/reducing flows.

5/ Defined as a primary deficit minus a change in the public debt-to-GDP ratio ((-): a primary surplus), which would stabilizes the debt ratio only in the year in question.

6/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

Figure 1. The Federal Democratic Republic of Ethiopia: Indicators of Public and Publicly Guaranteed External Debt



Customization of Default Settings	Size	Interactions
Tailored Stress		
Combined CL	Yes	
Natural disaster	n.a.	n.a.
Commodity price	n.a.	n.a.
Market financing	No	No

Note: "Yes" indicates any change to the size or interactions of the default settings for the stress tests. "n.a." indicates that the stress test does not apply.

Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG MLT debt	100%	
Terms of marginal debt		
Avg. nominal interest rate on new borrowing in USD	1.3%	1.3%
USD Discount rate	5.0%	5.0%
Avg. maturity (incl. grace period)	30	30
Avg. grace period	6	6

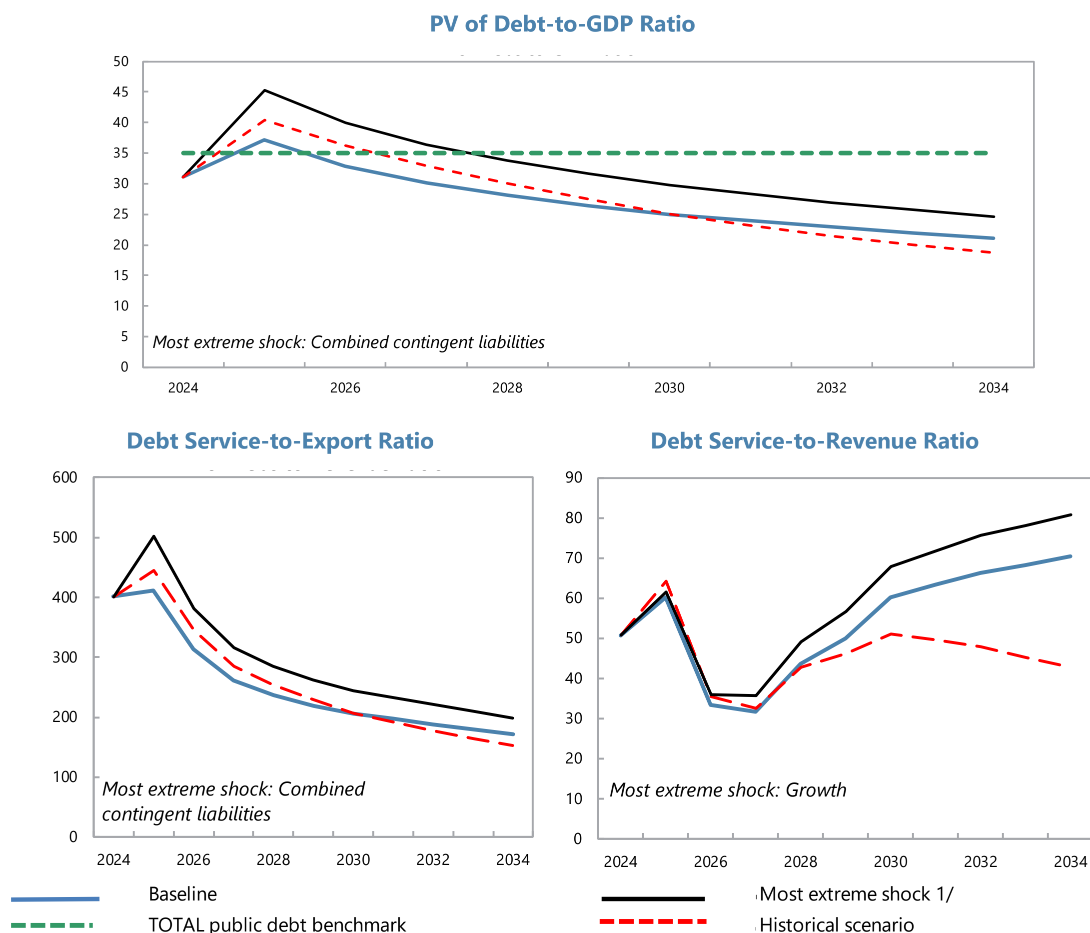
* Note: All the additional financing needs generated by the shocks under the stress tests are assumed to be covered by PPG external MLT debt in the external DSA. Default terms of marginal debt are based on baseline 10-year projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2034.

Source: IMF staff projections based on LIC DSF.

Figure 2. The Federal Democratic Republic of Ethiopia: Indicators of Public Debt

(In percent)



Borrowing assumptions on additional financing needs resulting from the stress tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	25%	30%
Domestic medium and long-term	25%	25%
Domestic short-term	50%	45%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	1.2%	1.2%
Avg. maturity (incl. grace period)	31	31
Avg. grace period	6	6
Domestic MLT debt		
Avg. real interest rate on new borrowing	0.7%	0.7%
Avg. maturity (incl. grace period)	7	7
Avg. grace period	2	2
Domestic short-term debt		
Avg. real interest rate	1.4%	1.4%

* Note: The public DSA allows for domestic financing to cover the additional financing needs generated by the shocks under the stress tests in the public DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2034. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most exterme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

Table 3. The Federal Democratic Republic of Ethiopia: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2024–2034

(In percent)

	Projections 1/										
	2024	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**	**2031**	**2032**	**2033**	**2034**
PV of debt-to GDP ratio											
Baseline	12	20	19	17	16	14	12	11	10	9	8
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2024-2034 2/	12	13	13	14	15	15	15	15	15	15	15
B. Bound Tests											
B1. Real GDP growth	12	20	20	19	17	15	13	11	10	9	8
B2. Primary balance	12	20	21	19	18	16	14	13	11	10	9
B3. Exports	12	20	21	19	17	15	13	12	11	10	9
B4. Other flows 3/	12	21	22	20	19	16	14	13	12	11	9
B5. Depreciation	12	**53**	**42**	**39**	**35**	30	26	23	20	18	16
B6. Combination of B1-B5	12	18	19	18	16	14	12	11	10	9	8
C. Tailored Tests											
C1. Combined contingent liabilities	12	21	21	20	19	16	15	13	12	11	10
C2. Natural disaster	...	...	...	...	...	...	...	...	...	...	...
C3. Commodity price	...	...	...	...	...	...	...	...	...	...	...
C4. Market Financing	12	24	23	21	19	17	14	13	12	10	9
Threshold	30	30	30	30	30	30	30	30	30	30	30
PV of debt-to-exports ratio											
Baseline	**219**	**220**	**199**	**175**	**154**	139	131	118	107	95	84
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2024-2034 2/	**219**	**146**	139	139	**142**	**148**	**159**	**162**	**165**	**162**	**159**
B. Bound Tests											
B1. Real GDP growth	**219**	**220**	**199**	**175**	**154**	139	131	118	107	95	84
B2. Primary balance	**219**	**225**	**219**	**195**	**173**	**158**	**151**	137	126	113	101
B3. Exports	**219**	**247**	**278**	**244**	**215**	**194**	**185**	**167**	**152**	134	119
B4. Other flows 3/	**219**	**239**	**234**	**205**	**181**	**165**	**158**	**143**	130	115	102
B5. Depreciation	**219**	**220**	**163**	**143**	125	111	103	91	82	72	64
B6. Combination of B1-B5	**219**	**240**	**219**	**227**	**200**	**182**	**173**	**156**	**143**	126	112
C. Tailored Tests											
C1. Combined contingent liabilities	**219**	**238**	**224**	**200**	**179**	**164**	**159**	**146**	135	122	110
C2. Natural disaster	...	...	...	...	...	...	...	...	...	...	...
C3. Commodity price	...	...	...	...	...	...	...	...	...	...	...
C4. Market Financing	**219**	**220**	**199**	**175**	**154**	139	131	117	107	94	84
Threshold	140	140	140	140	140	140	140	140	140	140	140
Debt service-to-exports ratio											
Baseline	8.4	**24.7**	**17.4**	**16.1**	**17.7**	**17.4**	**15.5**	**10.1**	9.8	9.1	8.5
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2024-2034 2/	8	**14**	10	9	**10**	**10**	10	7	7	7	7
B. Bound Tests											
B1. Real GDP growth	8	**25**	**17**	**16**	**18**	**17**	**15**	**10**	10	9	8
B2. Primary balance	8	**25**	**18**	**17**	**19**	**18**	**16**	**11**	**11**	**10**	9
B3. Exports	8	**27**	**22**	**21**	**23**	**23**	**20**	**13**	**13**	**13**	**12**
B4. Other flows 3/	8	**25**	**18**	**17**	**18**	**18**	**16**	**11**	**11**	**11**	10
B5. Depreciation	8	**25**	**17**	**15**	**17**	**17**	**15**	10	9	7	7
B6. Combination of B1-B5	8	**26**	**21**	**19**	**21**	**21**	**19**	**12**	**12**	**12**	**11**
C. Tailored Tests											
C1. Combined contingent liabilities	8	**25**	**18**	**17**	**18**	**18**	**16**	**11**	**10**	10	9
C2. Natural disaster	...	...	...	...	...	...	...	...	...	...	...
C3. Commodity price	...	...	...	...	...	...	...	...	...	...	...
C4. Market Financing	8	**25**	**17**	**16**	**18**	**18**	**16**	**11**	**10**	9	8
Threshold	10	10	10	10	10	10	10	10	10	10	10
Debt service-to-revenue ratio											
Baseline	6	**26**	**17**	**15**	**16**	**15**	12	8	8	7	7
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2024-2034 2/	6	**15**	10	8	10	9	8	5	6	6	6
B. Bound Tests											
B1. Real GDP growth	6	**27**	**18**	**16**	**17**	**16**	13	8	8	7	7
B2. Primary balance	6	**26**	**17**	**16**	**17**	**16**	13	9	8	8	7
B3. Exports	6	**26**	**17**	**15**	**17**	**15**	13	8	8	8	7
B4. Other flows 3/	6	**26**	**17**	**15**	**17**	**16**	13	8	8	8	8
B5. Depreciation	6	**72**	**46**	**39**	**43**	**40**	**32**	**21**	**20**	**16**	**15**
B6. Combination of B1-B5	6	**24**	**16**	14	**15**	**14**	12	8	7	7	7
C. Tailored Tests											
C1. Combined contingent liabilities	6	**26**	**17**	**15**	**17**	**16**	13	8	8	7	7
C2. Natural disaster	...	...	...	...	...	...	...	...	...	...	...
C3. Commodity price	...	...	...	...	...	...	...	...	...	...	...
C4. Market Financing	6	**26**	**17**	**15**	**17**	**15**	13	9	8	7	6
Threshold	14	14	14	14	14	14	14	14	14	14	14
Memorandum item:											
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	43.6	43.6	43.6	43.6	43.6	43.6	43.6	43.6	43.6	43.6	**43.6**

Sources: Country authorities; and staff estimates and projections.
1/ A bold value indicates a breach of the threshold.
2/ Variables include real GDP growth, GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
3/ Includes official and private transfers and FDI.

Table 4. The Federal Democratic Republic of Ethiopia: Sensitivity Analysis for Key Indicators of Public Debt, 2024/2034

(In percent)

	Projections 1/										
	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
PV of Debt-to-GDP Ratio											
Baseline	31	**36**	32	30	28	26	25	24	23	22	21
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2024-2034 2/	31	**40**	**36**	33	30	27	25	23	21	20	19
B. Bound Tests											
B1. Real GDP growth	31	**38**	34	32	30	29	28	27	27	26	25
B2. Primary balance	31	**39**	**37**	34	31	30	28	27	26	24	23
B3. Exports	31	**37**	34	31	29	27	26	25	24	23	22
B4. Other flows 3/	31	**38**	**36**	33	30	29	27	26	25	24	23
B5. Depreciation	31	32	27	24	22	20	18	17	16	14	13
B6. Combination of B1-B5	31	**36**	33	30	28	26	25	23	22	21	20
C. Tailored Tests											
C1. Combined contingent liabilities	31	**45**	**39**	**36**	33	31	30	28	27	26	24
C2. Natural disaster	...	...	...	...	...	...	...	...	...	...	...
C3. Commodity price	...	...	...	...	...	...	...	...	...	...	...
C4. Market Financing	31	**36**	32	30	28	26	25	24	23	22	21
TOTAL public debt benchmark	35	35	35	35	35	35	35	35	35	35	35
PV of Debt-to-Revenue Ratio											
Baseline	403	378	313	261	237	219	207	199	190	181	173
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2024-2034 2/	403	412	347	288	256	231	210	195	180	167	156
B. Bound Tests											
B1. Real GDP growth	403	388	333	283	260	244	234	229	222	214	208
B2. Primary balance	403	402	360	299	270	249	234	224	213	202	192
B3. Exports	403	383	329	275	249	230	217	209	199	189	180
B4. Other flows 3/	403	398	346	289	262	241	228	219	208	197	187
B5. Depreciation	403	333	262	214	188	168	153	142	130	118	107
B6. Combination of B1-B5	403	379	326	269	241	220	206	195	184	173	163
C. Tailored Tests											
C1. Combined contingent liabilities	403	462	381	317	285	262	246	235	223	211	201
C2. Natural disaster	...	...	...	...	...	...	...	...	...	...	...
C3. Commodity price	...	...	...	...	...	...	...	...	...	...	...
C4. Market Financing	403	378	313	261	237	219	207	199	190	181	173
Debt Service-to-Revenue Ratio											
Baseline	51	56	35	33	44	50	58	63	66	68	70
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2024-2034 2/	51	60	37	34	43	46	50	49	48	45	43
B. Bound Tests											
B1. Real GDP growth	51	58	38	37	50	57	66	72	75	78	81
B2. Primary balance	51	56	48	49	54	57	65	69	71	73	74
B3. Exports	51	56	35	33	44	50	59	63	66	68	71
B4. Other flows 3/	51	56	35	33	45	50	59	63	67	69	71
B5. Depreciation	51	47	31	24	39	43	51	55	57	59	61
B6. Combination of B1-B5	51	54	42	37	45	50	57	61	64	66	67
C. Tailored Tests											
C1. Combined contingent liabilities	51	56	78	53	58	61	68	72	74	74	75
C2. Natural disaster	...	...	...	...	...	...	...	...	...	...	...
C3. Commodity price	...	...	...	...	...	...	...	...	...	...	...
C4. Market Financing	51	56	35	33	44	50	59	64	66	68	70

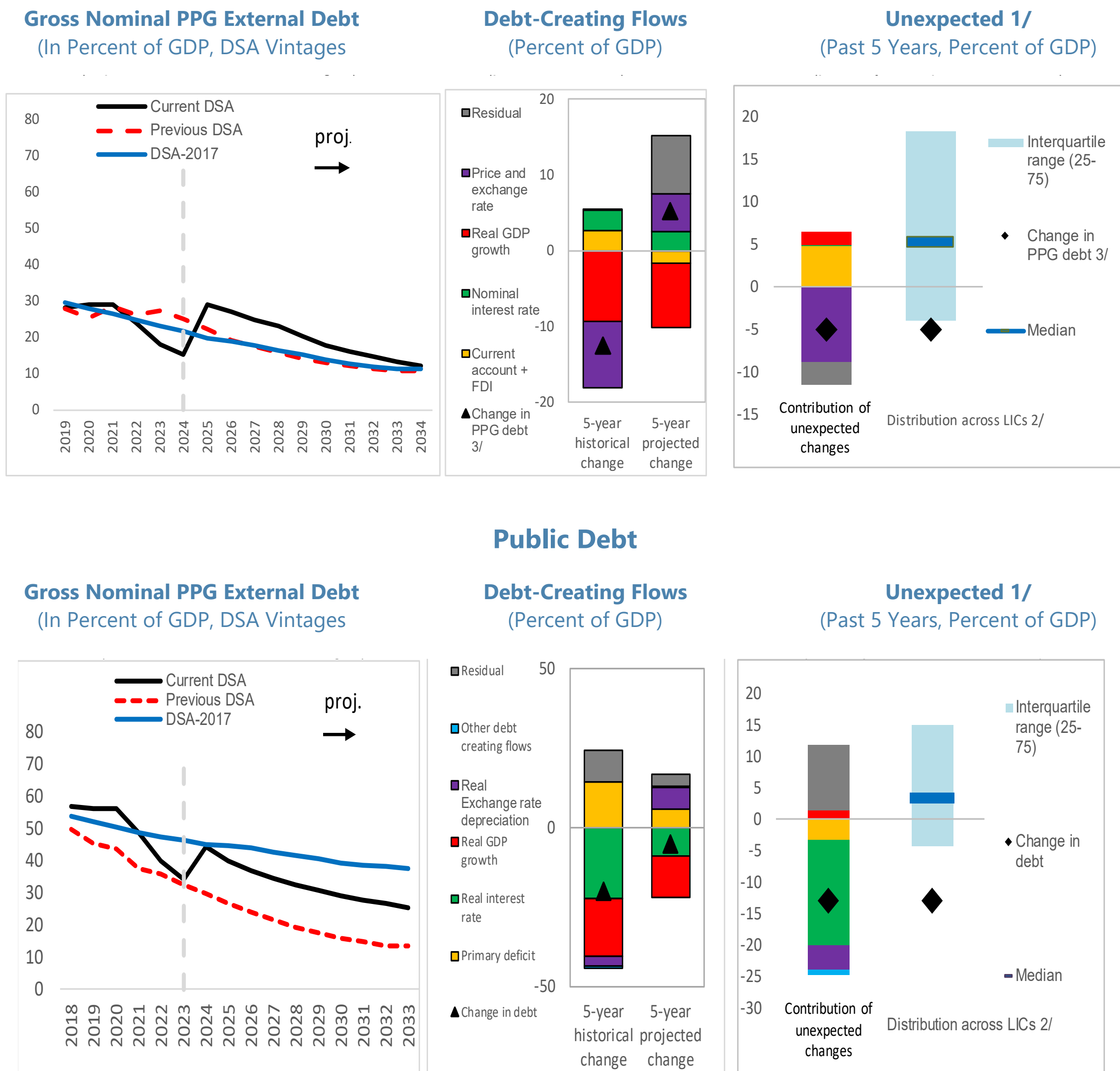
Sources: Country authorities; and staff estimates and projections.

1/ A bold value indicates a breach of the benchmark.

2/ Variables include real GDP growth, GDP deflator and primary deficit in percent of GDP.

3/ Includes official and private transfers and FDI.

Figure 3. The Federal Democratic Republic of Ethiopia: Drivers of Debt Dynamics—Baseline Scenario, External Debt



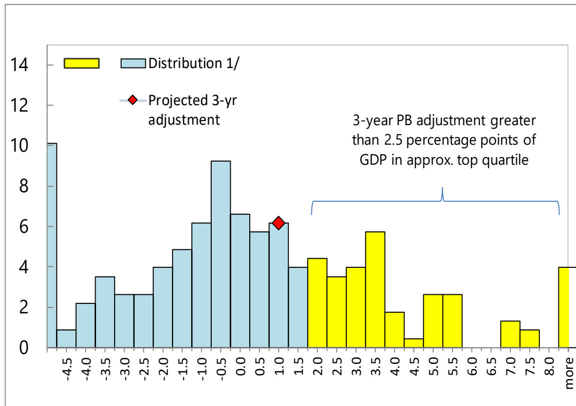
1/ Difference between anticipated and actual contributions on debt ratios.

2/ Distribution across LICs for which LIC DSAs were produced.

3/ Given the relatively low private external debt for average low-income countries, a ppt change in PPG external debt should be largely explained by the drivers of the external debt dynamics equation.

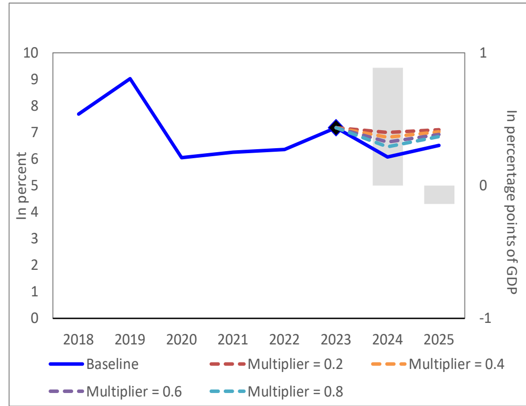
Figure 4. The Federal Democratic Republic of Ethiopia: Realism Tools

3-Year Adjustment in Primary Balance
(Percentage Points of GDP)



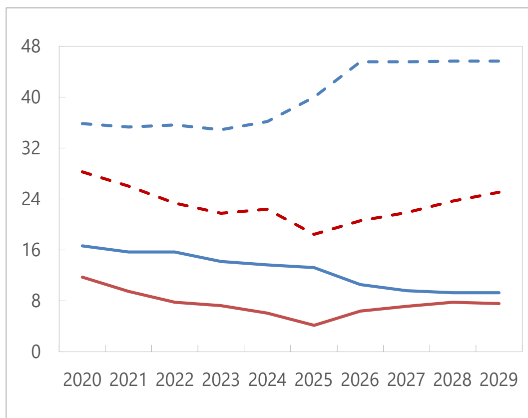
1/ Data cover Fund-supported programs for LICs (excluding emergency financing) approved since 1990. The size of 3-year adjustment from program inception is found on the horizontal axis; the percent of sample is found on the vertical axis.

Fiscal Adjustment and Possible Growth Paths 1/



1/ Bars refer to annual projected fiscal adjustment (right-hand side scale) and lines show possible real GDP growth paths under different fiscal multipliers (left-hand side scale).

Public and Private Investment Rates
(Percent of GDP)



Contribution to Real GDP Growth
(Percent 5-Year Average)

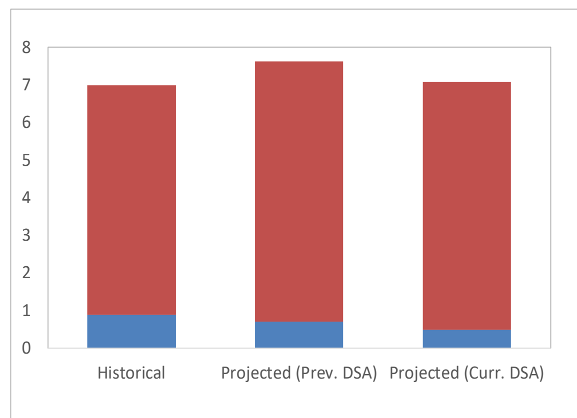
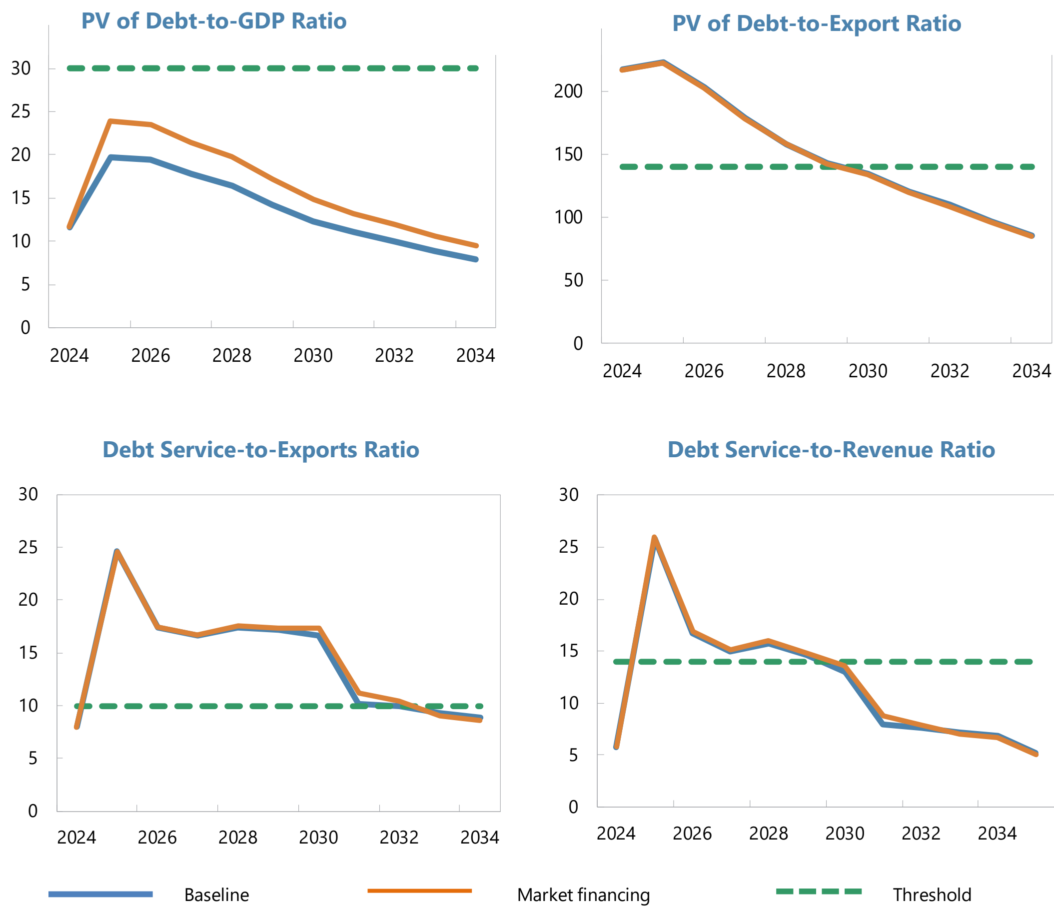


Figure 5. The Federal Democratic Republic of Ethiopia: Market Financing Risk Indicators

	GFN 1/	EMBI 2/
Benchmarks	14	570
Values	7	4612
Breach of benchmark	No	Yes
Potential heightened liquidity needs	Moderate	

1/ Maximum gross financing needs (GFN) over 3-year baseline projection horizon.
2/ EMBI spreads correspond as of January 18, 2024.



Sources: Country authorities; and staff estimates and projections.

INTERNATIONAL MONETARY FUND

THE FEDERAL DEMOCRATIC REPUBLIC OF ETHIOPIA

REQUEST FOR AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—SUPPLEMENTARY INFORMATION

July 29, 2024

Prepared By African Department.

This supplement provides an update on recent program and economic developments since the issuance of the staff report on July 15, 2024. This update does not alter the thrust of the staff appraisal.

1. **Prior actions.** The authorities met the remaining prior action for approval of the Extended Credit Facility arrangement related to liberalization of the foreign exchange market. On July 28, 2024, Prime Minister Abiy announced the adoption of market-determined exchange rate, and today the NBE published a directive announcing that Authorized Dealers can buy and sell foreign exchange from their clients and among themselves at freely negotiated rates, allowing market participants to determine a market-clearing exchange rate for current account transactions, and eliminating current account controls.

2. **Recent economic developments.** Inflation declined to 19.9 percent year-over-year at end-June 2024, declining somewhat faster than expected, driven by easing food price inflation. Efforts to modernize the monetary policy framework are progressing. On July 11, 2024, the NBE announced the introduction of the National Bank Rate at 15 percent, as the monetary policy rate, and has successfully conducted two open market operations (OMOs) since. There has been broad participation, with 16 and 21 of 32 banks bidding in the first and second auctions, respectively, for a collective amount of 58 billion Birr. The NBE indicated that it will regularly conduct OMOs every two weeks. In implementing the recapitalization of Commercial Bank of Ethiopia, the authorities raised the total recapitalization amount to 900 billion Birr, and modified the terms including lengthening maturities, similarly with respect to the debt swap undertaken with pension funds. Neither change has significant macroeconomic or debt sustainability implications. The authorities raised fuel prices upwards by 5 percent on July 10, 2024, in line with their commitment to close the price gap resulting from foreign exchange reform (MEFP 35).

Statement by the Executive Director, Mr. Willie Nakunyada, and the Advisor of the Executive Director, Mr. Mawek Tesfaye Mengistu on The Federal Democratic Republic of Ethiopia July 29, 2024

I. Introduction

1. Our Ethiopian authorities acknowledge the constructive engagement with staff and appreciate the Fund's unwavering support. They also extend their gratitude to their creditors for providing the debt service standstill alongside financing assurances. Special mention goes to China and France, for successfully co-chairing the Official Creditors Committee (OCC).

2. Ethiopia achieved significant economic and social development over the past two decades, but recently, macroeconomic conditions have deteriorated due to several factors. These include the legacy debt-financed public investments, limited external financing, as well as shocks from the COVID-19 pandemic, domestic conflicts, adverse climate events, and recurrent locust infestations. Consequently, macroeconomic imbalances have emerged, leading to protracted external and fiscal financing gaps, persistent pressure on reserves and the exchange rate, and an unsustainable debt. **In this context, the authorities are seeking Fund support under a 48-month Extended Credit Facility (ECF) arrangement amounting to SDR 2,555.95 million (850 percent of quota), as well as request for temporary approval of exchange restrictions and multiple currency practices.** They consider support under the ECF arrangement, as important to help address underlying BoP challenges, catalyze additional donor support, and anchor efforts to achieve the objectives of the Home-Grown Economic Reform Plan (HGER 2.0 – 2024–2026). Under the HGER 2.0, the authorities attach prominence on advancing macro-financial, sectoral, and structural reforms to address remaining vulnerabilities, restore macroeconomic stability, and unlock the country's enormous growth potential.

3. To demonstrate their strong commitment, the authorities have completed all seven Prior Actions. Specifically, they have undertaken significant reforms, including adoption of a market-clearing exchange rate regime, removal of current account restrictions, and transitioning to an interest rate-based system monetary policy framework. Measures aimed to increase tax revenues, enhance financial sector stability, and reduce financial repression have also been implemented. To further underline their reform credentials, the authorities have persevered with reforms aimed to tighten monetary and fiscal policies, promote private sector development, rationalize fuel subsidies, liberalize the telecom sector, and advance state-owned enterprise (SOEs) reforms. They expect their reform outcomes to extend well beyond Ethiopia, contributing to regional stability and fostering robust growth, noting Ethiopia's status as the second most populous country in Africa and the third largest economy in Sub-Saharan Africa.

4. The authorities attach a high premium on lasting peace and stability to support inclusive and robust growth. To this end, they have been actively implementing the Cessation of Hostilities Agreement reached in November 2022 to end the conflict in the Tigray region, resulting in the formation of an interim regional administration and the restoration of humanitarian and basic

services. Significant efforts are currently underway to facilitate returnees of Internally Displaced Population (IDP). Additionally, with the support of the World Bank, a multi-donor trust fund has been established to mobilize resources for recovery and reconstruction efforts. Furthermore, the Ethiopian National Dialogue Commission has commenced its work to facilitate broad-based dialogue on key national issues.

II. Recent Economic Developments and Outlook

5. Real GDP growth is expected to remain robust at 6.1 percent in 2023/24, despite some moderation from 7.2 percent growth in 2022/23. The strong growth performance has been driven by the resilient services sector that has benefitted from restored peace and strong agricultural production in the context of favorable rainfall and supporting government initiatives to expand irrigated crop production. Looking forward, real GDP growth is expected to expand on average by 8.0 percent per annum in the medium term, bolstered by policy measures under the ECF arrangement that should help entrench macroeconomic stability and support far-reaching structural reforms. Nevertheless, the outlook remains subject to significant downside risks, including spillovers from regional conflicts, and volatility in global commodity prices. The authorities' strong program ownership, proven track record of reform implementation, and robust social support integrated into the reform agenda, will be expected to help mitigate these risks.

6. Meanwhile, inflation declined from its peak of 37 percent in May 2022 to 19.9 percent in June 2024. The marked decline in inflation reflects tight fiscal and monetary policies, as well as supply-side improvements. In the short term, the re-alignment of the exchange rate could generate inflationary pressures, while a gradual disinflation towards single digits is expected by the end of the program period. The current account[1] deficit is projected to widen to 4.5 percent of GDP in 2024/25 from 2.8 percent in 2023/24, reflecting elevated imports driven by pent-up demand occasioned by foreign exchange shortages.

III. Fiscal Policy and Debt Management

7. Fiscal consolidation efforts continue to rank high on the authorities' agenda to strengthen fiscal and debt sustainability, while preserving priority spending. To this end, the authorities' strategy centers on ambitious revenue mobilization, comprehensive debt treatment, enhancing pro-poor spending, and improving the efficiency of public investments. Concurrent efforts to enhance fiscal transparency while managing potential fiscal risks will be prioritized. Effectively, the consolidation efforts are expected to be much higher considering off-budget and quasi-fiscal operations. That said, the authorities are committed to implementing contingency measures to achieve program objectives in case fiscal risks materialize, including further reducing non-essential expenditures. As the financial market develops, the authorities plan to increase reliance on domestic sources for deficit financing while committing to refrain from monetary financing and contracting of non-concessional external borrowing as well as promoting financial liberalization.

[1] Excludes prospective donor financing and/or exceptional financing.

8. The authorities are committed to increasing the tax-to-GDP ratio by 4.0 percentage points over the program period. Their medium-term tax reforms will be guided by the National Medium-Term Revenue Strategy (NMTRS) which is nearing final adoption. In this connection, they recently took decisive actions including introducing an excise stamp regime, amending the VAT proclamation, and rolling out a new Real Estate Tax Proclamation, expected to boost the tax-to-GDP ratio by 1.0 percentage point in FY2024/25 alone. Further, the authorities plan to sustain tax policy reforms and rationalize exemptions while widening the tax base. To this end, they will pursue initiatives such as the minimum alternative tax, reforming the presumptive tax regime, and implementing a motor vehicle circulation tax. They also plan to integrate the fuel excise and VAT regime into the budget revenue while exploring a new avenue for increased tax revenue such as agricultural sector taxation and further rationalization of exemptions. These reforms prioritize fairness, equity, and compliance while facilitating WTO accession and regional trade bloc integration. In addition, the authorities plan to enhance tax administration, focusing on taxpayer registration, e-filing, and tax audits, alongside custom tax administration reforms. In this vein, they plan to introduce the Integrated Tax Administration System and leverage the findings of the TADAT Assessment planned for 2025 to further enhance tax administration.

9. To mitigate the effects of exchange rate reforms on the most vulnerable, the authorities, in collaboration with development partners, have prepared a comprehensive fiscal package. Towards this end, they have requested to earmark a portion of the ECF disbursement for direct budget support. For FY2024/25, they have allocated a fiscal package amounting to 1.5 percent of GDP, which includes expanding and increasing allocations to their Productive Social Safety Net Programs (PSNP) to provide targeted cash-transfers to the most vulnerable. Additionally, temporary subsidies on fuel, selected food items, medicine, and fertilizer will lessen the pain of adjustment on the most vulnerable, with plans for gradual removal of these subsidies. The authorities also plan to increase public servants' salaries in FY2024/25 to partially offset the erosion of purchasing power caused by persistent inflation. Looking ahead to the medium term, the authorities will prioritize pro-poor spending and higher-priority public investments. They will draw upon recent PIMA/C-PIMA recommendations to enhance the efficiency of public investment, maximize value for money through comprehensive project appraisal, selection, maintenance, prioritization, and budgeting. Furthermore, they plan to leverage Public-Private Partnerships (PPP) to address significant infrastructure investment needs while mitigating potential fiscal risks and enhancing fiscal transparency.

10. The authorities are committed to restoring debt sustainability with the aim of achieving a moderate level of debt distress by the end of the program period. Total Public and Publicly Guaranteed (PPG) debt declined from 56.1 percent of GDP in 2020/21 to 34.4 percent of GDP in 2023/24, reflecting restrain on SOEs' borrowing and robust GDP growth. Despite severe forex shortages, the authorities have prioritized honoring their debt service commitments, before reaching a debt service standstill agreement with official bilateral creditors in November 2023. In addition, they withheld a USD 33 million Eurobond coupon payment to commercial creditors in December 2023 to ensure comparability of treatment. Since they applied for official debt treatment under the G-20 Common Framework (CF) in February 2021, the Ethiopian authorities are effectively engaging with their bilateral official and commercial creditors including by appointing legal and financial advisors.

The authorities are committed to continued close creditor engagement to secure timely debt treatment consistent with the ECF program parameters. They aim to reach a Memorandum of Understanding (MOUs) on the terms of debt treatment with official bilateral creditors and to make tangible progress with their commercial creditors by the time of the second ECF review.

11. The authorities reaffirm their strong commitment to refrain from contracting non-concessional external borrowing. They requested an exemption from the zero-limit on new non-concessional borrowing for the Koysha Hydroelectric Dam project, noting its critical role in the country's development, particularly as two-thirds of the project is already completed, and no concessional financing has been secured. Concurrently, the authorities are focusing on strengthening governance and transparency of SOEs, with plans to develop a comprehensive debt management strategy. They are also strengthening the governance and transparency of SOEs through centralized oversight led by the Public Enterprise Holding and Administration Agency (PEHAA) and Ethiopian Investment Holding (EIH). Significant progress has also been achieved under their oversight, including the preparation of audited financial statements of SOEs in compliance with IFRS. Additionally, the authorities have committed to implementing targeted reform measures for individual SOEs to enhance the viability of their operations. These reforms encompass revised tariff setting methodologies in the electricity sector, improvements in infrastructure management through increased private sector participation in railway, and accelerated privatization of sugar factories.

IV. Monetary, Exchange Rate, and Financial Sector Policies

12. The NBE remains committed to a tight monetary policy stance aimed at restoring price stability, considering inflationary pressures stemming from transition to the new exchange rate regime. The Bank will closely monitor inflation developments and stands ready to further raise the policy rate to stabilize expectations, foster confidence in the new regime, and achieve price stability. To complement the newly implemented interest-based framework and considering the liquidity in the system, the Bank may deploy direct policy instruments such as increasing reserve requirements and imposing caps on credit growth for commercial banks, in order to achieve price stability. At the same time, they are strengthening their communication strategy to guide expectations.

13. The NBE embarked on far-reaching reform measures aimed at modernizing the monetary policy framework and strengthening the Bank's institutional standing as articulated in its three-year strategic plan (2023-2026) launched in December 2023. As part of this reform, the Council of Ministers approved the amended NBE proclamation and submitted it for Parliamentary consideration. The amended proclamation encompasses changes to the NBE's mandate to accord primacy to price stability, improved governance, transparency, strengthened capital position, as well as enhanced autonomy. Additionally, the central bank recently announced its transition to an interest-rate-based monetary policy framework, launched biweekly Open Market Operations (OMO), and revitalized the functioning of the interbank money market. An initial policy rate of 15 percent, with 3 percent range around standing deposit and lending facilities was also announced in July 2024. These significant changes in the monetary policy framework are crucial to anchor inflation and exchange rate expectations under the newly introduced market-clearing exchange rate regime. That said, the NBE

reaffirms its strong commitment to implementing the outstanding Fund's 2020 Safeguards Assessment recommendations including publication of audited financial statements and rotation of external auditors.

14. The authorities have announced extensive reforms to liberalize the foreign exchange market, to allow market participants to freely determine the market-clearing exchange rate. This bold move is well synchronized with a tight monetary policy and a well-calibrated fiscal package designed to anchor the exchange rate and ensure stability. The realignment of the exchange rate is expected to eliminate speculative behavior occasioned by longstanding distortions and promote export competitiveness. At the same time, the NBE conducted a comprehensive review of its FX regulations and implemented a consolidated directive that eliminates current account restrictions. These revisions include discontinuation of the FX allocation mechanism, elimination of import reference price systems, and removal of the 50 percent security deposit requirement when queuing for foreign exchange for import payments. Additionally, foreign exchange surrender requirements to NBE were abolished and replaced by surrender to commercial banks to ensure availability of liquidity in the foreign exchange market.

15. The operational guidelines for foreign exchange transactions have been revised, and a code of conduct for such transactions has been established. Furthermore, a real-time data collecting system has been established to calculate the benchmark exchange rate. The NBE will also enhance monitoring of daily net open positions (NOP) of banks to ensure effective management of foreign exchange risks and support liquidity in the inter-bank market. The NBE has adopted a foreign exchange intervention strategy that permits, but does not obligate, the Bank to intervene only to smoothen disorderly movements in the exchange rate, without committing to any specific exchange rate or trajectory. The authorities requested temporary approval of an exchange transactions commission solely aimed at generating income for NBE, inadvertently giving rise to a multiple currency practice. They plan to eliminate this practice by the end of the program period. That said, the authorities committed to building up of international reserves to 3.5 months of prospective import coverage by the end of the program period.

16. Ensuring financial sector stability remains central to the authorities' reform agenda. To address vulnerabilities in the systemically important public-owned Commercial Bank of Ethiopia (CBE), the authorities have implemented a series of reform measures, supported by technical and financial assistance from the World Bank including under their Financial Sector Strengthening Project. A substantial capital injection of Birr 900 billion has bolstered the bank's financial position, addressing legacy issues related to SOEs. Concurrent reforms are underway to transform the bank into a commercially viable entity, by enhancing governance and risk management practices. Similarly, comprehensive reforms at the public-owned Development Bank of Ethiopia (DBE), including governance enhancements, a revised business model, and capital injections, have significantly improved its financial footing. Building on these achievements, the authorities are focused on developing a sustainable funding model for the DBE, leveraging upcoming capital market opportunities. More generally, the authorities are strengthening the legal framework to enhance competitiveness, notably through amendments to the Banking Business Proclamation aimed at

opening the sector to foreign competition. Recently, the NBE introduced directives aimed at fortifying corporate governance within the banking system to bolster overall stability and soundness. Additionally, they are seeking IMF TA support to strengthen their AML/CFT framework and combat financial crimes.

V. Structural Reforms

17. The authorities attach great importance to complementary structural reforms to help unleash the country's enormous growth potential. In pursuit of this goal, various reforms have been implemented to enhance private sector participation by improving public service delivery, upgrading the legal and regulatory framework, and fostering business integration with regional and global trading blocs. The authorities have revised the Commercial Code, which had been in effect since 1960, to align the country's legal framework with international best practices and current economic needs. Decisive steps have also been taken to open sectors that were previously closed to both domestic and foreign investors. The telecoms sector has already been opened to foreign competition, with licenses granted to a foreign telecom company, while efforts towards partial privatization of Ethio-telecom and granting a second private sector telecom license are currently underway. Additionally, the banking sector, retail and wholesale markets, residential, and logistics sectors are being opened to foreign competition.

18. Addressing sector-specific bottlenecks to enhance productivity, exploit opportunities, and create employment within an improved trade and investment environment ranks among the key priorities of the authorities' reform agenda. To this end, the authorities identified a range of reform measures to enhance productivity in the agricultural sector, including improved land use and administration frameworks, expanded irrigation, strengthened integration with the manufacturing sector, and enhanced access to tailored financial services. Further, they embarked on initiatives to expand production of key crops, such as wheat, through large-scale irrigation-based production aimed to attain food self-sufficiency. They are also making significant efforts to enhance productivity in manufacturing, mining, tourism, and Information Communication Technology (ICT). The authorities also launched a National Artisanal and Small-Scale Mining Strategy aimed at formalizing and supporting the informal sector, which faces challenges related to limited scale-processing technology and low market access. Additionally, they have implemented an Industrial Parks (IP) development program aimed at addressing issues related to land access, infrastructure, logistics, and customs processes to attract investments in the manufacturing sector. The authorities are also working to unlock the abundant tourism potential by enhancing the attractiveness of tourist sites and improving tourist-related infrastructure.

19. Recognizing the central role of digitalization within the economic transformation agenda, the authorities have adopted Digital Ethiopia 2025, a national digital strategy, and implemented various initiatives. The liberalization of the telecom sector, substantial investments in power, an expanding financial sector, and a youthful demographic, coupled with effective government policies, have significantly propelled digital expansion. Presently, they are expediting the rollout of digital national IDs and enhance digital public service delivery through e-government initiatives, geared to boost

financial inclusion and streamline public services. They are undertaking sweeping financial sector reforms to leverage digital technologies to enhance coverage and usage of financial services to promote inclusion and improve living standards. At the same time, the amended legal framework to allow third parties, such as telecom companies, to provide financial service, has spurred electronic payments and rapid e-commerce growth. In parallel, the authorities, are finalizing preparatory work to operationalize the Ethiopian Securities Exchange (ESX), the first formal securities exchange in the country, which will further modernize the financial sector and enhance private sector investment.

20. Recognizing the country's susceptibility to recurrent climate shocks, the climate agenda assumes great importance on the authorities' reform agenda. Their ten-year development plan (2021-2030) set building a climate-resilient green economy as one of its key strategic pillars. Their Climate Resilient Green Economy (CRGE) strategy outlines specific measures to enhance adaptation and mitigation policies consistent with their Nationally Determined Contributions (NDC) targets. Under their NDC, they have set an ambitious agenda to reduce emissions by 68.8 percent by 2030, reforest and restore 15 million hectares, and implement adaptive measures across various sectors. Over the past five years, the authorities have driven their Green Legacy Initiatives through a nationwide movement towards planting seedlings, aiming to build a green and climate-resilient economy. They have also completed the IMF's C-PIMA and the World Bank's CCDR, which they will use to guide their macro-fiscal policies as they further integrate climate considerations into their project selection and implementation. Once the ECF arrangement gathers pace, Fund support under the RST would be critical to unlock additional climate financing and support on-going climate efforts.

VI. Conclusion

21. The Ethiopian authorities are committed to the objectives of the ECF arrangement, which are well-aligned with the objectives of the HGER 2.0. They are determined to pursue far-reaching and coordinated package of prudent economic reform measures and addressing structural bottlenecks to ensure durable, green, and inclusive growth. Specifically, they are committed to removing distortions in the foreign exchange market, modernizing the monetary policy framework, ensuring financial sector stability, increasing fiscal revenue, accelerating SOE reforms, and advancing the climate agenda. They highly value the Fund's support, which they consider as indispensable to the success of their reform agenda. As such, they look forward to Executive Directors' support in approval of their request for an ECF arrangement, which is expected to catalyze additional donor support. They also rely on their creditors and development partner to provide timely debt treatment and necessary financial and technical support.